



ANNIVERSARY  
**EPRA** 20<sup>TH</sup>  
EUROPEAN PUBLIC  
REAL ESTATE ASSOCIATION

GLOBAL  
REIT SURVEY

# EPRA Global REIT Survey 2019

A comparison of the major REIT  
regimes around the world.

2019

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As EPRA marks its 20<sup>th</sup> anniversary, it is encouraging to look at how far the listed real estate sector has come over the past two decades.

While there was only one REIT regime in Europe in 1999, today 14 European countries have introduced the legislation, with a few more in the pipeline. Portugal is the latest addition to the club, following the introduction of the so-called SIGI regime earlier this year. A boost for the Iberian and European property markets as an increasing number of countries recognise the public benefit to incentivise real estate investment through public markets.

Today, the EPRA Global REIT Survey covers now around 40 countries across the globe, exploring in detail their history, developments and recent trends. It is thanks to the experts in various advisory firms that this publication is possible. I would like to thank all the authors for their time and commitment as well as the EPRA public affairs team for the coordination of what is our Association's flagship publication.

**Dominique  
Moerenhout**

**EPRA CEO**

## EUROPE

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### FLAGS LINKED TO CHAPTER



Belgium



Italy



Bulgaria



Lithuania



Finland



Luxembourg



France



Netherlands



Germany



Portugal



Greece



Spain



Hungary



United Kingdom



Ireland



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GLOBAL  
REIT SURVEY

EUROPE

Belgium

BE-REIT

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction

	Enacted year	Citation	REIT type
<i>SICAFI (pro memorie)</i>	1995	<ul style="list-style-type: none"> <li>- Royal Decree of December 07, 2010</li> <li>- Law of April 19, 2014</li> <li>- Other tax laws</li> </ul>	Corporate type
	2014	<ul style="list-style-type: none"> <li>- Law of May 12, 2014 as modified by the Law of October 22, 2017 (together the 'BE-REIT Law')</li> <li>- Royal Decree of July 13, 2014 as modified by Royal Decree of April 23, 2018 (together the 'BE-REIT Decree')</li> <li>- Other tax laws</li> </ul>	Corporate type

Under the current Belgian REIT regime, an undertaking investing in real estate can either take the form of (i) a SICAFI/Vastgoedbevak (société d'investissement en immobilier à capital fixe/vastgoedbeleggingsvennootschap met vast kapitaal), (ii) a SIR/GVV (société immobilière réglementée/gereguleerde vastgoedvennootschap) commonly named **BE-REIT**, an FIIS/GVBF (fonds d'investissement immobilier spécialisé/gespecialiseerde vastgoedbeleggingsfonds) or (iv) stay unregulated (meaning that only the laws applicable to companies in general, as set forth in the Companies Code will apply). Due to their status of collective investment undertaking, SICAFI/Vastgoedbevak and FIIS/GVBF are subject to additional obligations deriving from the AIFM Law<sup>1</sup>.

SICAFI/Vastgoedbevak and BE-REIT are public real estate funds.

As an alternative to maintaining the attractiveness and competitiveness of Belgium, the possibility to take the form of a BE-REIT has been introduced by the BE-REIT Law (as further implemented by the BE-REIT Decree) to allow undertakings investing in real estate that wish to opt for a regulated status (and thus benefit from a preferential tax regime) to avoid the burden of compliance with the Belgian AIFM Law.

An important difference between the SICAFI/Vastgoedbevak and the BE-REIT is, indeed, that the latter is not an AIF, i.e. an entity that 'raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors'. Such a difference is clearly reflected in Article 4 of the BE-REIT Law. Pursuant to such article, the activities of a BE-REIT may only consist of (a) placing, directly or through a company in which it participates in accordance with the law and its implementing regulations, immovable property at the disposal of users, (b) if applicable, possessing 'immovable property'<sup>2</sup> as mentioned in Article 2, 5° vi) to xi) of the BE-REIT Law within the limits of Article 7, b) of that same law<sup>3</sup> and (c) participate in infrastructure projects as further defined by

1 i.e. the Law of April 19, 2014 on alternative collective investment undertakings and their managers.

2 The BE-REIT Law defines what constitutes "immovable property". Immovable property is:

(i) real estate and rights in rem on real estate, with the exclusion of real estate of the following nature: forestry, agriculture or mining industry;  
(ii) shares with voting rights in real estate companies subject to participation threshold;  
(iii) option rights on real estate;  
(iv) shares in BE-REITs and in institutional BE-REIT subject to participation threshold;  
(v) rights arising out of contracts pursuant to which the BE-REIT leases one or more goods or is granted analogous rights of use;  
(vi) shares in public SICAFIs;  
(vii) units of foreign collective investment undertakings investing in real estate and registered on the Belgian FSMA list of foreign AIFs;  
(viii) units of collective investment undertakings investing in real estate, established in the EEA and subject to an equivalent control;  
(ix) shares issued by companies (i) with legal personality; (ii) governed by the law of another EEA member state; (iii) the shares of which are admitted to trading on a regulated market and/or are subject to a regime of prudential supervision; (iv) the main activity of which consists of the acquisition or establishment of immovable property in anticipation of placing such immovable property to the disposal of users, or the direct or indirect possession of participations in companies with a similar activity; and (v) that are exempted from taxes on the revenues arising out of the profit that results from the activity mentioned under (iv) above, provided certain legal obligations are complied with, and that are at least obliged to distribute part of their revenues among their shareholders (i.e. "Real Estate Investment Trusts" or REITs);  
(x) real estate certificates;  
(xi) shares of FIIS / GVBF.

3 The fair value of those investments cannot exceed 20% of the consolidated asset of the BE-REIT.

the legislation. The BE-REIT must thus mainly engage in an operational activity instead of an investment activity. The BE-REIT does therefore not follow a defined investment policy but has a business strategy based on creating long term value (instead of engaging in buying in order to sell within the framework of a defined investment policy). To that extent, Article 4 of the BE-REIT Law requires the BE-REIT to (a) exercise its activities itself, (b) maintain direct relationships with its clients and suppliers and (c) have, for the purpose of exercising its activities as described above, operational teams at its disposal that make up an important part of its work force. The fact that the BE-REIT engages in an operational/commercial activity, also entails that, contrary to what is the case for the SICAFI/Vastgoedbevak, the BE-REIT is not exclusively managed in the interest of the shareholders, but must take into account the overall interest of the company.

The BE-REIT Law also provides for the possibility of an institutional BE-REIT (société immobilière réglementée institutionnelle/institutionele gereguleerde vastgoedvennootschap), the shareholders of which qualify as 'eligible investors'. In this respect, the conditions to convert into an institutional BE-REIT have been eased and the list of 'eligible investors' provided by the BE-REIT Decree includes retail investors subject to a minimum investment value of EUR 100,000.

Last, the BE-REIT Law foresees the form of social BE-REIT, an unlisted vehicle dedicated to investment in real estate used for social purposes (e.g. education, care).

All former SICAFI/Vastgoedbevak have converted into BE-REIT, and therefore only the BE-REIT regime is commented below.

### Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Belgium	17	11	EUR 16,324	1.02%

### Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Warehouses De Pauw	EUR 3,413	41.39%	3.24%	0.23%
Cofinimmo	EUR 2,571	10.79%	4.64%	0.22%
Aedifica	EUR 2,063	20.31%	5.11%	0.18%
Befimmo (Sicafi)	EUR 1,429	2.62%	6.82%	0.09%
Montea	EUR 1,181	77.67%	3.04%	0.08%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Licence from the Financial Service and Markets Authority ('FSMA')
- BE-REIT list

The BE-REIT must obtain a licence as a collective investment undertaking from the FSMA. Then it can be registered on the list of Belgian regulated real estate companies ('BE-REIT list'). The granting of the licence by the FSMA is based on a licence request comprising the following information, out of which the FSMA can assess the compliance with the BE-REIT Law and the BE-REIT Decree:

- the articles of association and the fact whether the company has been constituted for an indefinite term;
- if it has an appropriate administrative, accounting, financial and technical organisation which ensures independent management;
- that its directors and the persons in charge of daily management have the appropriate professional reliability and experience to ensure independent management;
- that at least two persons in the board of directors supervise the daily management;
- that a minimum investment budget has been determined for a period of three years as of the registration on the BE-REIT list;
- that it has called upon one or more independent real estate experts who are responsible for the valuation of the invested real estate. Such experts have to be chosen from a list annexed to the application and may not have direct links to the so-called 'promoter' of the BE-REIT;
- that the real estate expert has the required professional reliability and experience, including the organisation;
- that it complies with the rules on risk diversification;
- that an entity in charge of the financial services is appointed;
- that the identity of its so-called 'promoter' is known and the confirmation of its obligations;
- that it engages to comply with the listing requirements.

### b. Legal form/minimum share capital and securities

Legal form	Minimum share capital
<ul style="list-style-type: none"> <li>- Belgian public limited liability company</li> <li>- Belgian limited partnership with shares</li> </ul>	EUR 1.20 million

#### Legal form

A BE-REIT must be a public limited liability company (*société anonyme, SA/naamloze vennootschap, NV*),

incorporated for an unlimited period of time. The statutory seat and general management of the BE-REIT must be located in Belgium. Note that as a result of the entry-into-force of the new Code of Companies and Association, the corporate form of a limited partnership with shares (*SCA/Comm VA*) is not available anymore meaning that existing BE-REITs having this corporate form shall have to convert into a public limited liability company (*SA/NV*).

The status of BE-REIT is open to corporations only; a foreign entity that is similar to a BE-REIT cannot benefit from a passporting regime nor request the application of the BE-REIT (tax) regime to a branch it would have in Belgium and/or the real estate assets it directly owns in Belgium.

### Minimum share capital and securities

The required minimum share capital amounts to EUR 1.20 million. In principle, each shareholder has an equal right to participate in the profits of the BE-REIT. However, different categories of shares may be issued if allowed by the articles of association. The BE-REIT is allowed to issue securities other than shares (e.g. bonds, convertible bonds) to the exclusion of profit shares (*parts bénéficiaires/winstbewijzen*).

A B-REIT is also allowed to raise capital in cash through the so-called Accelerated BookBuild ('ABB') process, without having to grant a preferential subscription right or irreducible allocation right to existing shareholders. The ABB refers to a capital increase in which the creation of the order book is spread over a short period of time of a few hours or a few days, with little or no means of promotion, so as to allow the company concerned to find financing quickly and/or to take advantage of special conditions of market. Given the timing, this type of operation is carried out through the authorised capital technique. Please note that the cumulative capital increases via the ABB process cannot exceed 10% of the share capital upon the capital increase decision over a period of 12 months.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
No requirements	Yes

#### Shareholder requirements

There are no specific shareholder conditions to fulfil in order to achieve BE-REIT eligibility.

#### Listing requirements

All shares of a Belgian BE-REIT must be listed on a stock exchange, with a minimum of 30% free float. Listing can only occur after registration on the BE-REIT list and after the publication of a prospectus. There are specific prospectus requirements for BE-REITs in Belgium.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- The principal activity must be the active management of real estate assets
- A maximum of 20% of the total assets can be invested in one real estate project (ensemble immobilier/ vastgoed geheel) ('risk diversification'); this risk diversification requirement does not apply in relation to infrastructure (public-private partnerships) when the tenant, user or beneficiary is an EEA Member State
- Developments are allowed, but cannot be sold before, during or within five years of completion (no promotion)
- The BE-REIT is allowed to hold shares in subsidiaries investing in real estate, including institutional BE-REITs but specific requirements, incl. minimum participation thresholds, apply in case of public-private partnerships or joint venture
- As an exception, the BE-REIT is allowed to invest in transferable securities
- The BE-REIT may hold hedging instruments (covering its financial risk), but excluding speculative transactions

##### Immovable property

The BE-REIT may only invest in 'immovable property', whether located in Belgium or not. This includes the following:

- real estate and rights in rem on real estate;
- shares with voting rights in real estate companies (including intermediary holding), whose share capital is held (directly or indirectly) for more than 25% by the BE-REIT;
- option rights on real estate;
- shares in BE-REITs and in institutional BE-REITs, whose share capital is held (directly or indirectly) for more than 25% by the BE-REIT;
- the units of a foreign collective investment undertaking investing in real estate and registered on the Belgian FSMA list of foreign collective investment undertakings;
- the units of a collective investment undertaking investing in real estate, established in the EEA and subject to an equivalent control;
- real estate certificates;
- shares of EEA REITs<sup>4</sup>;
- shares of SICAFI/Vastgoedbevak;
- shares of FIIS/GVBF;
- subject to limitations, rights resulting from financial leases as defined by IFRS and analogous rights of use.

A BE-REIT may develop real estate, provided that the BE-REIT maintains the completed developments for at least five years.

As an exception, the BE-REIT is allowed to invest in transferable securities to the extent that the articles of association authorise such investments. In such cases, investments in transferable securities must be considered ancillary or temporary. Belgian law does not provide for any specific minimum or maximum requirements. The FSMA will exercise its discretion when examining the BE-REIT's articles of association.

<sup>4</sup> As further defined by the Law of May 12, 2014.



The BE-REIT may hold hedging instruments covering its financial risk to the extent that the articles of association authorise such transactions. Speculative transactions are not allowed. The hedging strategy must be disclosed in the BE-REIT's financial reports.

## Public-private partnerships and infrastructure projects

The list of authorised activities of a BE-REIT include the execution, as the case may be indirectly and/or in a joint venture, with a public partner, of DBF agreements, DB(F)M agreements, DBF(M)O agreements, or agreements for the concession of public works (i.e. the participation to public-private partnerships). Important to note: the BE-REIT can conclude this type of contracts directly or in a joint venture in a project company (such a project company having the possibility to opt for the status of institutional BE-REIT).

These agreements must relate to buildings or infrastructures for which:

- the BE-REIT is liable for their putting at disposal and maintaining or operating, for a public entity or the citizen as a final user; and
- the BE-REIT can assume, in whole or in part, the financing risk, the availability risk, the demand risk or the operation risk, and the construction risk.
- The BE-REIT should also be allowed to take care, in the long term, of the development, establishment, management and operation, as the case may be in a joint venture and through sub-contracting of:
- installations and warehouses for the production, transport, distribution or stocking of energy in the broad sense;
- installations for the transport, distribution, stocking and purification of water; and
- incinerators and waste installations.

The infrastructure activity can also be operated by a project company, in which the BE-REIT shall participate. In such a case, and as a derogation to the minimum participation threshold, the BE-REIT is allowed to take initially a participation of less than 25% in the share capital of the project company concerned, provided that this percentage is increased within two years (or a longer period of time if required by the public partner) after the construction phase, in order to comply with the below requirements for investing in a joint venture. The project company can also opt for the status of institutional BE-REIT and benefit from its tax regime.

## Risk diversification

The BE-REIT may not invest more than 20% of its total assets into one single real estate project. Under certain specific conditions it is possible to obtain a derogation of this rule from the FSMA, provided that its leverage limit does not exceed 33% of its consolidated assets

This risk diversification requirement and limit of 20% of the B-REIT's assets do not apply when an EEA Member State is the tenant, user or beneficiary of an infrastructure in the framework of a public-private partnership.

It is also specified that the restriction for the BE-REIT to grant loans or vest securities for third parties does not apply in the framework of the infrastructure activities described for public-private partnerships in view of a bid bond or similar mechanism. Subject to a series of conditions, the limit according to which a mortgage or other guarantee cannot exceed 75% of the relevant asset's value is also not applicable and the indebtedness related to those infrastructure projects is also not subject to the leverage limit and not taken into account to determine the leverage limit of a BE-REIT.

## Joint ventures

Considering the interests of the BE-REIT's investors, the regulation also contains specific provisions applicable to joint ventures.

The minimum participation required is 25% (plus one share) in the capital of the perimeter company, which can also opt for the status of institutional BE-REIT. For the BE-REIT, those participations (in absence of exclusive or joint control) cannot exceed 50% of its consolidated assets.

It is prohibited for a BE-REIT to enter into a shareholder's agreement which derogates to its vote cast according to its participation (being at least 25% plus one share) in a joint venture.

## e. Leverage

### Leverage

- LTV ratio limited to 65% of the (consolidated) assets (under specific conditions limited to 33%)
- (consolidated) Interest expenses limited to 80% of the total income
- Mortgage (or other collateral) is limited to 50% of the global fair value of the 'immovable property' and to 75% of the value of each 'immovable property' mortgaged, subject to exceptions when it concerns the participation in public-private partnerships

Belgian legislation requires that the aggregate loans do not exceed 65% of the total fair value of the assets of the BE-REIT (at the time of entering into the loan). Furthermore, the annual interest costs may not exceed 80% of the total annual operational and financial income. If the BE-REIT holds shares in affiliated companies investing in real estate, the leverage restrictions will be applicable on a consolidated basis.

In order to guarantee proactive management, the BE-REIT must present a financial plan to the FSMA as soon as its consolidated debt-to-asset ratio exceeds 50%.

In case the BE-REIT has obtained a derogation to the risk diversification rule, the debt-to-asset ratio may not exceed 33%.

A BE-REIT may only vest a mortgage (or other collateral) on real estate in relation to the financing of its 'immovable property' activities or of the 'immovable property' activities of the group. The total amount covered by a mortgage (or other collateral) may not exceed 50% of the total fair value of the 'immovable property' held by the BE-REIT and its subsidiaries. Moreover, it is not allowed to vest a mortgage (or other collateral) on one immovable property for more than 75% of its fair value, except in case of infrastructure activities in relation with public-private partnerships.

## f. Profit distribution obligation

Operative income	Capital gains	Operative income	Timing
80% of net profit as determined by Royal Decree	Not included in the distribution obligation, if reinvested within a four-year time period		Annually

### Operative income

Subject to the provisions of the Belgian Company code on capital protection, Belgian legislation requires the BE-REIT to distribute on an annual basis the positive difference between (i) 80% of its net operational

result (as determined by Royal Decree) and (ii) the net decrease of its indebtedness. No distribution is allowed if the (statutory or consolidated) indebtedness ratio exceeds 65% or will exceed this limit as a result of the distribution.

The same profit distribution obligations also apply to institutional BE-REITs.

## Capital gains

Capital gains are not included in the distribution obligation, provided the capital gains are reinvested within four years.

## g. Sanctions

### Penalties/loss of status rules

Various penalties (not necessarily resulting in the loss of BE-REIT status)

If the FSMA concludes that the BE-REIT does not observe the laws, regulations and/or its articles of association, this does not necessarily lead to a loss of BE-REIT status. Instead, the FSMA may, for example, make the necessary recommendations to the BE-REIT to remedy to the situation, subject to grace period which can be linked to a penalty of a maximum of EUR 50,000 per day of delay with a total of EUR 2,500,000. Or, the FSMA might impose temporary sanctions (for example, a public notice). The FSMA could also ask the market authorities to suspend the listing of the shares of the transgressing BE-REIT. The ultimate penalty would be to omit the BE-REIT from the BE-REIT list. The BE-REIT would then lose its status and would become a regular real estate company. The official loss of status would start as of the date of notification. Additionally, if there is an intentional infringement to certain laws and regulations, a prison sentence and/or a fine could be imposed on the directors of the BE-REIT, as well as on the ‘promoter’ of the BE-REIT.

The loss of BE-REIT status shall also have tax consequences. A recent ruling has clarified these consequences.

- With respect to the results of the year concerned, they will be subject to the B-REIT tax regime until loss of the regime and to the ordinary corporate income tax as from this date.
- The share capital of the B-REIT, in the sense of the corporate law legislation, shall be considered fiscal capital for the purposes of corporate income tax and withholding tax. The retained earnings, not yet distributed, of the B-REIT, built-up under the B-REIT status, shall be considered taxed reserves for
- The purposes of corporate income tax and withholding tax; these retained earnings have indeed been subject to their own tax regime.
- The revaluation surplus corresponding to the latent gain that has been subject to the exit tax, shall be considered a taxed reserve for the purposes of corporate income tax and withholding tax; this revaluation surplus has indeed been subject to its own tax regime.

## h. Institutional BE-REIT

The institutional BE-REIT status is available to companies investing in ‘immovable property’ as defined above or participating in public-private partnerships, provided that their share capital is owned, directly or indirectly, for 25% + 1 share by a BE-REIT. The capital of institutional BE-REIT is open to institutional

or professional investors, but also to retail investors, subject to a minimum investment value of EUR 100,000.

The fact that the status of institutional BE-REIT is available only to subsidiaries of BE-REITs (and not to subsidiaries of other EU REITs) might be considered to be contrary to EU law.

Even though the institutional BE-REIT's regulatory regime is less stringent, it is still subject to FSMA supervision. The key regulatory features are as follows:

- Given its capacity as a subsidiary of a BE-REIT, certain requirements applicable to BE-REITs should also impact the institutional BE-REIT. The risk diversification requirement of the BE-REIT is assessed on a consolidated basis. As the real estate expert is appointed to appraise the BE-REIT's assets and those of its subsidiaries, it was not necessary to subject institutional BE-REITs to the same obligation. Financial reporting obligations apply only to BE-REIT, but they concern consolidated information.
- Like BE-REITs, institutional BE-REITs can issue shares and bonds but with the exclusion of profit-sharing certificates. In the case of capital increase by contribution in kind, an institutional BE-REIT fully controlled by a BE-REIT or its subsidiaries is not subject to the requirement of a minimum subscription price. Specific requirements also apply to institutional BE-REITs jointly controlled by BE-REIT in case of capital increase by contribution in cash with a discount of more than 10%. Other capital transactions are subject to the common corporate law regime.
- The institutional BE-REIT is subject to the same distribution requirements.

#### i. Social BE-REIT

A new type of non-stock listed BE-REIT is created to finance and promote investments in 'care', subject to their accreditation by the competent authority, and defined as infrastructures dedicated to

- the housing or care of disabled persons;
- the housing or care of elderly persons;
- the care or help of youth persons;
- the collective welcoming and care of children under the age of three;
- the teaching and accommodation of students;
- the operation of a psychiatric institution; or
- the operation of a revalidation centre.

Social BE-REITs are incorporated as cooperative companies with a social purpose, having a minimum fixed capital of EUR 1,200,000. The variable capital can be subscribed by retail investors, in a proportion to be determined by Royal Decree. Due to their corporate form, they guarantee a dividend of maximum 6% (after deduction of the withholding tax) per year, but the exit is only structured as a buy-back of shares at nominal value. The social BE-REIT must build-up a liquidity reserve to execute these buy-back orders, which can themselves be limited.

The social BE-REIT is only allowed to invest in 'real estate assets' as defined by the Civil Code and in leasing. Its indebtedness level cannot exceed 33% of its asset value.

#### j. Qualification as an AIF

The BE-REIT does not qualify as an AIF.

### 3 Tax treatment at BE-REIT level

Unless indicated otherwise, the tax treatment applies to a BE-REIT as well as to an institutional BE-REIT and a social BE-REIT.

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
The eligible rental income is excluded from the taxable basis	Tax-exempt	N/A

#### Current income

Theoretically, the BE-REIT is subject to the Belgian corporate income tax at the rate of 29.58%. However, the taxable basis is reduced (i.e. de facto zero taxable basis). A BE-REIT is taxed on an accrual basis only on the sum of the non-arm's length benefits received and the expenses and charges due that are not deductible as expenses for tax purposes (other than reductions in value and capital losses on shares), and the undisclosed salaries and commissions. The taxable basis does thus not include rental income or other types of business income, nor exceeding borrowing costs pursuant to ATAD (Anti-Tax Avoidance Directive).

Due to the fact that the BE-REIT enjoys its own favourable tax regime which allows for a very low tax basis, it is not entitled to take advantage of the Belgian participation exemption nor of the Belgian notional interest deduction regimes. Additionally, Belgian law explicitly excludes a BE-REIT from the foreign tax credit on foreign source income.

#### Capital gains

Capital gains are not taxable, provided they are received at arm's length terms.

#### Withholding tax

In principle, non-Belgian source dividends and Belgian and non-Belgian source interest distributed to a BE-REIT are exempt from Belgian withholding tax.

Due to the fact that the (institutional) BE-REIT is subject to corporate income taxes, the BE-REIT will qualify as a Belgian resident. It will thus qualify for double taxation treaties, and benefits from the reduced withholding tax rates or withholding tax exemptions.

#### Other taxes

The special tax regime of the BE-REIT does not affect applicable local income tax, including the annual property tax, which is usually recharged to tenants of office buildings and retail spaces.

Furthermore, the BE-REIT is also subject to an annual tax of 0.0925% on the net amount invested in Belgium at the end of the financial year. The institutional BE-REIT is subject to an annual tax of 0.01%.

#### VAT

Management services invoiced to BE-REITs benefit from a VAT exemption.



## Accounting rules

The IFRS rules are applicable to the BE-REIT and institutional BE-REIT. Social BE-REITs have a choice between IFRS and BE-GAAP.

### b. Transition regulations

#### Conversion into BE-REIT status

- Real estate assets are to be assessed at market value, excluding Registration Duties.
- 12.75% tax on capital gains ('exit tax') (to be increased to 15% as from the 1st January 2020).

Upon conversion of a regular real estate company into a BE-REIT or upon the merger of such a company into a BE-REIT, the latent gain on the Belgian real estate and the tax-free reserves are subject to the exit tax at a rate of 12.75% (15% as from the 1st January 2020). The latent gain is computed on the basis of the appraised value of the real estate asset, excluding rights and taxes, and the tax losses of the Belgian company should be available for off-setting, subject to the minimum taxable base provided for by the tax legislation.

When a Belgian real estate asset is contributed to the BE-REIT (as a single asset or as part of a contribution of a line of business or universality), the capital gain realised by the transferor is also subject to the exit tax in its hands, but the transferor cannot claim the roll-over regime.

The tax law specifies that, in case of conversion, there is no withholding tax on the deemed dividend (in order to avoid any discussion in this respect).

Note that merger, de-merger, or assimilated restructuring in case all participants to the operation are BE-REITs occur in tax neutrality. This type of restructuring between BE-REITs can therefore be performed without adverse tax consequences for the shareholders.

### c. Registration duties

#### Registration duties

- No capital duty
- Real property transfer tax of 10% or 12.5% for full ownership rights or usufruct right
- Real property transfer tax of 2% for long-term lease right

No capital duty is due upon incorporation and capital increase.

Depending on the location of the real estate, the sale and purchase of real estate assets are subject to the 10% or 12.5% transfer tax. If the purchase or sale is subject to VAT, then no real estate transfer tax is levied. The granting of a long-term lease right (*droit d'emphytéose/erfpachtrecht*) is subject to a 2% transfer tax.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Dividends and capital gains are fully taxable, but if a dividend participation regime applies (in case of qualifying investment in foreign real estate), dividends and capital gains are in principle 100% tax-free	<ul style="list-style-type: none"> <li>- Withholding tax on dividends at 30% is the final tax burden (15% for BE-REITs investing in healthcare)</li> <li>- In principle, capital gains are tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- In principle, a 30% withholding tax (15% for BE-REITs investing in healthcare)</li> <li>- Withholding tax exemption in case of participation of at least 10% in the share capital of the BE-REIT during a minimum uninterrupted holding period of one year</li> </ul>

#### Corporate shareholder

Dividends received and capital gains realised, which derive from Belgian real estate, are fully taxable (29.58%). However, if the Belgian dividend participation exemption regime applies, dividends and capital gains benefit from a 100% tax deduction. Note that the Belgian dividend participation exemption regime is only available in case of redistribution by the BE-REIT of:

- real estate income deriving from foreign real estate assets located in EEA or in a treaty country (with an exchange of information clause) subject to this income being subject to tax without enjoying a derogatory tax regime; and
- dividends and capital gain deriving from company(ies) holding such foreign real estate assets, in case this company meets the subject-to-tax requirement.

A return of capital is in principle not taxable if it occurs on the basis of a regular decision in accordance with the Belgian Company Code or similar non-Belgian company law. Capital decreases are however re-characterised into dividend distributions pro rata certain taxed and untaxed reserves of the company. Untaxed and unavailable reserves not incorporated to the share capital (e.g. revaluation surplus), the legal reserve and the negative taxed reserve recorded further to corporate restructuring are not considered by this measure. The same rule applies to reimbursement of share premium.

For tax purposes, the capital decrease is deemed to be allocated pro-rata between the share paid-up capital and the reserves, and within the reserves, exclusively and in the following order:

- on the taxed reserves incorporated in the share capital; in such a case the dividend is subject to withholding tax (incl. the reductions and exemptions provided by law or tax treaty) and may benefit from the participation exemption in the hands of the recipient;
- on the taxed reserves not incorporated in the share capital; in such a case the tax treatment is the same as above; and
- on the untaxed reserves incorporated in the share capital; in such a case the amount qualified as dividend shall first be subject to corporate income tax in the hands of the company and then subject to the tax treatment applicable to taxed reserves.

The paid-up capital of the company shall be deemed to decrease only to the extent of the amount of the capital decrease imputed on this paid-on capital.

## Individual shareholder

The 30% dividend withholding tax is the final levy.

Capital gains realised on BE-REIT shares are not taxable, unless the Belgian tax authorities are able to demonstrate that the capital gain was not realised within the scope of the normal management of private assets or that the capital gain was speculative.

A return of capital is in principle not taxable if it occurs on the basis of a regular decision in accordance with the Belgian Company Code or similar non-Belgian company law. Capital decreases are however re-characterised into dividend distributions pro rata certain taxed and untaxed reserves of the company. Untaxed and unavailable reserves not incorporated to the share capital (e.g. revaluation surplus), the legal reserve and the negative taxed reserve recorded further to corporate restructuring are not considered by this measure. The same rule applies to reimbursement of share premium.

Moreover, a return of capital upon liquidation or redemption of the BE-REIT's shares would be taxable if, upon the public offering of the shares in Belgium, the SICAFI guarantees a certain repayment or rate of return for a period of eight years or less to its investors. In that case, the return is deemed to constitute an interest subject to 30% withholding tax.

## Withholding tax

In principle, 30% withholding tax is due on dividends distributed by a (institutional) BE-REIT.

Dividends distributed by the BE-REIT to its shareholders are subject to 15% withholding tax if the BE-REIT invests at least 60% of its assets in real estate used for healthcare in the EEA.

If the conditions of the European Parent-Subsidiary Directive are met (e.g. minimum participation of 10% or investment value of at least EUR 2.5 million, and held during an uninterrupted period of at least one year), no withholding tax will be due on dividend distributions to a corporate domestic shareholder.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Capital gains tax-exempt in Belgium	Capital gains tax-exempt in Belgium	<ul style="list-style-type: none"> <li>- Distribution of Belgian-source income subject to 30% withholding tax, subject to reduction or exemption based on tax treaty</li> <li>- Distribution of foreign-source income benefits from a withholding tax exemption without the subject-to-tax requirement</li> <li>- Distribution to foreign pension funds benefits from a withholding tax exemption</li> </ul>

## Investment in Belgian real estate

Dividends distributed to a **foreign pension fund** that (i) is not conducting a business or a lucrative activity, (ii) is totally tax-exempt in its country of residence, and (iii) is not contractually obliged to redistribute these dividends to a beneficial owner that cannot qualify for this exemption, benefit from a **withholding tax exemption**.

Dividends distributed to **foreign investors** shall be subject to 30% withholding tax subject to **exemption or reduction** by virtue of the applicable **tax treaty**.

Apart from this withholding tax, no non-resident taxation applies.

### Investment in foreign real estate

Dividends distributed to **foreign investors** shall benefit from a **withholding tax exemption** without the underlying condition of taxation in the source state.

## 5 Tax treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
No specific tax privilege	No specific tax privilege	No specific tax privilege

### Foreign REIT

A foreign REIT is not eligible for the REIT regime and is therefore subject to the ordinary Belgian non-resident income tax. The Belgian source net income of the foreign REIT will be taxable at a rate of 29.58%.

### Corporate shareholder

The tax treatment of a domestic corporate shareholder of a foreign fund depends on the specific characteristics of the fund.

If the foreign fund has no legal personality, then the corporate investor is deemed to have invested in real estate himself/herself. On the basis of the applicable tax treaty, the non-Belgian real estate income would most likely be taxed in the country where the real estate is located (thus tax-exempt in Belgium). Likewise, capital gains realised on the participation in a foreign fund without legal personality, would be considered capital gains on real estate. On the basis of the applicable tax treaty, the capital gain realised on non-Belgian real estate would most likely be taxed in the country where the real estate is located and therefore tax-exempt in Belgium.

Concerning a foreign fund with legal personality, the corporate investor will not be deemed to have invested in real estate but in the fund itself. The same rules apply for the dividends received, and the capital gains realised on the shares in a Belgian BE-REIT. The foreign withholding tax levied on dividends received from a non-Belgian real estate fund is a tax-deductible item.

### Individual shareholder

The tax treatment of a domestic individual shareholder of a foreign fund depends on the specific characteristics of this fund.

If it concerns a foreign fund without legal personality, the individual investor will be deemed to have invested in real estate himself. The same rules apply as for the corporate investors.

Concerning a foreign fund with legal personality, the individual investor will not be deemed to have invested in real estate but in the fund itself. The income received from the fund will be taxed according to the rules of dividend taxation. Consequently, the dividends would be taxable at a rate of 30% (plus communal surcharges if the fund is located outside the EER). The foreign withholding tax levied on the dividend income would be deductible from the Belgian taxable basis. Capital gains realised on foreign real estate fund shares are treated in the same way as capital gains realised on BE-REIT shares. ■

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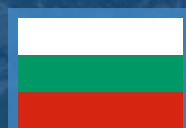
EUROPE

Bulgaria

SPIC

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
SPIC	2004	Special Purpose Investment Companies Act (SPICA)	Corporate type

The SPIC regime was introduced with the Special Investment Purpose Companies Act (SPIC), which came into force on January 1, 2004.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Bulgaria	29	0	EUR 430	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

- Licence from the Financial Supervision Commission
- Listing on Bulgarian Stock Exchange authorisation
- Depository bank mandatory

In order to qualify as a SPIC, a company is required to obtain a licence from the Bulgarian Financial Supervision Commission (FSC). An SPIC shall be established at a constituent meeting at which its shares are subscribed. The founders may not number more than 50. Within seven days after the SPIC is registered in the Commercial Register, the FSC shall be notified. The SPIC shall file with the FSC an application for a licence within six months as from its registration with the Commercial Register.

In addition, upon the incorporation of a SPIC, the constituent meeting is obliged to pass a resolution for an initial capital increase up to at least 130% of the initial share capital (i.e. the capital increase should be in the amount of at least 30 % of the initial share capital). This first capital increase can be performed only on the basis of a prospectus authorised by the FSC. Once the formal authorisation (licence) is granted, the SPIC may effectively increase its capital. This increase is to be performed through the issuance of rights entitling their holders to take part in the subscription of shares from the capital increase. Said rights must be listed on a regulated market (the Bulgarian Stock Exchange JSC) and no pre-emptions rights apply.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Joint stock company	BGN 500,000 (~ EUR 255,646)

## Legal form

An ASPIC can only be established and operate as a public joint-stock company (AD). The company name of the special purpose investment company needs to include the denomination 'joint-stock special purpose investment company' or the abbreviation 'JSSPIC'.

The registered seat and address of management of a SPIC must be located in Bulgaria. The same requirement applies to its service companies, which are required for certain SPIC activities.

## Minimum share capital

The minimum share capital requirement for a SPIC (at the time of incorporation) is BGN 500,000 (~EUR 255,646). The share capital must be fully paid in as of the date of applying for registration in the Commercial Register. No contributions in kind are permitted. The SPIC can issue only book-entry (dematerialised) shares.

The initial increase of registered capital via an IPO should amount to not less than 30% of the initial registered capital.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- At least 30% of the capital shall be owned by the institutional investor(s)</li> <li>- No more than 50 founders</li> </ul>	Yes

## Shareholder requirements

Upon the incorporation of a SPIC, at least 30% of the capital shall be subscribed by institutional investors. An 'institutional investor' is not legally defined by the SPIC. However, according to § 1, item 1, letter 'c' of the Supplementary Provisions of Public Offering of Securities Act ('POSA') 'institutional investor' is any of the following: a bank, a collective investment scheme and a national investment fund, an insurance company, a pension fund or another corporation whereof the objects require the acquisition, holding and transfer of securities. In addition, according to FSC guidelines, an institutional investor is described as a bank, insurance company, licensed pension fund or other financial institution, which are subject to the supervision of the FSC. Foreign legal entities may also act as institutional investors if approved by the FSC. An institutional investor may also have a licence granted by the FSC. As an alternative to FSC supervision, banks are subject to special legal acts. It is not allowed for more than 50 persons or entities to be founders of a SPIC. It has not yet clearly been stated whether a SPIC may be owned by just one shareholder.

## Listing requirements

Within six months after its registration in the Commercial Register, the SPIC must apply for the approval of its prospectus for IPO by the FSC. The prospectus is submitted to the FSC as a part of the documents accompanying the application for issuance of a licence for carrying on activities as a SPIC.

There is no clear rule regarding which stock exchange the SPIC must be listed on. However, based on the analysis of the current regulations and for other practical considerations, it seems that the SPIC can only be initially listed on the Bulgarian Stock Exchange JSC. Before it may do so, the SPIC's IPO prospectus must be approved by the FSC. However, SPICs may be listed on other EU regulated markets as well.

#### d. Asset levels/activity tests

##### Restrictions on activities/investments

- No more than 10% of the SPIC's assets may be invested in mortgage bonds
- No more than 10% of the SPIC's assets may be invested in service companies
- No more than 30% of the assets of a SPIC (investing in real estate) may be invested in SPVs for investments in real estate
- No more than 10% of the SPIC's assets (investing in real estate) may be invested in other SPICs investing in real estate
- No investments allowed in real estate subject to a legal dispute
- Real estate investments must be located in Bulgaria. However, the SPVs, in which SPICs (investing in real estate) can make investments, may, in turn, invest in real estate located in Bulgaria or other EU member state

The business activity of a SPIC investing in real estate is limited to:

- purchasing real estate (which must be located in Bulgaria) and limited property rights to real estate, carrying out real-estate construction and improvements (for property management, renting, leasing, sales); and
- raising funds by issuing securities. The IPO is mandatory for SPICs. However, additional financing is not prohibited. Therefore, the SPIC may engage in equity and debt financing.

SPICs can invest up to 10% of their assets in mortgage bonds. SPICs are entitled to invest up to 10% of their assets in service companies. SPICs investing in real estate may invest up to 30% of their assets in SPVs for investments in real estate if the respective SPIC exercises control over such SPV. In addition, SPICs investing in real estate may invest up to 10% of their assets in other SPICs investing in real estate. No other investments in shares are allowed.

An SPIC may not directly perform the maintenance services of the acquired real estate. The SPIC must delegate these services to one or more service companies. These companies can engage in the following activities: servicing and maintaining acquired real estate, constructing and improving real estate, servicing the receivables, keeping and safeguarding the accounting records and other reporting correspondence, and many other necessary activities.

#### e. Leverage

##### Leverage

Short-term loans cannot exceed 20% of income-generating asset

The only introduced debt financing limitation concerns loans granted for settlement of interest due by the SPIC. In that case, the company may only borrow (from a bank) an amount not greater than 20% of its balance sheet asset value and for a period not exceeding one year.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of the net income of the year	Included in net income	Distribution until the end of the following financial year required

## Operative income

The SPIC is obliged to distribute at least 90% of the profit as dividends. It must do so within 12 months following the financial year in which the profit was incurred.

## Capital gains

Special rules determining the formation of the profit of a SPIC are set out under the SPICA, and the capital gains/losses are explicitly provided as such items.

### g. Sanctions

#### Penalties/loss of status rules

Monetary penalties and a possible loss of SPIC status

The Finance Supervision Commission will cancel the SPIC's licence if:

- the SPIC does not begin activities within 12 months after receiving the licence or did not perform licensed activities for more than six months;
- the SPIC has provided wrongful information (based on which the licence was granted);
- the SPIC explicitly asked for the withdrawal of its license;
- the SPIC has not implemented an enforced coercive measure under SPICA, the Public Offering of Securities Act or the acts for its implementation;
- the SPIC does no longer meet the conditions under which the licence has been granted; or
- the SPIC systematically breaches SPIC statutory rules.

Furthermore, SPICs are not allowed to change their legal form as well as to change their scope of activity, except in the cases where the license of the respective SPIC has been withdrawn by the Financial Supervision Commission based on a request by the SPIC (in this case the respective SPIC may continue to exist as a public traded joint-stock company). Doing so would result in a loss of status.

SPICs which breach the profit distribution obligation may be penalised between BGN 10,000 (~EUR 5,113) and BGN 20,000 (EUR 10,226) for individuals and between BGN 20,000 (EUR 10,226) and BGN 40,000 (EUR 20,452).

## 3 Tax treatment at the level of REIT

### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt	Tax-exempt	N/A



## Current income

The income of a SPIC is not subject to corporate taxation. In this respect, the SPIC is not entitled to a tax credit for foreign income tax paid.

## Capital gains

Capital gains realised by a SPIC are not subject to taxation since they are included in the financial result of the SPIC, which is exempt from corporate taxation.

## Other taxes and fees

Other taxes may be applicable to SPICs such as VAT at a standard rate of 20%, garbage collection fees and annual real estate tax in the range of 0.01%-0.45% (the exact rate is determined by the municipality where the property is located).

## Accounting rules

Unless provided by the SPIC regime, the rules provided by the IFRS apply.

### b. Transition regulations

#### Conversion into SPIC status

The tax legislation does not envisage any special rules for SPIC

### c. Registration duties

#### Registration duties

- Transfer tax of 0.1% to 3%
- Land Registrar Entrance Fee of 0.1%

A real estate transfer tax the rate of which varies between 0.1% and 3% (the exact rate applicable in the respective year is approved by the Municipal Council as per the location of the real estate property) and a land registrar entrance fee of 0.1% are levied on the purchase price of the real estate or on the tax value determined by the municipality (in compliance with the Local Taxes and Fees Act).

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Dividends are subject to corporate income tax</li> <li>- Capital gains could be tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- 5% withholding tax on distributions is the final levy</li> <li>- Capital gains could be tax-exempt</li> </ul>	To credit withholding tax is not possible

## Corporate shareholder

### Dividends

Dividends distributed by a SPIC to domestic corporate shareholders are not subject to withholding tax except for shareholders who are not considered merchants according to the Bulgarian legislation. However, dividends are taxed with corporate income tax at the recipient level under the general tax rules.

### Capital gains

Capital gains realised from the sale of SPIC shares could be tax-exempt if they are traded on a recognised EU/EEA stock exchange.

### A return of capital distribution

Under the Bulgarian tax legislation, capital decrease does not have tax implications (with certain exceptions).

### Individual shareholder

If dividends are distributed to resident physical persons, a 5% domestic final withholding tax is applied. Capital gains realised on the sale of the SPIC shares could be tax-exempt if they are traded on a recognised EU/EEA stock exchange.

### Withholding tax

For individual shareholders and corporate shareholders who are not merchants, a withholding tax of 5% on dividend payments applies. It is not possible to credit this withholding tax. Dividend distributions to corporate shareholders are not subject to withholding tax.

## b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Dividends are subject to a 5% withholding tax</li> <li>- Possibility of dividend tax reduction</li> <li>- Dividends distributed to EU/EEA entities are tax exempt</li> <li>- Capital gains could be tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- Dividends subject to a 5% withholding tax</li> <li>- Possibility of dividend tax reduction</li> <li>- Capital gains could be tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- Treaty relief might apply</li> </ul>

### Corporate shareholder

A 5% domestic tax rate, or the lower respective DTT withholding tax rate, applies on the dividends distributed by the REIT.

If the income accrued to the foreign shareholder exceeds BGN 500,000 (EUR 255,646) for the calendar year DTT protection can be obtained following successful completion of the advance clearance procedure under the Tax and Social Security Procedure Code.

If the accrued income is less than BGN 500,000, the DTT can be applied directly by the REIT. For the direct application of the DTT relief, the foreign shareholder must give the REIT a tax residency certificate and a declaration of beneficial ownership of the income.

In addition, dividends distributed to EU/EEA tax resident entities are exempt from taxation.

### Individual shareholder

Dividends paid to foreign individuals face a 5% withholding tax unless a more favourable rate is provided under an applicable DTT, which is again applicable on the same conditions for corporate shareholders. Capital gains could be exempt from taxation, as long as the SPIC shares are listed on an EU/EEA stock exchange and the individual shareholder is EU/EEA tax resident.

### Withholding tax

A 5% withholding tax will be levied on dividend payments if the recipient is not an EU/EEA entity. Treaty relief may be available.

## 5 Tax treatment of foreign REIT and its domestic shareholder

### Income realised by a foreign REIT from Bulgarian source

Foreign REIT
Local rental income is subject to a Bulgarian withholding tax of 10%

### Income realised by Bulgarian residents from a foreign REIT

Corporate shareholder	Individual shareholder
Dividends distributed by EU/EEA corporations are tax-exempt	No tax privileges

### Foreign REIT

The Bulgarian rental income of a foreign REIT is subject to a withholding tax of 10%.

### Corporate shareholder

Corporate shareholders are taxed on the income from dividends distributed by a foreign corporation, except for dividends from EU/EEA tax residents.

### Individual shareholder

Individual shareholders are taxed on the income from dividends distributed by a foreign corporation under the general rules and such are subject to 5% one-off tax. ■

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2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type	REIT market
FINNISH REIT	2010	Act on Tax Incentives for certain Limited Companies Carrying on Residential Renting Activities (24.4.2009/299)	<ul style="list-style-type: none"> <li>- Private limited company (closed-ended)</li> <li>- Public limited company (closed-ended)</li> </ul>	No REITs currently in the market

The Finnish REIT was introduced with effect from January 1, 2010 by the Finnish Act on Tax Incentives for certain Limited Companies Carrying on Residential Renting Activities (24.4.2009/299). This was, however, subject to a state aid notification to the Commission. On May 12, 2010, the Commission announced that REIT is not illegal state aid. However, the Commission considered that a provision allowing REITs to use up to 30% of their annual profits to create tax-exempt re-investment reserves would constitute incompatible aid. Following the Commission's concerns, the Finnish authorities made the commitment not to put in force this provision. Under the REIT regime, a Finnish REIT is fully exempt from paying corporate income tax. However, penalty tax charges may apply on a REIT in certain circumstances.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Application for REIT status must be filed
- Certain conditions for REIT status apply

An application for REIT status must be filed with the Finnish tax authorities. REIT status must be granted to a Finnish limited liability company under the following conditions:

- the company does not carry on any other activities than renting of property and certain ancillary activities, such as property administration and maintenance and cash management. Property development on own account is permitted;
- at least 80% of the total assets of the company must comprise of shares in mutual real estate companies or residential real property (as defined in the relevant legislation) (measured using financial statements);
- the company does not hold any other assets than property, equipment required by its ancillary activities and liquid funds (as defined in the relevant legislation). The company may not, except for shares in mutual real estate companies, hold any shares in subsidiary companies;
- the company's total liabilities may not exceed 80% of the total assets (measured using consolidated financial statements);
- each shareholder must hold less than 10% of the share capital of the company; and
- the Finnish Act on Real Estate Funds (19.12.1997/1173) must apply on the company and hence it must be subject to supervision by the FIN-FSA.

The following additional conditions for REIT status apply as of the beginning of the first tax year as a REIT:

- the company must distribute as dividends at least 90% of its net income for each financial period;
- the company's shares must be listed on a regulated market or must be upon application admitted to trading on a Multi-lateral Trading Facility in the European Economic Area. Upon application to the Finnish tax authorities, this requirement may be suspended during the first two tax years as a REIT;
- the company does not distribute profits in any other form than as dividends; and
- the company or its mutual real estate company subsidiaries have not been involved in transactions the purpose of which is deemed to be tax avoidance.

In addition, at least 80% of the net income (excluding capital gains) of the REIT must be derived from the renting of residential property (measured using financial statements). Failure to fulfil this requirement results in a penalty tax charge on the REIT.

A REIT must file a tax return and a statement on fulfilling the conditions for REIT status with the Finnish tax authorities. The (consolidated) financial statement must be enclosed to the tax return.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
In practice, a public limited company	EUR 5 million

### Legal form

A Finnish REIT must be a private or public limited company incorporated in Finland. Under the Companies Act 21.7.2006/624, only a public limited company may be listed on a regulated market.

A Finnish REIT may own shares in so-called mutual real estate companies resident in Finland or, in principle, outside Finland. In general terms, a mutual real estate company is a company the shares of which entitle the shareholder to use (or rent to third parties) the premises owned by the mutual real estate company. A REIT may not hold shares in any other subsidiary companies except for shares in mutual real estate companies.

### Minimum share capital

Under the Finnish Act on Real Estate Funds (19.12.1997/1173), a Real Estate Fund must have a minimum share capital of EUR 5 million.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
A shareholder should not own 10% or more of the share capital	<ul style="list-style-type: none"> <li>- Yes</li> <li>- A requirement to be listed on a regulated market or admitted upon application to trading on a multilateral trading facility in the European Economic Area</li> </ul>

## Shareholder requirements

No shareholder should hold 10% or more of the share capital; otherwise a penalty tax charge will arise in relation to the dividend paid to such shareholder.

## Listing requirements

Under the Finnish Act on Real Estate Funds (19.12.1997/1173), a Real Estate Fund must apply for listing on a regulated market within three years of commencement of its activities, unless the FIN-FSA grants an exemption from this requirement.

Under the Finnish Act on Tax Incentives for certain Limited Companies Carrying on Residential Renting Activities (24.4.2009/299), a REIT's shares must be listed on a regulated market or admitted upon application to trading on a multilateral trading facility in the European Economic Area. Upon application to the Finnish tax authorities, this requirement may be suspended during the first two tax years as a REIT.

### d. Activity/asset level restrictions

#### Restrictions on activities/investments

- No other activities than renting of property and certain ancillary activities, such as property administration and maintenance and cash management, are allowed; development on own account is permitted
- At least 80% of the net income must be derived from the renting of residential property (measured using financial statements)
- At least 80% of the assets must consist of shares in mutual real estate companies or residential real property (measured using financial statements)
- May invest outside Finland

A REIT may not carry on any other activities than renting of property and certain ancillary activities, such as property administration and maintenance and cash management. Development by the REIT for its own account is permitted.

Disposals of property are permitted, but may result in a penalty tax charge unless the following requirements are met:

- the REIT disposes of less than 10% of its properties during a tax year (measured using balance sheet values);
- shares in mutual real estate companies have been held for five years; and
- more than five years have elapsed from a comprehensive modernisation fulfilling certain criteria (as defined in the legislation).

The financial restrictions are:

- at least 80% of the net income must be derived from the renting of residential property; and
- at least 80% of the total assets must consist of shares in mutual real estate companies or residential real property (as defined in the legislation).



## e. Leverage

### Leverage

Total liabilities may not exceed 80% of the total assets (measured using financial statements)

The REITs total liabilities may not exceed 80% of the total assets under (consolidated) financial statements.

## f. Profit distribution obligations

Profits	Capital gains	Timing
90% of the net income must be distributed	Realised capital gains are included in the distribution obligation	Not defined

### Dividends

A REIT must distribute as dividends at least 90% of its net income for each financial period.

### Capital gains

Gains arising from the disposals of property fall under the distribution obligation.

## g. Sanctions

### Penalties/loss of status rules

Tax charges not necessarily resulting in the loss of the REIT status

As a general rule, failure to meet any of the conditions for REIT status could result in the loss of REIT status. However, the failure to meet the requirement on 80% of the net income being derived from renting of residential property or the requirement concerning less than 10% ownership by each shareholder will result in a penalty tax charge only.

Where less than 80% of the net income (excluding capital gains) is derived from renting of residential property, a tax charge of 20% will arise on the REIT on the shortfall in the income from renting of residential property.

The REIT will incur a tax charge, at a rate corresponding to the valid CIT rate (currently 20%), on the amount equivalent to the dividend paid to a shareholder that holds at least 10% of shares in the REIT.

Disposals of property are permitted, but may result in a penalty tax charge unless the following requirements are met:

- the REIT disposes of less than 10% of its properties during a tax year;
- shares in mutual real estate companies have been held for five years; and
- more than five years have elapsed from a comprehensive modernisation fulfilling certain criteria (as defined in the legislation).

The tax authorities have general powers to make a REIT leave the REIT regime if they consider that the REIT has entered into arrangements with the sole or main purpose of tax avoidance. It is possible to appeal against such action.

### 3 Tax treatment at the REIT level

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
All income of a Finnish REIT is fully exempt from corporate income tax	Disposals of property are permitted but may result in penalty tax charges unless certain conditions are met	<ul style="list-style-type: none"> <li>- Distributions to Finnish resident individuals are subject to tax prepayment withheld at source</li> <li>- Under Finnish domestic law, dividends distributed by a Finnish REIT to a non-resident recipient will be subject to 15/20/30% withholding tax at source, subject to applicable tax treaties</li> </ul>

#### Corporate income tax

A Finnish REIT is fully exempt from paying corporate income tax. However, penalty tax charges may apply on a REIT in certain circumstances.

#### Capital gains

Disposals of property are permitted, but may result in a penalty tax charge unless the following requirements are met:

- the REIT disposes of less than 10% of its properties during a tax year;
- shares in mutual real estate companies have been held for five years; and
- more than five years have elapsed from a comprehensive modernisation fulfilling certain criteria (as defined in the legislation).

#### Withholding tax

Distributions to Finnish resident individuals are subject to tax prepayment withheld at source.

Under domestic law, dividends distributed by a REIT to a non-resident recipient will be subject to a withholding tax at source, subject to applicable tax treaties. The applicable domestic withholding tax rate is currently 30% for private individuals and 15/20/30% for other recipients depending on the type of the recipient.

If an overseas jurisdiction levies a withholding tax on payment to a Finnish REIT, the REIT will not be able to obtain credit for such tax as the income is exempt in Finland.

## Other taxes

Asset transfer tax, property tax and value-added tax apply in the same way that they apply for ordinary property companies.

## Accounting rules

As a general rule, accounting rules apply in the same way that they apply for ordinary property companies.

### b. Transition regulations

#### Conversion into REIT status

Conversion charge of 20% of the unrealised gains on all assets held by property company converting to REIT status

For Finnish tax purposes, all assets held by a property company converting to REIT status are revalued to market value. A 20% conversion charge is levied on the unrealised gains on all assets held at the day of conversion. The conversion charge can upon application be spread over three years from the year of conversion to REIT status.

### c. Asset transfer tax

#### Asset transfer tax

Asset transfer tax of 2% (shares in mutual real estate companies and other real estate companies), 1.6% (shares in other companies) or 4% (real property) (no different within the REIT regime)

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Tax at source
Dividends distributed by a Finnish REIT are fully taxable at 20%	Dividends distributed by a Finnish REIT are capital income fully taxable at 30/34%	The REIT must withhold tax at source on dividends paid to Finnish individuals and pay it forward to the tax administration

Under the Finnish Act on Tax Incentives for certain Limited Companies Carrying on Residential Renting Activities (24.4.2009/299), dividends distributed by a Finnish REIT are defined as fully taxable income for Finnish recipients.

#### Corporate shareholder

Dividends distributed by a Finnish REIT are fully taxable at 20%.

Capital gains on the disposal of shares in REITs are taxable under normal capital gains tax rules.

## Individual shareholder

Dividends distributed by a Finnish REIT (a listed company) are fully taxable capital income.

The tax rate for capital income is currently 30% for income not exceeding EUR 30,000, and 34% for income exceeding EUR 30,000.

Capital gains on the disposal of shares in REITs are taxable under normal capital gains tax rules.

## Taxation at source

The REIT must withhold tax at source on dividends paid to Finnish individuals and pay it forward to the tax administration.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder/ other shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- 15/20% final withholding tax on dividends (subject to tax treaties)</li> <li>- Disposal of shares in a Finnish REIT should typically be outside the scope of Finnish capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- 30% final withholding tax on dividends (subject to tax treaties)</li> <li>- Disposal of shares in a Finnish REIT should typically be outside the scope of Finnish capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- Tax treaty relief may be available; should be treated as a dividend distribution under most tax treaties</li> <li>- Parent-Subsidiary Directive not applicable</li> </ul>

## Corporate shareholder

Under domestic law dividends by a REIT to a non-resident recipient will be subject to 15/20% withholding tax at source, subject to the applicable tax treaties.

Gains on disposals of shares in a Finnish REIT could be subject to tax at 20% in the case at least 50% of the REIT's assets are directly held property located in Finland (as opposed to shares in mutual real estate companies), subject to the applicable tax treaties. In practice, disposals of shares in a Finnish REIT should typically be outside the scope of Finnish capital gains tax.

## Individual shareholders/other shareholders

Under domestic law dividends by a REIT to a non-resident recipient will be subject to 30% withholding tax at source, subject to the applicable tax treaties.

Gains on disposals of shares in a Finnish REIT could be subject to tax at 30/34% (or 20% in case of shareholders other than individuals) in case at least 50% of the REIT assets are directly held property located in Finland (as opposed to shares in mutual real estate companies), subject to the applicable tax treaties. In practice, disposals of shares in a Finnish REIT should typically be outside the scope of Finnish capital gains tax.

## Withholding tax

A non-resident shareholder suffers a withholding tax of 30% (individuals) or 15/20/30% (other recipients), subject to applicable tax treaty provisions. Treaty relief can be claimed ex-ante or retrospectively. The dividend should be treated as a dividend distribution under most treaties. The EU Parent-Subsidiary Directive is not applicable.

## Future developments

The Finnish withholding tax legislation will be changed with the effect from January 1, 2021. In short, the application of a tax treaty will always require that the custodian or the payer of a dividend provides the Tax Administration with the information on the final recipient of the dividend. The tax at source for the dividend will be increased to 35% if the final recipient information is not provided. Assuming the final recipient information is provided, the withholding tax rate is similar as described above.

## 5 Tax treatment of foreign REITs and its domestic shareholders

	Corporate shareholder	Individual shareholder
Taxed under normal Finnish tax rules	A foreign REIT distribution to a Finnish shareholder is likely to be treated as a normal dividend from the non-resident company (will depend on structure of foreign REIT)	A foreign REIT distribution to a Finnish shareholder is likely to be treated as a normal dividend from the non-resident company (will depend on structure of foreign REIT)

### Foreign REIT

A foreign REIT will be taxable under normal Finnish rules.

### Corporate shareholder

A foreign REIT distribution to a Finnish corporate shareholder is likely to be treated as a normal dividend (which may be fully or partially tax-exempt under certain conditions) from the non-resident company (will depend on structure of foreign REIT).

### Individual shareholder

A foreign REIT distribution to a Finnish individual shareholder is likely to be treated as a normal dividend from the non-resident company (will depend on the structure of foreign REIT). As a general rule, 85% of a dividend from a listed company is taxed at 30/34%, whereas a dividend from a non-listed company is divided into capital income (taxed at 30/34%) and earned income (taxed at progressive rates) under a certain formula. ■

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SIIC

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation
SIIC	2003	Article 11 of the Finance Act for 2003 Official comments from the French tax authorities

Article 11 of the Finance Act for 2003 (Law n° 2002-1575 of December 30, 2002) introduced a specific corporate income tax exemption regime applicable to listed real estate investment companies (sociétés d'investissements immobiliers cotées, SIICs) available upon election and subject to conditions. This regime is governed by articles 208 C, 208 C bis, 208 C ter and 219 IV of the French tax code (FTC). The SIIC regime has been amended by the Amending Finance Act for 2004, the Finance Act for 2005, the Amending Finance Act for 2006, the Amending Finance Act for 2007, the Finance Act for 2008, the Finance Act for 2009, the Amending Finance Act for 2009, the Finance Act for 2012, the Amending Finance Act for 2013 and the Amending Finance Act for 2014. In addition, the French tax authorities had published administrative tax guidelines on September 25, 2003, February 01, 2010, December 27, 2011, March 08, 2012, and on June 15, 2012. These are now all included in the French tax authorities' official comments published in the Bulletin Officiel des Finances Publiques BOI-IS-CHAMP-30-20-20140304 dated March 4, 2014 (and updated on March 27, 2019, BOI-IS-CHAMP-30-20-20190327).

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
France	30	6	EUR 51,010	1.77%

## Top five REITs\*

Company name	Mkt Cap	1 yr return (EUR)%	Div Yield	% of Global REIT Index
Gecina	EUR 9,755	-6.19%	4.10%	0.60%
Klepierre	EUR 8,564	-5.36%	3.56%	0.49%
Covivio	EUR 7,643	8.47%	5.00%	0.35%
Icade	EUR 2,146	3.46%	9.53%	0.04%
Carmila	EUR 1,064	-27.99%	9.65%	0.06%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

The SIIC regime has attracted a number of foreign companies such as Corio, and Wereldhave (Netherlands), Hammerson (UK), Cofinimmo, Montea and Warehouse de Pauw (Belgium).



## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- The election letter must be filed with the relevant tax office of the parent company with a list of the subsidiaries which also elect
- Subsidiaries list must be updated once a year

To benefit from the SIIC regime, an eligible real estate investment company (i.e. the listed parent company) must file an election letter with the French tax authorities by the end of the fourth month of the financial year in which this company wishes to benefit from the SIIC regime.

This election may also be made by subsidiaries subject to corporate income tax provided (i) at least 95% of their share capital is directly or indirectly held by one or several listed parent companies that have themselves elected for the SIIC regime or jointly held by one or several SIIC parent companies and one or several SPICAV (Société de Placement à Prépondérance Immobilière à Capital Variable), and (ii) their main object is identical to that of the listed parent company. The election letter must be filed with the relevant tax office of the parent company with a list of the subsidiaries elected for the SIIC regime. The list must be updated every year, together with the company's annual corporate tax return.

A subsidiary that wishes to elect for the SIIC regime must also identify the parent company and file the election letter with the relevant tax office.

Due to the changes in the company's tax regime, the process of election results in a partial cessation of business (Articles 221 and 201 of the FTC – see after 3.2 Transition regulation for the tax consequences of such cessation of business). Therefore, the listed parent company and its elected subsidiaries must file a specific cessation tax return.

The election is irrevocable and takes effect as from the first day of the fiscal year during which it was realised. Once it is made, the eligible companies may not waive it. The election is also considered global because it applies to all the properties and shares in the qualifying partnerships (subject to Article 8 of the FTC) (see 3.2. Transition regulation for the consequences of the option).

In the event where income and gains deriving from directly held properties located abroad would not be exclusively taxable in the foreign jurisdiction where the property is located (under provisions of the applicable tax treaty), the SIIC election would apply to such properties. However, these properties, upon specific election, may definitely be excluded from the SIIC regime, either (i) on the date of the election for the SIIC regime, or (ii) on the date of their acquisition if later. In this case, the profits deriving from these excluded properties will then be treated as part of the SIIC taxable sector.

The revenues deriving from properties located abroad and exclusively taxable in the foreign jurisdiction where they are located (under provisions of the applicable tax treaty) do not benefit from the SIIC regime since such revenues are not liable to CIT in France.



## b. Legal form/Minimum share capital

Legal form	Minimum share capital
<ul style="list-style-type: none"> <li>- Joint-stock company and simplified stock company</li> <li>- Partnership limited by shares</li> </ul>	EUR 15 million (except for subsidiaries of a listed parent company opting for the SIIC regime)

### Legal form

The parent company opting for the SIIC regime must be a corporation (*Société Anonyme*) or any other company whose capital is divided into stocks (*actions*) that can be listed (e.g. *Société en Commandite par Actions*). The SIIC regime does not require that the parent company be incorporated under French law or be a tax-resident in France. Indeed, the parent company can be a foreign company whose running and functioning rules are similar to the French SIIC regime.

Foreign companies which are listed on an EU-regulated stock exchange (or in any stock exchange functioning under the same rules as EU-regulated stock exchanges) and which comply with other SIIC conditions may elect for the SIIC regime as a parent with respect to their French direct or indirect qualifying operations. In order to be eligible for the SIIC regime, the French tax authorities require that the foreign company has a permanent establishment in France and is subject to French corporate income tax. The foreign company's French assets and shares of qualifying French subsidiaries are recorded as assets of the branch for French tax purposes.

In order to qualify for the SIIC regime, the subsidiary company must (i) be subject to French corporate income tax, either due to its legal form or pursuant to a tax election; (ii) be at least 95% directly or indirectly held by one or several listed SIIC parent companies having validly elected for the SIIC regime during the entire financial year in which the SIIC regime was applied for or together by one or several SIIC and one or several SPICAV (or foreign companies subject to a similar tax regime); and (iii) have a SIIC activity (see after 2.4 Asset level/activity test).

### Minimum share capital

The share capital of the listed parent company must amount to at least EUR 15 million. This condition is not applicable to the subsidiaries of a listed SIIC or of one or several SPICAV (or foreign companies subject to a similar tax regime) which elect for the SIIC regime under the conditions exposed above.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- Shareholders must not hold more than 60% of share capital or voting rights except for subsidiaries of a SIIC parent company</li> <li>- At the time of the election, 15% of the share capital and voting rights must be held by shareholders, who individually own fewer than 2%</li> </ul>	Yes

### Shareholder requirements

A single shareholder (other than a SIIC parent) or a group of shareholders acting jointly (*agissant de concert*) pursuant to article L. 233-10 of the French Commercial Code (i.e. persons who have entered into an agreement in order to buy or sell voting rights, or to exercise voting rights aiming to implement a policy in relation to a company) must not hold, either directly or indirectly, more than 60% of the share capital or voting rights of the listed parent company. This '60% shareholders test' must be met on a

continuous basis (temporary breaches resulting from takeovers, exchange offers, mergers or conversions or redemptions of bonds into shares are allowed subject to conditions).

Failure to the 60% shareholder test leads to the suspension of the SIIC tax regime. If the 60% condition is fulfilled again before the end of the fiscal year, the SIIC regime can apply again as from the opening of the next fiscal year, and the suspension of the regime consists in a cessation of business (see after, 3.2 Transition regulations). In addition, a permanent failure to the 60% shareholder test (i.e. including after the closing of the fiscal year) leads to the exit of the SIIC regime (see after, 2.7 Sanctions in the case of breach of SIIC regime conditions).

However, such ‘60% shareholders test’ do not apply to the fraction of the SIIC’s capital share owned by (i) another French SIIC or (ii) a foreign company whose functioning and tax regime are similar to French SIICs’ ones, under the condition such companies are not acting jointly.

At least 15% of the listed parent company’s share capital and voting rights must be held by shareholders who individually own, directly or indirectly, less than 2% of such share capital and voting rights. This condition aims to ensure a minimum level of free float before the company can elect for the SIIC regime. It only has to be met on the first day of the first year of application of the SIIC regime (and no longer after that date).

## Listing requirements

The parent company must be listed on an EU or EEA-regulated stock exchange. It can also be listed on any stock exchange under the condition the functioning rules of this stock exchange are the same as EU and EEA’s ones (European directive 2004/39/CE).

### d. Asset level/activity test

#### Restrictions on activities/investments

- Principal activity restricted to property acquisition and/or construction with the aim of renting, out the property as well as direct or indirect portfolio investments in partnerships (sociétés de personnes) or other companies liable to corporate income tax, having business activities and goals similar to the SIIC
- No required asset level
- Ancillary activities must not exceed 20% of the company’s assets gross book value

In order to be eligible for the SIIC regime, the principal activity of the company must be restricted to property acquisition and/or construction with the aim of renting out the property as well as direct or indirect portfolio investments in partnerships (sociétés de personnes) or other companies liable to corporate income tax, having business activities and goals similar to the SIIC. The eligible rental activities are those realised for residential, commercial or industrial purposes. Such activities can be either carried out in France or abroad and will only benefit from the SIIC regime under the condition they are, in principle, taxable in France (see before, 2.1).

The listed parent company and its subsidiaries may also engage in activities other than just passive investments. However, these activities must remain ancillary to the principal qualifying activity. Income from these activities is fully taxable under standard corporate income tax rules. Qualifying ancillary activities are most notably comprised of the following:

- the financial leasing of properties (crédit-bail immobilier) provided that the net book value of the outstanding portfolio of the properties does not exceed 50% of the total gross asset value of the company. This applies to entities that are lessor; and

- other activities such as real estate development or real estate brokerage provided that the gross book value of the relevant assets does not exceed 20% of the total gross asset value of the company. For the purpose of this 20% test, the value of properties subject to finance leases is disregarded. If these qualifying ancillary activities are performed through subsidiaries, then only the book value of the participation and current-account receivables would be considered for the purpose of the 20% test.

If the SIIC parent company or subsidiary entered into a financial lease for a building as lessee that is sub-let to tenants, this activity is considered as an eligible activity no matter if the SIIC entered into the financial lease before or after January 1, 2005. Nevertheless, only revenues deriving from financial leasing contracts entered into after January 1, 2005, benefit from the corporate tax exemption (i.e. are eligible for the SIIC regime).

The exploitation of a parking lot qualifies as an eligible activity only when the parking lot constitutes an ancillary of an eligible real estate rental activity.

The regime is also applicable with respect to assets which the listed parent company and elected subsidiaries enjoy a usufruct right to, or which they leased under certain long-term leases (baux emphytéotiques) or building leases (baux à construction).

The qualifying activity may be conducted outside of France, either directly or through subsidiaries.

The listed parent company's subsidiaries electing for the SIIC regime must have the same business purpose as SIICs.

The SIIC regime may also apply to the listed parent company's shares in a partnership if such partnership has a corporate business purpose identical to a SIIC's. There is no percentage participation requirement with respect to partnerships that engage in qualifying activities.

It is possible to create joint ventures between two SIIC groups. Indeed, as mentioned above, a subsidiary subject to corporate income tax may elect for the SIIC regime when at least 95% held by one or several listed companies that have themselves elected for the SIIC regime.

## e. Leverage

### Leverage

Several French rules limit the deduction of financial expenses (e.g. maximum deductible tax rate, thin capitalisation rules, anti-hybrid mechanism, new thin capitalisation and general interest deduction limitation from the Finance Act of 2019)

The French SIIC regime does not provide for specific leverage restrictions. However, French several interest deduction limitation rules apply to companies that have elected for the SIIC regime, affecting their tax-exempt income, which is subject to profit distributions obligations (see paragraph 2.6 below).

First of all, the deduction of interests paid to a shareholder is limited at a rate not exceeding the annual average rate of interest charged by financial institutions on variable interest rate loans to enterprises with a duration exceeding two years (article 39, 1-3° and 212 (I) of the French tax code). The maximum tax rate is determined by the Central Bank of France and published every trimester in the Official Journal (for companies having a fiscal year corresponding to the civil year, the rate was 1.47% for 2018). This limitation applies to all shareholders. Related companies (under the definition of article 39, 12° of the French tax code) may deduct a higher interest paid if (i) it corresponds to the rate that the company could obtain from an independent financial institution under similar circumstances and (ii) if duly documented. In this framework, the proof of the arm's length character of the practised rate if higher than the maximum rate of the year can be provided by any mean. Nevertheless, the French Tax Authority considers that the only documentation to be accepted is an offer from an independent financial institute for a similar loan

(notably in terms of the amount of capital, duration and interest) and of the same date the intragroup loan was settled.

A specific anti-hybrid financing provision applying to loans granted by affiliated companies of the borrowing company (article 212 (I)(b) of the French tax code). Under this provision, a French borrower is not allowed to deduct the interest when the lender is not liable for the interest income to a corporate income tax equal to at least 25% of the ordinary French corporate income tax.

Due to this rule, subsidiaries of SIIC may suffer a non-deduction of interest relating to loans granted by the SIIC parent company or its subsidiaries having elected for the SIIC regime if such interest is not regarded as affected to a taxable sector at the lender level (according to the French administrative doctrine, the burden of the proof of such affectation to the taxable result of the lender falls on the borrower).

In the application of the Finance Act for 2018, the ordinary French corporate income tax will progressively reduce to 25% by 2022, as follows:

Fiscal years opened as from:	Turnover	Proportion of the taxable result (in EUR)	Corporate income tax rate applicable
January 1, 2018	No matter the turnover	Up to 500.000	28% (28.92% with social contributions)
		Beyond 500.000	31% (32.02% with social contributions)
January 1, 2019	Up to 1 billion	Whole income	28% (28.92% with social contributions)
	Beyond 1 billion	Up to 500.000	28% (28.92% with social contributions)
		Beyond 500.000	31% (32.02% with social contributions)
January 1, 2020	No matter the turnover	Total taxable result	28% (28.92% with social contributions)
January 1, 2021	No matter the turnover	Total taxable result	26.5% (27.37% with social contributions)
January 1, 2022	No matter the turnover	Total taxable result	25% (25.83% with social contributions)

A reform of the rules on the deductibility of financial expenses has been settled by the Finance Act for 2019. From a general standpoint, the former thin capitalisation rules and the general interest deduction limitation on the net financial expense have been merged into one scheme.

In application of the article 34 of the French financial law for 2019, codified at the article 212 bis of the FTC, the companies subject to CIT should limit the deduction of the net financial expenses at the highest amount of EUR 3 million and 30% of the tax result retreated (hereinafter 'Tax EBITDA') or at the highest amount of EUR 1 million and 10% of the Tax EBITDA if they are thin-capitalised. The financial expenses added-back can nevertheless be carried over to the following fiscal years.

In this framework, the financial expenses (after the application of the mechanism of the limitation of financial expenses rate, FTC article 212 (I)) and financial products means interests on all forms of debt to interests of any form of debt (i.e. financial interests related to sums of money left or put at the disposal

of the company or by the company). This includes notably payments under profit-participating loans, alternative financing arrangements, notional interest amounts under derivative instruments or hedging arrangements, financial leases, etc.

In this framework, a company should be considered in a thin capitalisation position when its total debt towards related entities exceeds one and a half its equity (fonds propres).

Nevertheless, a safe harbour clause shall apply in such a case. Indeed, a company of which the amount of debts exceeds 1.5 times the amount of equity (fonds propres) is not in a situation of thin capitalisation if demonstrated that its debt ratio at its stand-alone level is lower than the same ratio determined at the level of the consolidated group to which it belongs. As such, the company's debt ratio will be considered equal to that of the consolidated group if its ratio is higher than that of the group by a maximum of 2% (French financial law for 2019, article 34, 5°, VII, 3°).

For the application of this safe harbour clause, the perimeter of the consolidated group and the ratio should be determined from the data published in accordance with the French standards relating to the preparation of annual and consolidated accounts or the other international accounting standards adopted in the European Union (IFRS). It results in this precision of the law that only companies which published consolidated accounts can benefit from the safe harbour clause. In addition, only fully consolidated companies (global integration) must be included in the consolidated group as defined for the new mechanism purposes.

At the date of the publication of the financial law for 2019, the law does not provide with a definition of the Equity (Fonds Propres). In such way, meanwhile, the publication of the comments of the French tax authorities on the new mechanism of limitation of the deductibility of the financial expenses, the equity accounting definition should be used for the application, of the mechanism.

Provided the company is not in a thin-capitalisation position, when the net financial expenses are lower than EUR 3 million or 30% of its tax EBITDA, no limitation of deduction will be applied according to the new mechanism.

We note that the text foresees the possibility to carry forward and over a period of 5 fiscal years the deduction capacity unused as regards the tax EBITDA of the fiscal year. This capacity corresponds to the spread between (i) the maximum between EUR 3 million and 30% of the tax EBITDA and (ii) the net financial expenses of the financial year.

Companies member of an accounting consolidated group and not in a thin capitalisation position benefit from an additional deduction of 75% of the net financial expenses exceeding the regular threshold, provided that the equity-to-asset ratio of the company is at least equal to, or is not lower, than more than 2% than the same ratio determined at the level of the consolidated group.

A thin-capitalised entity must determine two bases of net financial expenses, each subject to its own rules of deduction.

- The first base corresponds to the portion of interest on (i) debts towards unrelated parties and (ii) towards related entities which do not exceed 1.5 times the equity (fonds propres).
- The second base corresponds to the portion of interests for the debts towards related entities exceeding 1.5 times the equity (fonds propres).

As regards the first base of financial expenses, the portion of financial expenses will be deductible on a prorated basis of 30% of the tax EBITDA, or EUR 3 million (standard limit). As regards the second base, the portion of financial expenses will be deductible on a prorated basis of 10% of the tax EBITDA, or EUR 1 million (strengthened limit).

In addition, a deferral mechanism of added-back financial expenses and a carry forward of unused deduction capacity are included in the new mechanism.

## f. Profit distribution obligations

Operative income	Capital gains	Dividends	Timing
95% of tax-exempt profits	70% of capital gains	100% of dividends	See below

### Operative income

At least 95% of the tax-exempt profits realised during tax years closed as from December 31, 2013, derived from qualifying leasing activities (including profits realised by directly owned partnerships or pass-through entities), must be distributed before the end of the tax year following the year in which they are generated. Formerly, this distribution obligation was 85% of these tax-exempt profits.

### Capital gains

At least 70% of the capital gains realised during tax years closed as from December 31, 2018, resulting from the sale of (i) rights relating to leasing contracts regarding real estate assets, (ii) properties (including the sale of properties by directly held partnerships or pass-through entities), (iii) shares of qualifying partnerships or (iv) shares of corporate subsidiaries that have elected for the SIIC regime (including the sale of shares by a directly held partnership or a pass-through entity) must be distributed before the end of the second tax year following the year in which they have been realised. Formerly this distribution obligation was 60% of these tax-exempt gains (and 50% before 2013).

As from December 31, 2018, The 2019 Finance Act has increased the profit distribution obligations on capital gains realised during financial year closed from 60% to 70%. The capital gains realised during financial years closed before this date remain subject to the 60% distribution obligation.

### Dividends

100% of the dividends received from SIIC's subsidiaries which have elected for the SIIC regime must be distributed before the end of the tax year in which they are levied by the SIIC parent company.

### Incomes arising from partnerships

Incomes arising from partnerships are deemed to be directly realised by the parent SIIC company and benefit from the tax exemption under the same distribution obligations. Thus, these incomes are spread between (i) qualifying rental activities, (ii) sale of properties previously used for qualifying activities and (iii) dividends received from subsidiaries which have elected for the SIIC regime. Distribution obligations are then determined for each type of activity by applying the corresponding rate.

### Limitation and capping of the distribution obligations

SIIC's total distribution obligations for a financial year (i.e. the sum of the distribution obligations of the three sectors) are limited to the company's total tax result of this financial year eligible to the tax exemption. The surplus distribution obligations do not have to be distributed. French law and administrative doctrine are not clear on whether the distribution obligations exceeding this first limitation must be carried forward or not for the computation of the future distribution obligations of the SIIC.

Moreover, the SIIC's distribution obligations for a financial year are capped at the financial year's accounting result (i) decreased by previous accounting losses and the sums allocated to the legal reserve and (ii) increased by the retained earnings. When the total distribution obligations exceed this retreated accounting result, the surplus is deferred on the first following profitable year and the following ones.

#### g. Sanctions in case of breach of SIIC regime conditions

##### Penalties/loss of status rules

- Profit and gain exemption is denied for the financial year in which the distribution shortfall appears or when the exit occurs
- In the case the SIIC leaves the status within ten years following the SIIC election, unrealised capital gains subject to the exit tax upon the election for the SIIC status are subject to corporate income tax at the standard rate (after deduction of the 16.5% or 19% exit tax paid at the time of the election for the SIIC regime) and unrealised capital gains accrued during the period of the SIIC election must be taxed at a 25% tax rate

#### Sanctions in case of distribution obligations shortfall

If a SIIC company does not meet its distribution requirements, profit and gain exemption is denied for the financial year in which the distribution shortfall appears.

Moreover, if the French tax authorities were to conduct a tax audit and reassess exempt profits or gains, the reassessed result would be fully taxable because it would not have been distributed in due time. However, the reassessed amount should not be considered taxable for the portion already covered by previous distribution in excess of the minimum distribution obligations. In any case, such reassessment would not question the benefit of the tax exemption regime for the corresponding year.

#### Sanctions in case of a breach of the eligibility conditions

The exit from the SIIC regime occurs if the following conditions are no longer met:

- (i) minimum capital share, (ii) market listing, (iii) object condition, during the ten years following the option conditions; and
- 60% cap of majority ownership condition.

Such exit also causes the exit of the SIIC Parent Company's subsidiaries.

If the listed parent company no longer fulfils the conditions for the SIIC regime within ten years following the SIIC election, then:

- The distributable income previously exempted from corporate income and existing at the date of the exit is subject to CIT under the general conditions and the standard rate.
- Unrealised capital gains on its real estate assets that had been subject to corporate income tax at the reduced 'exit tax' rate (19% since 2009, 16.5% before) at the time of entry into the SIIC regime become subject to corporate income tax at the standard rate applicable during the year of the exit (see paragraph 3.2 below). For fiscal year 2019, this rate is 31% plus the additional surcharges of 3.3% making an effective tax rate 31.02%, after deduction for the 19% (or 16.5%) exit tax paid at the time of entry into the SIIC regime (Article 84 of the French financial law for 2018 provides for the reduction of the French corporate income tax rate progressively to 25% by 2022).
- Unrealised capital gains accrued during the period of the SIIC election on the real estate assets are taxed at a special rate of 25% (subject to a rebate of 10% per civil year passed since the election for the SIIC regime);



If the listed parent company no longer fulfils the conditions for the SIIC regime more than ten years after the SIIC election, the exit of the SIIC regime should take effect as from the opening of the fiscal year during which the exiting event occurred and does not impact the benefit from the SIIC regime for the previous years (e.g. the exit does not entail additional CIT charge on the SIIC revenues exempted from CIT during the application of the SIIC regime).

Should one of the qualifying subsidiaries that elected for the SIIC regime no longer fulfil the conditions, it would lose the benefit of the leasing profits and gains exemption as of the beginning of the financial year in which the loss of status takes place, regardless whether such exit happens during the ten years following the date of election or later. This could occur if, for example, more than 5% of its capital shares are sold to an unrelated entity that is not a SIIC parent.

A specific mechanism applies when a SIIC does not meet the 60% shareholder test for a limited period of time (when that period is exceeded then the SIIC definitively exits the regime).

In the case of a merger or acquisition of one SIIC by another SIIC, the exemption regime remains valid insofar as the distribution conditions are executed by the acquirer. In the case of acquisition, the target SIIC parent, which becomes a subsidiary as a result of that acquisition, must remain subject to the SIIC regime (as a subsidiary) for the remainder of the ten-year period from its own election as SIIC parent.

According to the French Administrative doctrine, in the case of a reassessment of the tax-exempted result by the French tax administration, the amount of the reassessment that was not distributed is subject to corporate income tax under the general conditions.

### 3 Tax treatment at the REIT level

#### a. Corporate income tax

Election	Current income	Capital gains	Withholding tax
Cessation of activity (see after: 3.2)	Eligible income is tax-exempt	Eligible capital gains are tax-exempt	<ul style="list-style-type: none"> <li>- In principle, domestic sourced income is not subject to withholding tax</li> <li>- The taxes withheld on foreign-sourced income could be credited if a double tax treaty allows</li> </ul>

#### Current income

The listed parent company and its qualifying corporate subsidiaries that have elected for the SIIC regime are, in principle, subject to French corporate income tax.

However, the following income is fully exempt from corporate income tax, provided that the distribution requirements are met:

- Income realised directly or through qualifying partnerships from qualifying leasing activities. The exemption regime is applicable to financial lease contracts (i) entered into force after January 1, 2005 when the SIIC company is the lessee, (ii) to sublease agreements regardless the date of conclusion of the initial financial lease and (iii) to certain long-term leases (baux emphytéotiques) or building leases (baux à construction);
- Dividends received from qualifying subsidiaries that have elected for the SIIC regime, and paid out of the tax-exempt income of such subsidiary;

- The listed parent company may also benefit from the dividend exemption in respect of dividends received from (i) another SIIC, (ii) or a SPICAV or (iii) a foreign REIT, provided the listed parent company holds at least 5% of the distributing entity's capital shares and voting rights for at least two years.

## Capital gains

Capital gains arising from the sale or disposal of properties used for qualifying leasing activities, from the disposal of participation in qualifying partnerships or other pass-through entities, or from disposal of participation in qualifying corporate subsidiaries that have elected for the SIIC regime are fully tax exempt.

Capital gains are only considered tax-exempt if the acquirer is unrelated to the seller (under the definition of a related company given by article 39, 12 of the French tax code). Two entities are considered to be related to each other if one of the two directly or indirectly holds the majority of the capital shares of the other (or has de facto control), or if both of the entities are directly or indirectly under control of the same entity.

The straight sales of properties among members of the same SIIC group or between members of a SIIC group and a SPICAV may, however, benefit from an exemption under certain conditions (with a rollover of the tax basis). In this respect, the tax treatment of the capital gain allocated to buildings will differ from the one allocated to land:

- Non-depreciable assets (e.g. land): for tax purposes, the acquirer takes over sellers' basis. Capital gain upon a subsequent sale would therefore, for tax purposes, be computed from this rolled-over tax basis, which will increase the 70% distribution obligation;
- Depreciable assets (e.g. construction): for tax purposes, the acquirer has a stepped-up tax basis. However, the gain recognised in the transaction must be recaptured in the tax-exempt rental income (over 15 years generally, or over the residual useful life if construction represents more than 90% of the value of the depreciable assets). This recapture increases the exempt income and therefore the amount of the compulsory 95% distribution, which in practice offsets the increased depreciation allowances (which themselves reduce the exempt income and the distribution obligation).

## Incomes arising from partnerships

Incomes arising from partnerships are deemed to be directly realised by the parent SIIC company and benefit from the tax exemption under the same distribution obligations. Thus, these incomes should be spread between the different revenues of the parent SIIC for the computation of the distribution obligations.

## Contribution on payment of dividends

Dividends paid by the listed parent company used to trigger a 3% additional contribution to corporate tax at the level of the distributing company (article 235 ter ZCA of the French tax code). The Amending Finance Act for 2013 provided for an exemption from this contribution for dividends distributed by the listed parent company up to the amount distributed in accordance with the SIIC distribution requirements.

The French Constitutional Council recently declared the 3% surcharge on dividends contrary to the French Constitution and thus, repealed this tax as of the date of its decision (Cons. Const. n°2017-660 QPC October 6, 2017). As a consequence, the Finance Act for 2018 abrogated the 3% contribution on dividends as from January 1, 2018. Depending on the payment date and if conditions are met, the surcharge paid before this date may be claimed back in front of the courts.

## Withholding tax

If a French listed company or a subsidiary receives foreign source income that is subject to French corporate income tax, the tax withheld could be credited if a double tax treaty allows. There is no actual cash refund for foreign tax withheld. In principle, outbound dividends paid by a SIIC to French tax residents are not subject to a withholding tax.

## Accounting rules

The French *Comité de la Réglementation Comptable* adopted a Resolution on December 12, 2002 (Regulation CRC, December 12, 2002, n°2002-10) which devoted a large section of IFRS relating to depreciation and impairment of assets under French GAAP. French companies are required to prepare financial statements in accordance with these rules as from January 1, 2005. Accordingly, French SIICs are also subject to the French GAAP rules regarding depreciation and property impairment.

### b. Transition regulations

#### Conversion into REIT status

- Exit tax payment
- Tax losses carried forward are deductible from the exit tax basis, within certain limits
- Remaining losses are cancelled

As a result of the SIIC election, the listed parent company and its electing subsidiaries experience a cessation of activity and a tax regime change. Under ordinary tax rules, this would trigger immediate taxation of deferred profits and unrealised capital gains. Upon the transition, the following tax rules apply:

- The election for the SIIC regime triggers liability for an exit tax at a rate of 19% (16.5% before 2009) on unrealised capital gains on real estate assets and on interest in qualifying real estate partnerships owned by the listed parent company and its corporate subsidiaries electing for the SIIC regime. This exit tax is payable in four instalments (every December 15 for the first four years after the election). Conversely, there is no taxation of the unrealised capital gains on participation held in qualifying corporate subsidiaries. However, there is a rollover of tax basis on these gains;
- The unrealised capital gains on other assets are tax-exempt when attributed to an ancillary activity, but subject to a rollover tax basis;
- Prior tax losses, if any, may be offset against such cease of activity result but the surplus cannot be used in the future (i.e. cannot be offset against the taxable or non-taxable result of the SIIC and will not be available in the situation of an exit of the SIIC regime).

The SIIC regime election does not trigger any taxation at the shareholder level.

### c. Registration duties

#### Registration duties

- Notary and land security fees
- VAT and/or registration duties

NB: The rules described below are not SIIC-specific.

The French tax costs arising from property acquisition are:

- Notary fees equal to 0.814% of the property purchase price (proportional rate depending on the value of the immovable asset acquired) with a possible maximum 40% rebate for the part of the property exceeding EUR 10 million (as for non-residential properties).
- Land security fees amounting to 0.1% of the purchase price of the property;
- Depending on the nature of the property, either (i) a 20% VAT plus a 0.715% reduced registration duty for real estate completed or renovated less than five years before the transfer date, or (ii) VAT exemption and registration duties at the standard 5.8% rate (5.09% in a few locations) (plus an additional tax on registration duties of 0.60% in the case of a transfer of office premises, commercial premises or warehouses located in the Ile-de-France region).

Property acquisition is either subject to VAT or registration duties in France:

- Pursuant to article 257 of the FTC, the French standard VAT of 20% applies on the stipulated price (or current value if greater) to transfers of real estate that have been completed or renovated less than five years before the considered sale. In such a case, the 0.715% reduced registration duty rate applies.
- Sales of other real estate (not built or renovated less than five years before the sale date) are exempt from French VAT and subject to French registration duties at a rate of 5.8% (5.09% in a few locations).
- Sales of building lands are subject to 20% VAT on (i) the stipulated price or (ii) the seller's margin, depending on whether the seller deducted VAT burden on his acquisition or not. These sales are subject to French registration duties at the 5.8% rate when VAT applies to the seller's margin and 0.715% rate when VAT applies on the stipulated price.
- Sales of other lands are exempted from VAT (with the possibility for the seller to opt for the VAT as regards the sale of the land) and subject to 5.8% registration duties.

The acquisition of shares or interests in French predominantly real estate subsidiaries or partnerships (sociétés à prépondérance immobilière) is subject to registration duties at the rate of 5% assessed on the sale price of the transferred shares or interests.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholders

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Dividends and capital gains are taxed at the standard rate (for 2019: 31% plus surcharges)</li> <li>- Return of capital is normally tax-free</li> </ul>	<ul style="list-style-type: none"> <li>- Capital gains and dividends are subject to French income tax, as from January 1, 2018, through a flat withholding tax of 30% (12.8 % + 17.2 % social contributions)</li> <li>- The return of capital is normally tax-free</li> </ul>	15% withholding tax may apply as regards dividends paid-out of the tax-exempt income by the listed parent company

### Corporate shareholders

The tax treatment of French corporate shareholders receiving dividends from a SIIC differs depending on whether the dividends are paid out of taxable or tax-exempt income and gains.

Dividends paid out of the tax-exempt income and gains are fully subject to French corporate income tax at the standard rate. They are not eligible for an exemption pursuant to the domestic parent-subsidiary regime.

Dividends paid out of the taxable portion are also subject to corporate income tax at the standard rate. However, if the qualifying parent companies hold at least 5% of the shares of the SIIC for at least two years, it could be eligible for the domestic parent subsidiary 95% dividend exemption.

A return of capital is normally tax-free. Any reduction of share capital or the distribution of share premium will be treated as a tax-free return only to the extent that all reserves or retained earnings have already been distributed. The latter condition does not apply in the case of share redemption.

Capital gains earned on the sale of the listed parent company shares are subject to corporate income tax at the standard rate (for 2019, the standard corporate income tax rate is 31% - effective tax rate of 32.02% for companies liable to the additional corporate income tax contribution of 3.3%). In addition, article 84 of the French Financial Act for 2018 provides for the reduction of the French corporate income tax rate progressively to 25% by 2022.

The rate could be reduced to 19% (effective tax rate of 19.63% or 21.66% for companies liable to the exceptional corporate income tax surcharge) pursuant to the long-term capital gain tax regime if the shares have been held for at least two years and can be considered qualified participation (e.g. treated as participating shares for accounting purposes, which is presumed in the case of a detention exceeding 10% of the share capital).

## Individual shareholders

Finance Act for 2018 (of December 30, 2017) introduced a flat withholding tax as regards dividends paid to individual shareholders as from January 1, 2018, at a rate of 30% (i.e. flat rate of 12.8% increased by social contributions of 17.2%) (Article 200 A of the French tax code).

However, individual shareholders can opt for the former taxation regime, i.e. the progressive tax rates of personal income tax (up to 49%) and the social contribution at a total rate of 15.5%. In such a case, dividends paid out of the tax-exempt income and gains are subject to the income tax on their total amount and dividends paid out of the taxable income and gains are taxed on a basis of 60% of their amount.

French individuals deriving capital gains from the sale of SIIC shares are also subject to the 30% flat withholding tax and be subject, under election, to the progressive tax rate (up to 49%) and the social contribution at the rate of 15.5%. If such election is made, the capital gains may benefit from the mechanism of the progressive rebate on the taxable gain subject to personal income tax available after a two-year holding period. This rebate amounts to 50% for securities held less than eight years and to 65% for securities held at least eight years.

As for corporate shareholders, a return of capital distribution is normally tax-free. However, any reduction of capital shares or share premium distributions will be treated as a tax-free return of capital only to the extent that all reserves or profits have already been distributed. The latter condition is not applicable to share redemption.

## Withholding tax

In principle, dividends paid to French tax residents are not subject to a withholding tax.

However, a specific 15% withholding tax applies on dividends distributed by the listed parent company or its subsidiaries, having elected for the SIIC regime:

- to French public institutions, associations and non-profit sector; and
- to the following French collective investment vehicles (organismes de placement collectif): UCITS (OPCVM), real estate collective investment schemes (organismes de placement collectif immobilier) and closed-end investment companies (sociétés d'investissement à capital fixe), or to foreign collective investment vehicles fulfilling the conditions to benefit from the general exemption of withholding tax on dividends (see 4.2) when such dividends are paid out of the tax-exempt revenues.

Such withholding tax does not apply to dividend distributions paid out of tax-exempt revenues by subsidiaries of SPPICAVs or both SPPICAVs and SIIC Parent Companies, having elected for the SIIC regime to the French collective investment vehicles mentioned above.

Moreover, a 20% withholding tax applies on such dividends distributed to legal persons who (i) hold directly or indirectly at least 10% of the distributing company and (ii) are not subject to CIT. Nevertheless, the levy is not made whenever the beneficiary of the distribution is a company bound by an obligation to distribute all the dividends that it receives shall its shareholder holding directly or indirectly at least 10% of the beneficiary capital be subject to CIT on such distributions.

This withholding tax is not in lieu of corporate or personal income tax and may neither be offset nor refunded.

### b. Foreign shareholders

Corporate shareholder	Individual shareholder	Withholding tax
Withholding tax on dividends	Withholding tax on dividends	<ul style="list-style-type: none"> <li>- Generally 30% withholding tax (or a reduced treaty tax rate)</li> <li>- EU Parent-Subsidiary Directive not applicable</li> </ul>

### Corporate and individual shareholders

Under French national laws, dividends distributed by a French parent company or a qualifying subsidiary having elected for the SIIC regime to non-resident shareholders are subject to a withholding tax at the rate of 30%. If the shareholders are residents of a treaty country, they may, however, benefit from an exemption or a reduced withholding tax rate which is generally equal to 15% and such withholding tax is often creditable against the income tax liability in their home jurisdiction.

However, the latest tax treaties concluded by France provide for specific provisions relating to distributions by REITs as advised by the OECD in the report Tax treaties issues related to REITs dated October 30, 2007, included in the 2008 update of the model tax convention.

According to these provisions, the tax treaty reduced rates of withholding tax do not apply to dividends paid out of income or gains derived from immovable property by an investment vehicle:

- which distributes most of its income annually; and
- whose income and gains from such immovable property are exempted from tax.

Where the beneficial owner of these dividends holds, directly or indirectly, 10% or more of the capital of the vehicle paying dividends.

In such a case, the dividends may be taxed at the rate provided for by French domestic law, i.e. at 30%. The 15% tax treaty withholding tax rate is thus applicable only for small investors – i.e. when the beneficial owner holds fewer than 10% of the capital of the vehicle.

France has included this provision in the tax treaties recently concluded (among others) with the United Kingdom (tax treaty dated June 19, 2008), Panama (tax treaty dated June 30, 2011), Andorra (tax treaty dated April 02, 2013), China (tax treaty dated November 26, 2013), Singapore (tax treaty dated January 15, 2015), Germany (tax treaty dated March 31, 2015) and Colombia (tax treaty dated June 25, 2015).

The 30% withholding tax does not apply to dividend payments made by a French parent company to collective investment vehicles established on the basis of foreign law located in a Member State of the EU or in another state or territory that has concluded with France a convention on administrative assistance in order to fight against tax fraud and evasion, and which fulfil both the two following conditions:

- raising capital from a number of investors in order to invest in accordance with a defined investment policy in the interests of these investors;
- presenting characteristics similar to those of the following French collective investment vehicles (organismes de placement collectif): UCITS (OPCVM), real estate collective investment schemes (organismes de placement collectif immobilier) and closed-end investment companies (sociétés d'investissement à capital fixe), etc.

However, according to the French tax authorities' doctrine, a specific 15% withholding tax is due when these dividend distributions are paid out of tax-exempt revenues under the same conditions as exposed previously in section 4.1.

EU corporate shareholders are not eligible for the withholding tax exemption pursuant to the EU Parent-Subsidiary Directive to the extent that the dividends are paid out of the tax-exempt revenues.

A return of capital is normally tax-free. However, any capital share reduction or share premium distribution will be treated as a tax-free return of capital only if all reserves or profits have already been distributed. This latter condition does not apply in the case of share redemption.

Capital gains realised on the sale of the listed parent company shares are taxable in France at a flat rate of 19% (for all non-individual shareholders irrespective of their State of residence and corporate shareholders EU resident or resident of a State member of the EEA which has concluded with France a convention on administrative assistance in order to fight against tax fraud and evasion)

In the case of a substantial participation (at least 10%), capital gains realised on the sale of the listed parent company shares are taxable at the normal corporate income tax rate (for 2019, 31%), when the listed parent company's asset is mainly composed of immovable properties and related rights located in France. Such tax treatment is subject to a double tax treaty.

There are uncertainties as to whether capital gains on the sale of the listed parent company shares are taxable in France when the seller holds less than a 10% participation.

Capital gains realised on the sale of qualifying subsidiaries' shares that have elected for the SIIC regime are taxable in France at the standard rate and subject to a double tax treaty.



### c. Anti-abuse measures

#### Specific levy of 20%

Applicable to the dividends paid by the parent company to domestic or foreign shareholders under certain circumstances

The specific levy regime applicable to domestic distribution paid to exempted beneficiaries (see before, 4.3) also applies under certain circumstances to the dividends paid by the parent company to foreign shareholders.

The parent listed company must assess and pay a 20% levy in respect of the dividends distributed if the beneficiary of the dividends (i) is a French or foreign taxpayer other than an individual (ii) which holds, directly or indirectly, at least 10% of the financial rights of the parent company at the payment date, and (iii) which is either exempt from any corporate tax on the dividends or subject to tax thereon at a low rate (i.e. a rate lower than a third of the corporate income tax rate).

## 5 Tax treatment of foreign REITs and its domestic shareholders

Foreign REIT	Corporate shareholder	Individual shareholder
Election for SIIC regime is possible	Same treatment as domestic shareholders of SIIC	Same treatment as domestic shareholders of SIIC

### Foreign REIT

In principle, the double tax treaties state that the income and gains deriving from property located in a foreign State are taxable in that foreign State.

Accordingly, the rental income of a foreign company is taxed in France as long as the relevant properties are located in France. In this respect, the foreign company can benefit from the SIIC exemption regime if it meets the applicable conditions and if it has validly elected for the SIIC regime (notably, the parent company and its corporate subsidiaries meet the SIIC requirements, see *supra* 2.2, 2.3 and 2.4). ■

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EUROPE

# Germany

G-REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
G-REIT	2007	Law on German real estate joint-stock companies with publicly quoted shares (Real Estate Investment Trust law – REIT law)	Corporate type

After intensive three-year political discussions, Germany implemented the German Real Estate Investment Trust (G-REIT) in 2007 in order to meet the market demands inspired by the introduction of the REIT in other European countries. The G-REIT is a joint-stock company with specific rules laid out by the REIT law.

The REIT law came into force on June 1, 2007, with retroactive effect as of January 1, 2007. The REIT law is supported by changes in various tax laws, such as the German Income Tax Act and the Investment Tax Act. The REIT law has been amended by the Tax Amendment Act 2009 (Jahressteuergesetz 2009) and the UCIT IV Transformation Act in 2011 (OGAW IV Umsetzungsgesetz). One of the major changes was that shareholders may benefit from the privileged taxation generally applicable for dividend income if such dividends are sourced by pre-taxed profits of the G-REIT and certain further requirements are fulfilled. However, for corporate shareholders of a G-REIT, this privileged taxation has de facto been abolished (see under section 4.1).

The tax authorities published on July 10, 2007, administrative guidance according to which upon registration as a REIT with the Commercial Register; tax exemption is to be assumed to start with the beginning of the year of registration, and therefore upon application, no tax prepayments are to be assessed.

According to Sec. 1 (3) no. 5 Investment Tax Act 2018, the G-REIT does not qualify as an Investment Fund in the meaning of the law. The ITA 2018 is applicable as of January 1, 2018. For further details see Sec. 56 ITA 2018.

Up to now the following five REITs are listed: alstria Office REIT-AG, Hamborner REIT AG, Fair Value REIT, Deutsche Konsum REIT-AG and Deutsche Industrie REIT-AG. No company is registered at the Federal Central Tax Office (Bundeszentralamt für Steuern – BZSt) as pre-REIT.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Germany	5	2	EUR 4,241	0.25%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
alstria office REIT AG	EUR 2,526	14.81%	3.65%	0.20%
Hamborner REIT AG	EUR 718	3.94%	5.11%	0.05%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- G-REIT: Registration with the Commercial Register
- Pre-REIT: Registration with the Federal Central Tax Office

### G-REIT

The G-REIT must be registered with the Commercial Register which examines whether the G-REIT qualification requirements are met. The G-REIT comes into existence with its registration.

The main requirements for the registration of a G-REIT are as follows:

- joint-stock company with a minimum share capital of EUR 15 million;
- corporate seat and place of management in Germany;
- by-laws must provide for certain provisions (e.g. purpose of the company, compensation of shareholders with a shareholding of less than 3% in case of termination of the tax-exempt G-REIT status, etc.);
- listing at the stock exchange;
- at least 25% widely held shares at IPO (after listing reduced to 15%);
- direct shareholding of a shareholder must be less than 10%; and
- asset, equity and activity requirements (see under no. 2.4. and 2.5).

### Pre-REIT

Before registration with the Commercial Register, a pre-REIT status can be obtained. A pre-REIT can be characterised as a joint-stock company which does not yet have to fulfil all the requirements for a G-REIT. The Pre-REIT status requires registration with the Federal Central Tax Office. Similarly to the G-REIT, the Pre-REIT status allowed capital gains from the transfer of real estate to the pre-REIT to be subject to exit tax rules, which have since been abolished (see no. 2.3 “Listing requirements” and 3.2 “Transition regulations/Exit-Tax”). At the end of each business year following the year of registration, the pre-REIT must prove to the Federal Central Tax Office that its activities comply with certain G-REIT requirements.

For the registration as a pre-REIT the company must fulfil the following requirements:

- joint-stock company; and
- corporate seat in Germany.

The pre-REIT must fulfil at the end of the business year following the year of registration and each consecutive year the following requirements:

- objectives of the pre-REIT must be limited to the objectives of a G-REIT;
- 75% of its total assets must consist of immovable property;

- 75% of its gross earnings must be derived from renting, leasing, letting and disposal of real estate;
- a pre-REIT service company's assets may not exceed 20% of the pre-REIT's total assets; and
- a pre-REIT service company's gross earnings may not exceed 20% of the pre-REIT's gross earnings.

The assets and gross earnings requirements mentioned above must be verified by an auditor upon the request of the Federal Central Tax Office.

With the exception of the exit tax rules which are no longer applicable for purchases realised after December 31, 2009, the taxation of the pre-REIT follows the general tax rules applicable for corporations. As a consequence, there is no longer a need to obtain pre-REIT status.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Joint stock company	EUR 15 million

### Legal form

The only legal form which is permitted for a G-REIT is the joint-stock company (*Aktiengesellschaft* – AG). The company's name must include the words “*REIT-Aktiengesellschaft*” or any other reference, which contains the words ‘*Real Estate Investment Trust*’ or the abbreviation ‘REIT’. Because of its qualification as a joint-stock company, the G-REIT is subject to the standard regulations of the Joint Stock Company Act and the Commercial Code. This is the case unless the REIT Act specifically indicates otherwise.

### Minimum share capital

A G-REIT must have a share capital of at least EUR 15 million. All shares must be voting shares. Different categories of shares are not allowed. Shares can only be issued against the full payment of the issuance price.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- 15% of the shares must be widely held (25% at the time of IPO)</li> <li>- A shareholder is not allowed to own directly 10% or more of the shares or the voting rights of the company</li> </ul>	Yes

### Shareholder requirements

At least 15% of the G-REIT shares must be widely held, which means that such shares must be owned by shareholders who may each hold less than 3% of the voting rights of the G-REIT. Consequently, at least six shareholders are needed to satisfy this 15% requirement. At the time of the stock exchange listing, the precondition of widely held shares must be fulfilled for at least 25% of the shares of the G-REIT.

In addition, a single shareholder is not allowed to directly hold 10% or more of the shares or the voting rights of a G-REIT (including shares held on his/her behalf by a third party). However, this limitation is not applicable to an indirect shareholding. Consequently, holding structures legally allow circumventing this threshold.

At the end of each calendar year, the G-REIT is obliged to inform the Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstaufsicht) of the shares which are widely held. The Federal Financial Supervisory Authority will inform the Federal Central Tax Office if the 15% widely held shareholding requirement is not met. The REIT law provides for further reporting requirements which apply to a shareholding of 3%, 80% and 85% of the G-REIT's voting rights.

### Listing requirements

Securities Trading Law in a Member State of the European Union or in another signatory state to the Treaty on the European Economic Area (Iceland, Liechtenstein, Norway).

A pre-REIT must apply to be admitted to trading in an organised market mentioned above within three years of the application being made to register the joint-stock company as a pre-REIT. The time allowed may be extended twice, for one year each time on application by the Federal Financial Supervisory Authority if there are exceptional circumstances justifying such an extension. Should no application be made within the time allowed, or should an application be made within that time and be refused, the company will lose its status as pre-REIT.

#### d. Asset levels/activity test

##### Restrictions on activities/investments

- 75% immovable property requirement
- 75% immovable property income requirement

At least 75% of the total assets of the G-REIT must be comprised of immovable property and at least 75% of its gross earnings must derive from rental, leasing, letting and disposal of immovable property.

A G-REIT may only provide secondary activities (activities serving third party investment portfolio) via a 100% owned REIT service company. The assets related to such services are not allowed to exceed 20% of the total assets of the G-REIT. In addition, the gross earnings from such services are not allowed to exceed 20% of the gross earnings of the G-REIT.

A G-REIT must not engage in trading in real estate. Trading is assumed when the G-REIT receives revenues from the disposal of real estate within a period of five years which exceeds 50% of the average value of its real estate portfolio within that same period. The valuation of the real estate portfolio will be based on fair value as defined in IAS 40.

Investments in immovable property, which is used primarily (i.e. more than 50%) for residential purposes, are prohibited if the property is located in Germany and was built prior to January 1, 2007. The G-REIT may invest in all kinds of real estate abroad insofar as the real estate can be owned by a REIT corporation, REIT partnership or a REIT trust or a corporation, partnership or trust comparable to a REIT under the laws of the respective foreign country.

The G-REIT is allowed to hold German real estate via a German partnership, but not via a German corporation. A German corporation may only be held for such purposes if the company acts as an unlimited liable partner in a real property partnership without any participation in the property of the partnership (i.e. the corporation is a general partner and holds no interest in the real estate partnership.) This refers to the structure of a GmbH & Co. KG, which is a partnership with an unlimited liable partner corporation. The partnership must have the same business objectives as the G-REIT itself.

Foreign real estate may be held through a German or foreign property partnership as well as through a 100% owned German or foreign property corporation of the G-REIT.



## e. Leverage

### Leverage

The equity must equal at least 45% of the total asset value of immovable property (valuated at IAS 40)

The equity of the G-REIT, as generally shown in its consolidated accounts (if no obligation to consolidated accounts is existing, the single accounts are decisive) at the end of the fiscal year, must equal at least 45% of the total asset value of immovable property in the accounts (valued at IAS 40). As at least 75% of all assets at the end of each business year must be immovable assets, the equity must not fall below 33.75% of total assets. This means the leverage of a G-REIT cannot exceed 66.25%.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of the net income of the year	Deferral of 50% of the capital gains from real estate assets is allowed	Distribution is required until the end of the following business year

### Operative income

The G-REIT has to distribute at least 90% of its net income, calculated under German GAAP, to its shareholders until the end of the following business year.

### Capital gains

Up to half of the proceeds from disposals can be transferred to a reserve; distributable profits will be reduced accordingly.

Any unused reserves must be dissolved at the latest by the end of the second financial year after creation. The reserves can either be deducted from the acquisition or construction cost of real estate assets acquired or created in the respective two years or must be added to the distributable profits in the year in which they are dissolved.

## g. Sanctions

### Penalties/loss of status rules

- Several penalties
- Loss of REIT status

Penalties will be levied by the competent tax office as follows:

- if less than 90% of the gross earnings are distributed, the penalty amounts from 20% to 30% of the difference;
- if less than 75% of the assets consist of immovable property, the penalty amounts from 1% to 3% of the difference;
- if less than 75% of the gross earnings is derived from qualifying income, the penalty amounts from 10% to 20% of the difference; or



- if more than 20% of the gross revenue consists of real estate advisory or other related services to third parties, the penalty amounts from 20% to 30% of the earnings exceeding this threshold.
- If more than 20% of the gross revenue consists of real estate advisory or other related services to third parties, the penalty amounts from 20% to 30% of the earnings exceeding this threshold.

If for three consecutive years the G-REIT continuously violates one and the same qualifying requirement as defined by the REIT law, it will lose its status as a tax-exempt corporation after the end of the third year. If the G-REIT continuously violates different qualifying requirements over five consecutive years, it will lose its status as a tax-exempt corporation after the end of the fifth year.

If the G-REIT performs forbidden real estate trading activities, it will lose its status as a tax-exempt corporation with effect from the financial year in which the limit is exceeded.

If the G-REIT is de-listed, it will lose its status as a tax-exempt corporation at the end of the financial year prior to the year of de-listing.

If 10% or more of the shares or the voting rights of a G-REIT can be attributed directly to one shareholder, this will not cause the G-REIT to lose its tax-exempt status. Nor will the shareholder forfeit his dividend or voting rights. However, he would only be able to exercise the rights of a double tax treaty applicable for a shareholding of less than 10% of the G-REIT's shares.

If less than 15% of a G-REIT's shares are in free float for three consecutive years, the G-REIT will cease to be tax exempt from the end of the third year. The same applies if the aforementioned 10% threshold is violated for three consecutive years. These rules do not apply as long as the G-REIT cannot infer the breach from the notifications required under the Securities Trading Law.

### 3 Tax treatment at the level of the REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
All income is tax-exempt	Capital gains are tax-exempt	Reduced withholding tax on distributions to the G-REIT

#### Current income

The income of a G-REIT is not subject to corporate or trade income taxes irrespective of whether the income is generated from real estate assets or not. The tax exemption applies for the first time as of the beginning of the business year in which the G-REIT is registered as a REIT with the Commercial Register. The tax exemption only applies to the G-REIT's income.

Consequently, the income of a subsidiary or a partnership of the G-REIT (the latter is, according to German tax principles, only tax transparent for corporate income tax but not for trade income tax) remains subject to taxation at their level. In this context, it should be noted that German trade tax law provides under certain requirements for a trade tax exemption for income from real estate.

#### Capital gains

As in the case of the G-REIT's other income, capital gains are exempt from corporate and trade income taxes.

## Withholding tax

Dividend distributions from German subsidiaries of the G-REIT to the G-REIT are in the first place subject to the standard withholding tax of currently 25%, but two-fifth of this tax can be reclaimed by the G-REIT upon application.

## Other Taxes

Taxes other than income taxes will be levied. Specifically, real estate transfer taxes will be levied on the acquisition and sale of real estate.

## Accounting rules

The income is to be determined based on German GAAP. Real estate assets can only be depreciated using the straight-line method.

The thresholds which must be met by the G-REIT (see no. 2.4 and 2.5) are determined based on IFRS rules.

The financial statements of the G-REIT must be audited. The auditor must confirm inter alia that the threshold requirements were met.

### b. Transition regulations/Exit-Tax

#### Conversion to REIT status

The G-REIT law does not provide for a tax-free conversion

The G-REIT obtains tax-exempt status at the beginning of the taxable year in which the joint-stock corporation has been registered as a G-REIT in the Commercial Register. This event is treated as a taxable liquidation of the (prior) taxable joint-stock corporation. The conversion of a property company into a G-REIT is thus (always) a taxable event, and the REIT law does not provide for a tax-free conversion. The exit tax privilege initially granted no longer exists.

### c. Registration duties

#### Registration duties

Real estate transfer tax

The transfer of real estate to and from a G-REIT is not exempt from real estate transfer taxes of 3.5% to 6.5% of the sales price. For real estate transfer tax, the conversion of a corporation into a pre-REIT or G-REIT is not regarded as a taxable event according to German tax principles. The same applies to the conversion of a limited liability company (GmbH) into a stock corporation (AG).

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
In general, fully taxable	In general, a final withholding tax of 25% plus a 5.5% solidarity surcharge on the withholding tax, totalling 26.375%	<ul style="list-style-type: none"> <li>- A final withholding tax for privately held shares</li> <li>- Otherwise, a creditable/refundable withholding tax</li> </ul>

#### Corporate shareholder

Before March 1, 2013, the taxation of dividends at the level of the corporate shareholder was dependent on the taxation of the underlying income (pre-taxed profits) distributed by the G-REIT. Pre-taxed profits of a G-REIT could be caused by the taxation of profits of the real estate of the G-REIT in a foreign jurisdiction or the taxation of a subsidiary or a partnership (with foreign real estate) of the G-REIT. If the underlying income had been taxed at least at the 15% German corporate income tax rate or a comparable foreign income tax rate and certain further requirements were met, dividends sourced by such pre-taxed profits were 95% exempt from corporate income tax at the shareholder level.

As of March 1, 2013 dividends are fully taxable at the level of the corporate shareholder of a corporation as long as the shareholder owns less than 10% of the shares at the beginning of the year in which the dividends have been received. Because of the shareholder restrictions outlined under section 2.3 above, this means that dividend income remains subject to corporate income tax at the level of the corporate shareholder at ordinary tax rates irrespective of whether the dividends are sourced by pre-taxed profits or not. The dividend income is also subject to trade income tax.

Capital gains on the disposals of G-REIT shares are always subject to corporate and trade income tax at ordinary tax rates.

#### Individual shareholder

From January 1, 2009, onwards, dividends and all (i.e. short- or long-term) capital gains on the disposition of shares in a G-REIT realised by individuals as non-business income are subject (in principle) to a final withholding tax of 25% (plus solidarity surcharge of 5.5% thereon).

Long-term capital gains on privately held G-REIT shares acquired prior to January 1, 2009, remain tax-exempt provided that the shares were held for more than one year and the shareholder did not own an interest of 1% or more in the G-REIT at any time during the five years preceding the sale of the shares.

Capital gains on privately held shares acquired on January 01, 2009 and onwards are fully subject to personal income tax (i.e. the final withholding tax does not apply), where during the five years preceding the sale the shareholder-owned an interest of 1% or more in the G-REIT.

Dividends received by individuals as business income are fully subject to personal and trade income tax (trade income tax will be credited for personal income tax under certain requirements) unless the underlying income has been taxed with corporate income tax as outlined above (see under corporate shareholder). In the case the underlying income has been taxed, the dividends are only with 60% subject to personal income tax but remain fully subject to trade income tax.

Capital gains on the disposal of G-REIT shares held in a business are fully subject to personal and trade income tax.

## Withholding tax

Dividends from a G-REIT, as well as other benefits granted in addition to or instead of dividends, are subject to a withholding tax at a rate of 25% plus a 5.5% solidarity surcharge on the withholding tax, in total 26.375%. In case the G-REIT shares are privately held by an individual shareholder, the withholding tax is final. Otherwise, the withholding tax is creditable/refundable at the shareholder's level.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- A final withholding tax for dividends</li> <li>- Generally, tax exemption for capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- A final withholding tax for dividends</li> <li>- Generally, tax exemption for capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- 25% plus a 5.5% solidarity surcharge, resulting in a rate of 26.375% (or a reduced treaty tax rate or a reduced withholding tax rate for foreign corporate shareholders)</li> <li>- EU Parent-Subsidiary Directive is not applicable</li> </ul>

### Corporate shareholder

The withholding tax on dividends to foreign (non-resident) shareholders is a final tax, provided that the G-REIT shares are not assets of a permanent German establishment of such shareholder.

Capital gains from the disposal of G-REIT shares are taxable if the shares are assets of a permanent establishment, or if the foreign shareholder has held at least a 1% shareholding at any time within a five-year period prior to the sale of the shares. Usually, double tax treaties provide for a tax exemption of capital gains on the disposal of shares in Germany. However, most of the German tax treaties do not protect investors from the German capital gains tax, as they give Germany the right to tax capital gains from the disposition of shares in a real estate company.

### Individual shareholder

The same principles apply as for foreign corporate shareholders.

### Withholding tax

German domestic tax law provides that the foreign corporate shareholder is principally entitled to a refund of two-fifths of the withholding tax resulting in a final tax of 15% (which is equal to the corporate income tax rate) plus a 5.5% solidarity surcharge, resulting to a rate of 15.825%.

A double tax treaty may reduce the dividend withholding tax rate which amounts under German tax law to totally 26.375% (25% withholding tax plus 5.5% surcharge on the tax). Most German tax treaties provide that foreign shareholders are entitled to a reduced withholding tax rate of 15% if they are domiciled in the other treaty state. Entitlement to a refund also requires that the investor qualifies for the treaty benefit under the German anti-conduit rules.

A corporate shareholder would not be able to exercise his rights to a further withholding tax reduction, which would accrue to him if his shareholding was 10% or more.

Because of the tax-exempt status of the G-REIT, the EU Parent-Subsidiary Directive is not applicable.

## 5 Tax treatment of foreign REITs and its domestic shareholders

Foreign REIT	Corporate shareholder	Individual shareholder
Fully-taxable	Like dividends from a G-REIT, if the foreign REIT is a qualifying REIT	Like dividends from a G-REIT, if the foreign REIT is a qualifying REIT

### Foreign REIT

According to Sec. 1 (3) no. 5 Investment Tax Act 2018, a foreign REIT in the meaning of Sec. 19 (5) of the German REIT law does not qualify as an investment fund.

A foreign REIT's German source income is taxable in Germany at the standard rules and rates applicable to a non-resident corporate taxpayer.

### Corporate shareholder

Dividends distributed from a qualified foreign REIT as defined by the REIT law are fully taxable at the corporate shareholder level. If the dividend was sourced by pre-taxed profits, and the corporate shareholder owns at least 10% of the shares in the foreign REIT, 95% of the dividends would be exempt from corporate income tax. Capital gains from the disposal of the shares in a qualified foreign REIT would be fully taxable at the level of the corporate shareholder. A foreign REIT is qualified under the following cumulative requirements:

- the REIT is not domiciled in Germany;
- the gross assets of the REIT consist of more than two-thirds of immovable property;
- more than two-thirds of the gross earnings are derived from rental, leasing, letting and disposal of immovable property; the distribution deriving from immovable property of the REIT do not carry underlying foreign taxes like the German corporate income tax;
- the REIT is not under the supervision of a financial supervision commission; and
- the shares of the REIT are listed at an organised market.

Foreign withholding taxes levied on distributions will generally be credited in Germany.

Dividends received from a non-qualifying foreign REIT as well as capital gains from the disposal of shares in a non-qualifying foreign REIT are taxed according to general German tax principles depending on the qualification of the foreign REIT as a corporation or transparent entity.

### Individual shareholder

For the tax treatment of dividends distributed from a qualifying foreign REIT and capital gains from the disposal of shares in a qualifying foreign REIT, see under section 4.1.

Dividends received from a non-qualifying foreign REIT as well as capital gains from the disposal of shares in a non-qualifying foreign REIT are taxed according to German tax principles depending on the qualification of the foreign REIT as a corporation or transparent entity. ■

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EUROPE

# Greece

REIC

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction

	Enacted year	Citation	REIT type
REIC	1999	Law 2778/1999 (REIC Law)	Corporate type

Greek Law recognises the legal forms of Real Estate Mutual Funds (REMF) and Real Estate Investment Companies (REIC), which are basically regulated by Law 2778/1999 (hereafter ‘REIC law’). Although the exact term ‘REIT’ does not exist in the Greek legislation, the REIC could be qualified as such. The REIC law was introduced in December 1999 and has been amended thereafter by different laws including recently enacted laws 4141/2013, 4209/2013, 4223/2013, 4261/2014, 4281/2014, 4370/2016, 4389/2016, 4410/2016, 4416/2016 and the recent law 4514/2018.

There are four listed REICs in Greece, subsequent to the absorption of Grivalia Properties by Eurobank resulting in the forfeiture of the former’s REIC status. The majority of listed REICs have been set up and managed by Greek banks. The investor base of listed REICs is predominantly made up of Greece-resident companies and individuals, although a few foreign investors have entered the market over the last years.

The tax and regulatory legislation applicable to Greek REICs is often imprecise, and several grey areas continue to exist in spite of the latest tax reforms.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Greece	4	0	EUR 1,528	0.00%

\*Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

Key requirements
<ul style="list-style-type: none"> <li>- A prior operating licence issued by the Hellenic Capital Market Commission required</li> <li>- Functions are supervised and regulated accordingly</li> </ul>

A Greek REIC has the legal form of a Société Anonyme (SA) and is subject to all the formalities and procedures set out by Greek Corporate Law (L.2190/1920). Moreover, its incorporation requires a prior operating license issued by the Hellenic Capital Market Commission. Its activities are also supervised and regulated accordingly.

Its operating activity must solely consist of managing a portfolio of real estate, certain ‘capital means’ (defined as certain highly liquid and short-term investments in bonds and certain marketable securities) and interests in other SAs whose sole purpose is to invest in real property and whose assets comprise solely of investments in real property. A thorough description of investment policy and real estate use must be submitted to the Hellenic Capital Market Commission for the issuance of the REIC’s operating license.

An REIC must file an application for its listing on the Athens Stock Exchange within two years of its incorporation. The Capital Market Commission may decide to extend the annual deadline for listing in the stock market for up to a total of 36 months subject to an application for an extension being filed by the REIC and demonstration that a force majeure or unfavourable market's conditions prevented the listing. If a REIC is not accepted to the Athens Stock Exchange, then the Capital Market Commission will revoke its operating license.

For a REIC to be considered Greek and hence be regulated by REIC law, its statutory seat must be in Greece. The effective place of management criterion is used by the Greek tax authorities (and is now included in the wording of the new Income Tax Code), when an overseas entity has its effective place of management in Greece. Nevertheless, this scenario should be avoided in order to prevent the authorities from questioning the nationality of the company.

Currently, under Greek law, it should be noted that no foreign managing company (even an EU company) may be the manager of a Greek REIC. In order for the REIC law to apply, the management company must be a Greek resident. REICs' investments in securities (not in real estate) must be supervised by a custodian bank operating in Greece.

No possibility of a pre-REIC structure is provided by the law.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Listed Société Anonyme	EUR 25 million

### Legal form

A REIC must have the legal form of a Société Anonyme listed on the Athens Stock Exchange operating in Greece.

### Minimum share capital

The required minimum share capital amounts to EUR 25 million..

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
None. Transfer of REIC's real property to shareholders, founders, board members and CEOs and their relatives is forbidden	Yes

## Shareholder requirements

The transfer of the REIC's immovable property to founders, shareholders with more than a 5% holding, Board of Director Members, CEOs and by their relatives up to the third degree is forbidden.

No difference between resident and non-resident shareholders in regard of ownership (status, shareholding percentage, etc.) is provided by the law.

## Listing requirements

The REIC's stocks must be listed on the Athens Stock Exchange. Parallel listing is also allowed.

### d. Asset level/activity test

#### Restrictions on activities/investments

- At least 80% of the total assets must be invested in real estate in Greece or in the EEA
- Investment in buildings under development is only allowed if the cost of development does not exceed 40% of the REIC's investment assets
- Greek REICs may invest in at least 80% of the shares of Sociétés Anonymes (A.E.) having as special-purpose the investment in real estate and whose capital is solely invested in real property
- Moveable and immovable assets owned by an REIC for its own operational purposes may not exceed 10% of the REIC's investment assets
- Real Estate investments in non-EEA countries must not exceed 20% of the total Real Estate Investments
- May not invest in a single property exceeding 25% of the REIC's total assets

At least 80% of the total assets must consist of real estate.

For REIC law purposes, 'real estate' means real estate situated in Greece or the EEA or, subject to certain conditions, in a non-EEA third country (see below), which is owned by the company as full or bare owner or as a beneficial owner and that may be used for business facilities or for other commercial, touristic, residential or industrial purposes. Within the meaning of "real estate" as defined by L. 2778/1999, a building plot and a building under construction are also included.

Real estate situated in countries (outside the EEA) may also be included, provided that they do not exceed the 20% of total real estate investments of the company.

Greek REICs may invest in at least 80% of the shares of Sociétés Anonymes (A.E.), having real estate investments as their special purpose, and of which the total capital is invested in real estate or in holding companies investing solely in companies whose capital is invested in real estate as above.

An REIC may invest in development/redevelopment property as long as the construction/redevelopment costs do not exceed 40% of the total value of the investment of REIC in real estate, as the latter results after the completion of the works.

A Greek REIC may not invest in a single property exceeding 25% of its total assets.

The REIC may also invest in other non-real estate assets serving its operational needs and which, together with real estate used for its operations, do not exceed 10% of the value of the investment real estate at the time of purchase.

As stated above, 80% of the total assets of the REIC must be invested in real estate. A further 10% (maximum) can be invested in self-used assets. The remainder (10-20% of total assets) can be invested in securities. There are no legal restrictions if the securities consist of a subsidiary's shares. Regarding a

partnership structure, the partnership interest would no longer be considered ‘securities’. Hence, such investment is not allowed.

#### e. Leverage

Leverage
<ul style="list-style-type: none"> <li>- Overall leverage must not exceed 75% of the REIC’s total assets</li> <li>- Leverage linked to development property must not exceed 40% of the value of the real estate under development</li> <li>- Specific 10% of the total net equity rule for the purchase of real estate</li> </ul>

Financing through either loans or credits must not exceed 75% of the REIC’s total assets. Loans received by the REIC for the purchase of real estate for its operational needs (i.e. non-investment property) must not exceed 10% of the total net equity of the REIC minus the total investments in real estate. The value of such loans is not included in the 75% threshold mentioned above.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
50% of its annual net profits	No obligation	Annually

##### Operative income

The REIC should generally distribute at least 50% of its annual net profits to its shareholders. The distribution of a smaller percentage or no distribution at all is only allowed pursuant to a Resolution taken at the Shareholders’ Meeting (provided a clause exists in the REIC’s Articles of Association) either for the creation of a tax-free reserve or the distribution of free shares accompanied by a share capital increase.

##### Capital gains

Capital gains do not need to be distributed.

#### g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Violations may trigger the imposition of penalties</li> <li>- Non-listing of REIC’s shares on the Athens Stock Exchange leads to the loss of REIC status</li> </ul>

If a REIC is not accepted to the Athens Stock Exchange, then the Capital Market Commission shall revoke its operating license and the company should be liquidated. As a consequence of liquidation, all tax benefits granted by the law will be retroactively rescinded.

Tax penalties may be applied at different levels on a case-by-case basis depending on the nature of the infringement.

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Investment and liquid assets taxed at 0.375% or 10% of the European Central Bank (ECB) interest rates plus 1%, whichever is higher	Exempt due to the special tax treatment of the REIC	No WHT except for dividend distributions received from Greek subsidiaries at a rate of 10%

#### Current income

REICs are subject to a special taxation rate, which amounts to 0.375% or 10% of the European Central Bank (ECB) interest rate in force (Reference Interest Rate) plus 1%, whichever is higher. The tax rate is applied to the average of the REICs investments plus any available funds (cash and securities), at their current value, as shown in their six-months investment tables, which are a legal requirement to produce. For example, assuming the ECB interest rate is 0.05%, the tax rate would be calculated as follows:  $10\% \times (0.05\% + 1\%) = 0.105\%$  and, because such rate is lower than 0.375%, the REIT will calculate tax using the higher tax rate of 0.375%. The tax is payable by the REIC. Its direct shareholders have no further tax liability upon receipt of dividends. Should a change of the Reference Interest Rate occur, a new taxation basis would be valid starting the first day of the month following the stated amendment.

#### Capital gains

Since REICs are subject to the special taxation rules described above, which exhausts any further tax liability of the company, there is no taxation on the capital gains on the sale of securities by the REIC. If a REIC sells listed shares, a 0.2% transfer duty will apply on the value of the shares transferred.

#### Other taxes

As from January 1, 2014, REICs are subject to the Annual Real Property Ownership Tax (the so-called 'ENFIA' tax). The ENFIA tax consists of the main ENFIA tax and the supplementary ENFIA tax (0.55% on the total tax value of the property owned). REICs are fully subject to both the main tax and the supplementary tax.

REICs are fully exempt from the Real Property Transfer Tax, and the local municipality surcharge levied at 3.09% on the value of the property, (payable by the purchaser), on the acquisition of real property. When an REIC sells real property, the purchaser is not exempt from the aforementioned transfer taxes.

#### Withholding tax

Income generated from foreign or Greek securities is not subject to any Greek withholding tax upon repatriation with the exception of dividends received from a Greek subsidiary. In respect of interest from bond loans, the said tax exemption is valid, provided that the bonds were acquired at least 30 days before the interest payment date. Dividends received by a Greek REIC from Greek entities are subject to withholding tax at 10%, which can be offset against the wealth tax imposed on its average net investments described above under 'current income'. Any unused amount may be carried forward to be set off against a tax on average investments in future tax returns. Income tax treaties may not apply to reduce the rate of withholding.

## Accounting rules

The REIC can choose whether to follow Greek GAAP or IFRS until it is officially listed on a stock exchange. Then, it must follow IFRS.

### b. Transition regulations

#### Conversion into REIC status

Tax benefits upon mergers, spin-offs, etc. of real estate companies

Greek REICs enjoy the tax benefits provided by Law 2166/1993 for certain cases of mergers, spin-offs etc. Benefits available may include exemptions from transfer taxes and capital gains.

### c. Registration duties

#### Registration duties

Exemption from any Greek tax and stamp duties on REIC's share issue

The issuance of REIC's shares and the transfer of real estate to an REIC are exempt from any Greek tax duties, stamp duties or any kind of tax liability. Capital Concentration Tax (CCT) at 1% is payable in the case of a share capital increase. However, no CCT is imposed on the initial share capital injected upon the formation of the REIC.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Tax-exempt on dividends received from REIC</li> <li>- Exempt from capital gains tax on the sale of shares in a non-listed Greek REIC</li> <li>- If the REIT is listed, the gain is taxed at 28%</li> </ul>	<ul style="list-style-type: none"> <li>- Tax-exempt on dividends received from REIC except for special solidarity tax (up to 10%)</li> <li>- Exempt from capital gains tax on the sale of shares in Greek REIC but subject to solidarity tax in most cases</li> </ul>	N/A

#### Corporate shareholder

The taxation of dividends distributed by the REIC should be exempt from any Greek withholding tax as well as corporate income tax at the level of the corporate shareholder, according to the wording of the law. Capital gains arising from the sale of shares in a non-listed Greek REIC are exempt from income tax. If the REIT is listed, the gain is taxed at 28%.

## Individual shareholder

Dividend income from REICs received by an individual shareholder should be exempt from income tax but subject to special solidarity tax at rates up to 10%. The special solidarity tax is imposed on the individual's total income, whether exempt or not. Capital gains arising from the sale of shares in a non-listed Greek REIC are exempt from income tax. If the REIC is listed, the gain will be taxable only in the case where the seller owns more than 0.5% of the share capital of the listed REIC and the shares transferred have been acquired after January 1, 2009. Accordingly, most retail investors would be exempt. The gain is subject to special solidarity tax at rates up to 10% in any case.

## Withholding tax

N/A

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- No Greek withholding tax on dividends paid by REIC</li> <li>- Exempt from capital gains tax on the sale of shares in Greek REICs in most cases</li> </ul>	<ul style="list-style-type: none"> <li>- No Greek withholding tax on dividends paid by REIC</li> <li>- Exempt from capital gains tax on the sale of shares in Greek REICs in most cases</li> </ul>	N/A

## Corporate shareholder

Dividends distributed by the REIC to a non-resident corporate shareholder should not be subject to withholding tax in Greece. Capital gains arising from the sale of shares in a non-listed Greek REIC are exempt from income tax. Capital gains from the sale of shares in listed REICs are also exempt on the additional condition that the foreign shareholder does not maintain a permanent establishment in Greece where the gain can be attributed.

It is not clear whether Greek REICs can benefit from double tax treaties entered into by Greece.

## Individual shareholder

Dividends distributed by the REIC to a non-resident individual shareholder should not be subject to withholding tax in Greece. Capital gains arising from the sale of shares in a non-listed Greek REIC are exempt from income tax. Capital gains from the sale of shares in listed REICs are exempt if the shareholder is resident in a double tax treaty country and can access the treaty (regardless of whether the Greek REIC can access the treaty, see below). Regardless of residence, no income tax is levied on the gain if the seller owns less than 0.5% of the share capital of a listed company or if the listed shares were acquired prior to January 1, 2009.

It is not clear whether the Greek REICs would be awarded a similar benefit from the same arrangement.

## Withholding tax

N/A



## 5 Treatment of the foreign REIT and its domestic shareholder

Foreign REIC	Corporate shareholder	Individual shareholder
No specific tax privilege	No specific provision	No specific provision

### Foreign REIC

The Greek REIC law only applies to Greek REICs and does not cover the cases of foreign REICs. Foreign REICs have not been dealt with by the Greek tax authorities, and therefore it is unclear as to the treatment of foreign REICs under Greek law.

As such, the exact treatment should be determined on a case-by-case basis.

### Domestic corporate shareholder

There is no specific tax provision dealing with the taxation of income received by a company resident in Greece from a non-resident REIC. In the absence of specific rules, it is expected that such foreign-sourced income should be taxed in the hands of the Greek corporate shareholder according to the general rules applicable to income from a foreign source.

Dividends from EU qualifying subsidiaries will be exempt from tax, provided that the conditions of the EU Parent/Subsidiary Directive are met. If the dividend income does not qualify for exemption under the EU Parent/Subsidiary Directive, then it is taxed as normal business income at 28% with a credit for any tax withheld at source. If the participation distributing the dividends is in the EU, then unlimited foreign tax credit is provided for both the dividends withholding tax and the underlying corporate income tax.

### Domestic individual shareholders

There is no specific tax provision dealing with the taxation of income received by an individual resident in Greece from a non-resident REIC. In the absence of specific rules, it is expected that such foreign-sourced income should be taxed in the hands of the Greek individual shareholder according to the general rules applicable actually to income from a foreign source. A 10% final tax is imposed on the amount of dividends, and 15% on capital gains received plus a special solidarity tax up to 10% which is imposed on total income (whether exempt or not). However, as this has not been dealt with by the Greek tax authorities previously, the exact treatment is unclear. ■

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GLOBAL  
REIT SURVEY

EUROPE

# Hungary

REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIT	2011	Act on Real Estate Investment Companies	corporate type

Traditionally, limited liability companies have been the preferred vehicle for holding real estate investments in Hungary. The REIT regime was introduced into the Hungarian legislation in 2011. The key tax benefits arising for the investor from a Hungarian REIT structure are that the income generated by the REIT is as a main rule not taxable from Hungarian corporate income tax and local business tax perspective and distributions from the REIT paid to corporate shareholders are not subject to withholding tax in Hungary.

The REIT is governed by the Act on Real Estate Investment Companies (the 'Act'). Public limited companies with a minimum starting capital of HUF 5 billion and which are registered as a REIT (upon the request of the company) with the Hungarian Tax Authority (the 'tax authority') may qualify as REITs if the conditions are met. The aim of the Act was to introduce the EU-wide known 'REIT structure' into the Hungarian market.

The law acknowledges the following entities as REITs<sup>1</sup>:

- a real estate investment pre-company;
- a real estate investment company; or
- a real estate project company (Special Purpose Vehicle, hereinafter 'SPV').

The activities of a REIT or its 100% subsidiary SPV should be limited to the following in the territory of Hungary:

- the sale of their own real estate;
- the rental and operation of their own real estate (including particularly real estate investment for operation purposes, rental and operation of real estate owned by the Hungarian government or state, operating own warehouse and stock room, and rental of a vacant warehouse and stock room);
- property management and facility management;
- asset management; and
- real estate project development.

Advantages of a Hungarian REIT structure:

- unlike Hungarian real estate funds, a REIT is able to hold shares in a project company that can also benefit from the REIT regime;
- corporate income-tax-free status is available at REIT and SPV levels (including gains on asset deals);
- local business tax-free status is available at REIT and SPV levels (including gains on asset deals);
- REITs do not have to pay the Fund tax based on their net assets; and

<sup>1</sup> Reference to 'REIT' in this document, includes real estate investment pre-companies, real estate investment companies, or real estate project companies under the preferential regime. Reference to only one of those entities, should be understood as a reference to that type of entity only.

- REITs are subject to only 2% real estate transfer tax (RETT) levied on the transfer of Hungarian real estate or any rights related to such property and also on the acquisition of shares in companies owning domestic real estate (real estate holding company).

Limitations and obligations:

- REITs' management have an obligation to have dividend proposed to be paid out at 90% of the REITs profits or distributable monetary assets each year, while SPVs in the regime have an obligation to have dividend pay-out proposed by management at 100% of their profits or distributable monetary assets each year as dividends;
- a starting capital of HUF 5 billion is required for a REIT;
- strict registration obligations are administered by the tax authority;
- limitations exist regarding top management; and
- a compulsory quarterly market valuation of the property portfolio is required for REITs.

## 2 Main requirements

### a. Formalities/procedure

#### Key requirements

REITs (including pre-companies) have to be registered at the tax authority. Strict formal and practical requirements should be met

REITs (including pre-companies) have to be registered at the tax authority. Registration is only possible if REITs have no outstanding tax liabilities with the tax authority, customs authority or at the local municipalities.

During the registration procedure, information - amongst others - the deed of foundation, availability of registered capital, related parties, name of the auditor and detailed information about the senior management should be filed.

REITs (including SPV) should notify the tax authority within 30 days if there have been any significant changes to their status (including any changes to SPVs held).

REITs should not be undergoing voluntary closure, bankruptcy or liquidation procedures prior to or during their registration.

REITs should have experienced managers, who have a college or university degree, at least three years of managerial experience and a clean criminal record. Further independence requirements should also be met.

REITs (including SPVs) should revalue their properties and accounts every quarter.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Publicly Limited Company	HUF 5 billion

### Legal form

A REIT should be a public limited company, and – broadly – at least 25% of the shares should be tradable on controlled financial markets (i.e. certain defined stock exchanges).

### Minimum share capital

The minimum share capital (registered capital, capital reserve and profit reserve) is HUF 5 billion.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
Limitation for banks and insurance companies and other REITs	Yes, as a general rule, 25% of the shares should be traded on controlled financial markets

### Shareholder requirements

At least 25% of the shares should be tradable on controlled financial markets (i.e. certain defined stock exchanges). At least 25% of the shares should be owned by minority shareholders (below 5% each). Direct voting rights in a REIT, by banks and insurance companies, altogether are limited to 10%.

REITs are allowed to own only a maximum of 10% of shares or voting rights in other REITs.

## d. Asset level

Restrictions on activities/investments
Investment policy limitations and liabilities are similar to those of real estate investment funds in Hungary

A REIT cannot have shares in another company other than an SPV, other REITs or companies whose main activity consists of real estate building project management. REITs cannot have more than 10% shares or 10% of the voting rights in any other REIT.

Beside real estate, the assets of REITs may include assets which are necessary for performing their regulated activities and cash and cash equivalents (including bonds issued by governments or financial institutions), shares of entities issued in regulated markets, appropriate interest in other REITs, REIT SPVs or SPVs who engage in real estate building projects, or hedge agreements on FX risks associated to their real estate activities or debt and interest repayments.

However, 70% of the total assets should be in the form of real estate. A single real estate asset or shares in other REITs should not make up more than 30% of the total assets. When performing this calculation, the revaluation of the real estate (recognized in line with the Hungarian Act on Accounting) should be considered as well. However, in the case of REITs performing bookkeeping under IFRS, the value of real estate already includes the revaluation, regardless of the valuation model applied.

The supervisory board's permission is required when purchasing an asset with an asset value exceeding 10% of the REIT's total assets. If the REIT uses a one-tier system, where the board of directors are responsible for both the directory and supervisory duties, the supervisory board's permission can be considered as granted, if the majority of the independent parties member vote for the acquisition of the asset exceeding the 10% of the REIT's total assets.

#### e. Leverage

Leverage
Debt is limited to 65% of the value of the real estate assets

The REIT's liabilities (other than equity) should not exceed 65% (SPV 70%) of the value of its real estate assets and investments.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
<ul style="list-style-type: none"> <li>- Any expected dividends should be distributed</li> <li>- SPVs should distribute their total profits of distributable monetary assets</li> </ul>	To the extent that it is included in the REITs' income, any capital gain realised on disposal of real estate or shares in other entities should be distributed	Annually

The REITs board of directors have an obligation to make an offer regarding the acceptance of dividends stipulated as expected dividends in their deed of foundation. In case of acceptance, the distribution of the profit should take place within 30 trading days after the annual report has been accepted by the shareholders. If the available cash amount does not reach the value of expected dividends, then at least 90% of the distributable monetary assets have to be distributed.

SPVs have the same obligation, but they need to pay dividends at 100% of their distributable monetary assets each year. Distribution of the profit should take place within 30 trading days after the annual report has been accepted by the shareholders.

REITs and SPVs should not enter into any agreement which limits their dividend payment obligation (except for loan agreements with financial institutions).

#### g. Sanctions

Penalties/loss of status rules
REITs that do not meet the requirements are deleted from the records and lose tax privilege

The tax authority will delete REITs from its records if the requirements are not met or not corrected within 90 days.

REITs should start their activities within six months of registration, and they cannot suspend their activities for more than six months; otherwise, the tax authority will delete them from its records.

REITs that do not meet the requirements determined by law cannot apply the benefits (from the day when

the resolution on the deletion from the registry issued by the tax authority becomes effective). From that point onwards, the REIT will be taxed similarly to an ordinary company.

As a general rule, if the real-estate pre-company is not registered as a REIT, then it is liable to pay twice the corporate income tax and local business tax that were due without applying for the REIT regime's tax benefits. A similar rule should be applied to the SPVs of pre-companies.

### 3 Tax treatment at the REIT level

#### a. Corporate tax/local business tax/withholding tax

Operative income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Corporate income tax and local business tax-free status are available for REITs and SPVs</li> <li>- Certain related-party transactions could be subject to corporate income tax if arm's length prices are not met</li> </ul>	Received capital gains are tax-free for corporate income tax and local business tax purposes	No withholding tax in Hungary for profit distributed to entities, other than individuals

#### Operative income

REITs should calculate their corporate income tax base according to the general CIT rules - with some exceptions; however, their corporate income tax base is not subject to tax.

Transactions with related parties which are not REITs are subject to transfer pricing rules. The difference between the arm's length prices and the applied prices in such transactions could be subject to corporate income tax at REIT level. Income realised on transactions with related parties, which are not subject to the Hungarian REIT legislation will be subject to Hungarian corporate tax.

Tax losses cannot be carried forward.

REITs local business tax base is tax-free.

#### Capital gains

By default, received capital gains are part of the profit before taxation. The received capital gains, as part of the total income of REITs, are free from corporate income tax and local business tax.

If a REIT owns more than 10% of the shares of a real estate project development company, then the capital gain realised on the sale of the shares or the gain realised on in-kind contribution will be subject to corporate income tax.

#### Foreign taxes

Considering that any REIT's income is tax-free, it is not possible to credit or exempt foreign taxes on foreign-sourced income.



## Accounting rules

An interim audit is required after the registration and deregistration.

REITs should revalue their real estate units at least quarterly. For the revaluation, the general accounting rules are applicable. If the market value of a real estate unit is higher than its accounting book value, then the difference might be accounted for as extraordinary depreciation and/or as capital depending on the revaluation result (positive/negative) on the real estate units. In the case of REITs performing under IFRS (including SPV), the value of real estate has to be determined based on a revaluation model or fair valuation model.

Apart from the above revaluation, there are no special accounting rules applicable exclusively for REITs.

REITs (i.e. entities whose shares are traded on the regulated market) have to use IFRS instead of Hungarian GAAP for local reporting purposes once their shares are introduced to the regulated market.

### b. Transition regulation

#### Conversion into REIT status

Possible

If a pre-company fulfils the requirement of REIT law, then it has to initiate the REIT registration..

### c. Registration duties

#### Registration duties

No duty on capital contribution

The registration fee at the Court of Registration is currently HUF 100,000 (around EUR 330) for public limited liability companies.

There is no duty on capital contribution, except RETT if the subject of the contribution is a real estate unit.

## 4 Tax treatment at the shareholder level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Dividends received are tax-deductible for CIT purposes</li> <li>- Capital gains are subject to corporate income tax; however participation exemption rules could apply</li> </ul>	<ul style="list-style-type: none"> <li>- Individual shareholders are subject to 15% personal income tax on their dividend income</li> <li>- Dividends are subject to 19.5% social contribution; however, if the individual shareholder's annual income exceeds 24 times of the monthly mandatory minimum wage, the exemption could be applied</li> </ul>	<p>There is no dividend withholding tax in Hungary on dividends paid to non-private individual entities</p>

## Corporate shareholders

According to the general rules, dividends received by corporate shareholders are tax-deductible for CIT purposes in Hungary.

Capital gains are subject to corporate income tax; however, the general participation exemption rules could apply. Domestic or foreign participation can be considered as an ‘announced participation’, and this should be reported to the tax authority within 75 days of the acquisition. The capital gains on such participations held for at least one year are exempt from corporate taxation. Any loss on write-offs, foreign exchange or losses incurred when cancelling from the books (except during transformations) should be added back to the corporate income tax base.

## Individual shareholder

Individual shareholders are subject to personal income tax of 15% on their dividend income. There is a 19.5% social contribution tax on dividends unless the individual’s annual taxable income exceeds 24 times the mandatory monthly minimum wage (in FY19 HUF 3,576,000, around EUR 11,200). The personal income tax and the social contribution tax charge (if applicable) should be deducted and paid to the tax authority by the REIT.

Capital gains on the sale of shares in REITs are subject to personal income tax at 15%. Direct expenses related to the acquisition of the shares are deductible. There is a 19.5% social contribution charge (exemption, as described above) on capital gains not derived from securities on an EEA exchange market.

## Withholding tax

There is no dividend withholding tax in Hungary on dividends paid to non-private individual entities.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Distributed dividends are not subject to Hungarian corporate income tax</li> </ul>	<ul style="list-style-type: none"> <li>- Foreign individual shareholders are subject to personal income tax at 15% on their dividend income</li> <li>- Treaty rates may apply</li> <li>- Individuals not resident for social security purposes are not subject to social contribution tax on dividends and capital gains</li> </ul>	<p>There is no dividend withholding tax in Hungary</p>

## Corporate shareholders

Distributed dividends are exempt from Hungarian corporate income tax even if the receiver is not a Hungarian entity.

Hungarian REITs listed on an accepted stock exchange should not be qualified as real estate holding companies for Hungarian corporate tax purposes; therefore, the capital gains realised on the sale of shares in such Hungarian REITs should not be subject to corporate income tax in Hungary.

## Individual shareholder

Foreign individuals are only liable for personal income tax at 15% on gains realised on the sale of shares; however, the tax can be reduced or eliminated by an applicable double taxation treaty. Individuals not resident for social security purposes are not subject to social contribution tax on dividends and capital gains.

## Withholding tax

There is no dividend withholding tax in Hungary on dividends paid to non-private individual entities.

# 5 Tax treatment of foreign REITs and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
<ul style="list-style-type: none"> <li>- Capital gain on the sale of shares of real estate companies could be subject to Hungarian corporate income tax</li> <li>- Treaty exemptions may be applicable</li> </ul>	<ul style="list-style-type: none"> <li>- Received dividends are generally exempted</li> <li>- Capital gains are subject to corporate income tax; however participation exemption rules could apply</li> </ul>	<ul style="list-style-type: none"> <li>- Individual shareholders are subject to personal income tax at 15% on their dividend income</li> <li>- Dividends are subject to 19.5% social contribution; however, if the individual shareholder's annual income exceeds 24 times of the monthly mandatory minimum wage, the exemption could be applied</li> </ul>

## Foreign REIT

Foreign REITs could be taxed on Hungarian source income and capital gains on taxable Hungarian properties.

The sale of a share in a so-called Hungarian real estate holding company is subject to corporate tax. Real estate holding companies, for Hungarian CIT purposes, are business entities whose shares are not traded on a recognised exchange market. In addition, real estate holding companies are those that also own real estate in Hungary constituting more than 75% of the balance sheet value of their assets or the consolidated balance sheet with their related parties. Their shareholders should be resident in jurisdictions which do not have tax treaties with Hungary or where the treaty allows Hungary to levy tax. The tax is based on the selling price of the shares, reduced by the purchase price paid and other justifiable costs. The tax can be reduced or eliminated by an applicable double taxation treaty.

In the case of Hungarian real estate transactions, treaty rules are applicable.

## Corporate shareholders

Dividends received from foreign sources (including foreign REITs) are free from Hungarian corporate income tax unless the foreign payer qualifies as a controlled foreign company.

Capital gains are subject to corporate income tax; however, participation exemption rules could apply.

A domestic tax credit system is available for companies in order to avoid double taxation on foreign-source income. Hungarian tax treaties apply either the exemption or the credit method to prevent double taxation.

## Individual shareholder

Under its double taxation treaties, Hungary mainly gives tax relief by way of exemption. The wording of each double-taxation treaty should be considered on its own merits. If the income is derived from a jurisdiction which does not have a tax treaty with Hungary, then the individual shareholders are subject to personal income tax at 15% tax on their dividend income from that source. However, foreign withholding tax can be credited against the Hungarian tax liability with certain limitations.

By default, the 19.5% social contribution charge on dividends not derived from securities on an EEA exchange market is applicable; however, a possible exemption could be investigated for each case.<sup>2</sup> ■

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<sup>2</sup> This document has been prepared based on the rules applicable in Hungary at the date of 31 May 2019.



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major REIT regimes  
around the world.



# 1 General introduction

Citation	REIT type
Introduced by the Finance Act 2013	Corporate entity

Since the introduction of the Irish REIT tax legislation in the Finance Act 2013, four REITs (Green REIT Plc, Hibernia REIT plc, IRES REIT and Yew Grove REIT plc) have been established in Ireland. Between them, they have managed to raise more than EUR 2 billion.

Irish REITs, as a property investment vehicle, provide an opportunity for diversified investment in real estate to both Irish and overseas investors at a time when the returns on Irish property may be viewed as attractive relative to similar overseas opportunities. In addition to providing an alternative means of access, REITs allow smaller-scale investors the opportunity to generate property investment returns in a regulated environment.

On April 15, 2019, Green REIT Plc announced that it had decided to sell the company and its assets following a strategic review. At the time of the announcement, Green REIT Plc was said to have property assets to the value of EUR 1.5 billion.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Ireland	4	3	EUR 3,135	0.25%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1yr return (EUR) %	Div Yield	% of Global REIT Index
Green Reit PLC	EUR 1,266	26.91%	3.04%	0.11%
Hibernia REIT PLC	EUR 1,008	-0.92%	2.34%	0.09%
Irish Residential Properties REIT	EUR 732	26.86%	3.32%	0.05%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Notice must be filed to become a REIT/Group REIT  
Certain conditions for REIT/Group REIT status

A notice must be filed with the Irish Revenue Commissioners to become a REIT. The notice shall contain a statement to the effect that the REIT or a principal company of a 'Group REIT' is:

- i. incorporated under the Irish Companies Acts 1990;
- ii. resident in Ireland for Irish tax purposes and not resident in another country;
- iii. listed on the main market of a recognised stock exchange in an EU Member State; and
- iv. not a closely controlled company for corporation tax purposes (unless owned by certain 'qualifying investors' such as pension funds, life businesses, Qualifying Investment Funds (an Irish regulated non-UCITs fund structure), charities and NAMA).

In respect of conditions (iii) and (iv), the REIT or principal company of a Group REIT has a grace period of three years from when it becomes a REIT to meet these conditions. This will enable companies to acquire REIT status and then have three years to diversify their shareholders and raise additional finance to facilitate a listing.

In addition, each of the following conditions should be met by the REIT or the Group REIT for each accounting period:

- i. At least 75% of the aggregate income of the REIT or Group REIT must derive from carrying on a property rental business;
- ii. The property rental business conducted by the REIT or Group REIT must consist of at least three properties. The market value of any one of these properties should not exceed 40% of the total market value of the property rental portfolio held by the REIT/Group REIT;
- iii. The REIT or Group REIT must maintain a ratio of at least 1.25:1 in respect of property income and property finance costs to property finance costs;
- iv. At least 75% of the aggregate value of the assets of the REIT or Group REIT relate to assets of the property rental business;
- v. The debt of the REIT or the Group REIT shall not exceed 50% of the market value of the assets of the REIT or Group REIT;
- vi. Subject to having sufficient distributable reserves, at least 85% of the REIT's or Group REIT's property income (excluding capital gains) must be distributed to shareholders within nine months of the year-end.

In respect of condition (ii) above, the REIT or Group REIT has a grace period of three years from when it becomes a REIT to meet this condition.

Every REIT or principal company in respect of a Group REIT shall by February 28 each year make a statement to the Revenue Commissioners confirming that the above conditions have been met.



Since January 1, 2015, where subsequent to the initial notice referred to above a new company is incorporated or acquired by the Group REIT as a wholly-owned subsidiary, an amended notice must be filed with the Revenue Commissioners (Form REIT 2A) within 30 days of the new company becoming a member of the Group REIT. This amended notice must specify:

- the date from which the new company will become a member of the Group REIT;
- a statement that the conditions referred to above in relation to the Group REIT are reasonably expected to be met at the end of the accounting period in which the amended notice is made; and
- a list of all the members of the group to which the Group REIT designation will apply.

Where the above-amended notice is not made within 30 days from the date the new company becomes a member of a Group REIT, the principal company shall be deemed to have made a notice to the Revenue Commissioners that it has ceased to be a Group REIT from a date that is 30 days after the date the new company became a member of the group.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
The REIT must be an Irish incorporated company listed on the main market of a recognised stock exchange in an EU Member State	A Public Limited Company (PLC) must have an allotted share capital of not less than EUR 25,000

### Legal form

The REIT or a principal company of a Group REIT must be listed on the main market of a recognised stock exchange in an EU member state.

The REIT or principal company of a Group REIT must be an Irish tax resident and Irish incorporated company.

Other members of a Group REIT need not be Irish incorporated and can be tax resident outside Ireland.

### Minimum share capital

Public Limited Companies must have a nominal value of share capital of not less than EUR 25,000. An Irish REIT may only have one class of ordinary shares, but it can also offer non-voting preference shares which carry no rights to dividends other than dividends at a fixed rate.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
Must not be a 'close' company A single corporate shareholder may not own 10% or more of the shares/voting rights	The principal company of a REIT needs to be listed on the main market of a recognised Stock Exchange in an EU Member State.



## Shareholder Requirements

The REIT must not be a ‘close company’. A company is ‘close’ where it is controlled by five or fewer shareholders. However, where a listed company is under the control of five or fewer participators, it shall not be treated as close if shares in the company carrying not less than 35% of the voting power are ‘held by the public’. Broadly, shares are considered ‘held by the public’ if the shares do not comprise part of a principal shareholders holding. A principal shareholder is a shareholder that possesses more than 5% of the voting power of the company and where there are more than five such shareholders if such person is one of the five persons who possesses the greatest percentages. Shares held by pension funds or non-close companies will be considered as ‘held by the public’.

The close company rule will not apply where the shares in the REIT or principal company of a Group REIT are controlled by ‘qualifying investors’, i.e. pension funds, life businesses, Qualifying Investment Funds, charities and NAMA.

Where a shareholder holds 10% or more of the share capital with voting rights in the REIT or principal company of a Group REIT or is entitled to 10% or more of a distribution, and the REIT or Group REIT has not taken ‘reasonable steps’ to prevent a distribution to such a shareholder, then the REIT or Group REIT shall be deemed as receiving an amount of income equal to the amount of the distribution to the shareholder. This income shall be taxable at the 25% rate, and no loss allowance or expense may be set against it for the purposes of calculating the amount chargeable to tax. The 10% shareholding rule does not apply to a ‘qualifying investor’, i.e. pension funds, life businesses, Qualifying Investment Funds, charities and NAMA.

It is not clear what will be considered as ‘taking reasonable steps’, and there is no guidance to date on this point.

The above penalty for excessive shareholdings will not apply in the first three years of the REIT. This provision should give the REIT time to attract new investors and thus diversify its shareholders.

## Listing requirements

As stated above, to qualify as a REIT, the company must be listed on the main market of a recognised stock exchange in an EU Member State. The requirement for the listing to be on the main market, compared to listing on a smaller alternative market, will result in additional costs/regulation and may deter smaller vehicles from taking up REIT status.

### d. Asset level/activity test

#### Restrictions on activities/investments

- At least 75% of the REIT or Group REIT’s aggregate income must be derived from the property rental business
- At least 75% of the market value of the REIT must relate to assets of the property rental business
- Within three years of commencement, the REIT must hold at least three separate assets, none of which having a market value in excess of 40% of the market value of the property rental assets
- The REIT can hold Irish and non-Irish assets
- The property rental assets may be either commercial, industrial or residential

A REIT can carry on a non-property rental business (the residual business). However, 75% of a REIT or Group REIT's aggregate income must derive from its property rental business that is the business generating rental income from properties. Capital gains on the sale of assets are not considered income for the purposes of the 75% income test.

Where the REIT or Group REIT raises cash either by selling a rental property or raising cash from the issue of ordinary share capital and invests the cash in non-property rental assets, then the profits from such investments will be treated as profits of the property rental business during the first 24 months following the sale or share issue ('re-investment provision'). Following the 24-month period, the profits will be treated as profits of the residual business. This should give REITs time to consider various re-investment opportunities. It should be noted that the re-investment provisions will not apply to funds raised by way of a preference share issue.

In addition to the income test, there is an asset test that requires that 75% of the market value of the REIT or Group REIT relates to assets of the property rental business. On a strict technical reading of the legislation, the re-investment provisions will only apply to the 75% income test and not to the 75% asset test. However, the revenue is prepared to apply the reinvestment provisions to the 75% asset test. Therefore, proceeds from share issues and property sales should be treated as property rental assets for a period of two years. The 75% asset and income test should limit the amount of investment in non-property rental generating assets.

In the case of a Group REIT, the 75% asset and income test will be determined using the consolidated accounts of the group.

A REIT or Group REIT must hold at least three separate property rental assets directly, and no one of these assets can exceed 40% of the market value of the total portfolio.

Qualifying properties may be residential, industrial or commercial and in any location worldwide.

Offices used in carrying on the business of the REIT itself are unlikely to be considered property rental assets for the purposes of the asset tests mentioned above. It should also be noted that if these offices cease to be used for the residual business and begin to be used for the property rental business, the asset shall be deemed to have been sold and reacquired by the REIT at market value. The deemed gain will be subject to capital gains tax at 33%.

## e. Leverage

### Leverage

Profit: Financing Ratio

The REIT or Group REIT must maintain a profit/financing ratio of at least 1.25:1. The ratio is calculated as follows:

- Property income plus property finance costs: property finance costs.
- Property financing costs will include interest, net swap or hedging costs, fees such as arrangement and commitment fees associated with raising debt finance.

Where the ratio is breached, the REIT shall be chargeable to tax at the rate of 25% on the amount by which the property financing costs would have to be reduced for the property financing cost ratio to equal 1.25:1 subject to certain limits.

For example, if the property income was EUR 100 million and the financing costs were EUR 500 million, then the profit/financing ratio would be 1.2:1. In order to bring the ratio back to 1.25:1, the financing costs would need to be reduced by EUR 100 million.

However, the taxable amount shall not exceed 20% of the property income of the REIT. Thus, the REIT or principal company of a Group REIT would be chargeable to tax at the rate of 25% on EUR 20 million (EUR 100 million at 20%).

Increases in interest rates or drops in rental yields may negatively impact on this ratio and result in a penalty as described above. In addition, it may result in the company or group's REIT status being cancelled.

While the profit/financing ratio appears generous, it will need to be considered in conjunction with the requirement that debt shall not exceed 50% of the market value of the assets of the REIT/Group REIT, i.e. all of the assets of the REIT/Group REIT and not just property rental assets.

#### f. Profit distribution obligations

Property income	Capital gains	Timing
85% of property income must be distributed to shareholders	Not included in the distribution obligation	On or before the tax return filing date for the relevant accounting period

#### Property Rental Income

At least 85% of property rental income earned by the REIT/Group REIT in an accounting period must be distributed to shareholders on or before the REIT's tax return filing date, i.e. within nine months of the period/year-end.

Where a REIT fails to make the required distribution, the REIT or the principal company of the REIT will be chargeable to tax at 25% on:

- i. Where no distribution is made, the amount chargeable will be equal to 85% of the property income for the period.
- ii. Where a distribution is made but it is less than 85% of the property income, then the amount chargeable will be the difference between the distribution made and the amount equal to 85% of the property income.

No deductions may be made in arriving at the amount chargeable to tax.

It should be noted that where the REIT is restricted under company law from distributing all or part of the property income (e.g. the company does not have sufficient distributable reserves), then regard will be had to this restriction when calculating the amount chargeable to tax. This will prevent a situation whereby for example a company is penalised for not distributing property rental income even though under company law it was not in a position to make a distribution as a result of not having sufficient distributable reserves.

#### Capital gains

The 85% distribution requirement does not apply to gains arising from the disposal of real estate. Profits arising on the proceeds, if not reinvested in property rental assets within 24 months will be treated as 'bad' income for the 75% income test. Similarly, if the proceeds are not reinvested in property rental assets within 24 months, the proceeds will be considered 'bad assets' for the purposes of the 75% test.

## Other profits

There is no requirement to distribute non-property rental profits. However, as mentioned these will be considered ‘bad’ assets for the purposes of the 75% asset test and any income deriving from them will be considered ‘bad’ income for the purposes of the 75% income test.

## g. Sanctions

### Penalties/loss of status rules

Tax penalties and potential loss of REIT status

Penalties or the withdrawal of REIT status may arise where any of the conditions (see 2.1) are breached.

Every REIT or principal company of a Group REIT shall, by February 28 of each year, deliver a statement to the Revenue Commissioners confirming that all of the conditions have been met throughout the most recently ended accounting period. Where a condition has been breached and it is not possible to make such a statement, the REIT or principal company of a Group REIT shall provide details to the Revenue of the breach and how it intends to rectify such breach. Where within a reasonable period of time as determined by the Revenue Commissioners, the REIT or the principal company of a Group REIT fails to rectify the breach, then the Revenue Commissioners may issue a notice withdrawing REIT status, and this withdrawal will take effect from the end of the previous accounting period.

The fact that a REIT will be given time to rectify a breach should ensure that a company does not automatically lose its REIT status due to an unavoidable breach, e.g. increase in interest rates, drop in rental yields or property values etc.

In addition, penalties may arise in the following circumstances:

1. Where a shareholder holds 10% or more of the share capital with voting rights in the REIT or Group REIT or is entitled to 10% or more of a distribution, and the REIT or Group REIT has not taken reasonable steps to prevent a distribution to such a shareholder, then the REIT or Group REIT shall be deemed as receiving an amount of income equal to the amount of the distribution to the shareholder. This income shall be taxable at the 25% rate. (See 2.3 above)
2. The REIT or Group REIT must maintain a profit financing ratio of at least 1.25:1. Where this requirement is breached, the REIT shall be chargeable to tax at the rate of 25% on the amount by which the property financing costs would have to be reduced for the property financing cost ratio to equal 1.25:1. (See 2.5 above)
3. Where a REIT fails to make the required 85% distribution, the REIT or the principal company of the REIT will be chargeable to tax at 25% on the amount that was not distributed. (See 2.6 above)

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Income from a property rental business is exempt from corporation tax</li> <li>- Residual business income is taxable at mainstream CT rates (i.e. 12.5% on trading profits, 25% on passive income or income from an 'excepted trade')</li> <li>- Deposits of a REIT or a Group REIT are exempt from deposit interest retention tax (DIRT)</li> </ul>	<ul style="list-style-type: none"> <li>- Gains realised on disposals of assets used in the property rental business are not subject to tax</li> <li>- Gains on the disposal of other investment assets are subject to capital gains tax (currently 33%)</li> <li>- Profits from trading in land are taxed at 25%</li> </ul>	<ul style="list-style-type: none"> <li>- Property income dividends paid by the REIT are subject to Dividend Withholding Tax at 20%</li> </ul>

#### Property Rental Income

Income from the property rental business is not subject to corporation tax. Non-rental business income (residual income) will be taxable at the rate of 25% unless such activities constitute a trade (other than an 'excepted trade', as defined by Irish tax law) in which case such profits will be taxable at the 12.5% rate.

#### Capital Gains

Capital gains or losses that arise on the disposal of property used in a REIT's or Group REIT's property rental business are not chargeable to tax.

The REIT or Group REIT may develop property for use in its property rental business. Profits on the disposal of such developed properties may be taxable at the rate of 25% if the cost of such development exceeds 30% of the market value of the property at the date on which the development commenced and the property is sold within three years of the completion of development.

Thus if the development costs do not exceed 30% of the market value of the property at the date on which the development commenced or if the development costs exceed the 30% threshold but are held for at least three years after completion of development, then any gains on disposal will be exempt.

Where properties are acquired which do not form part of the REIT's property rental assets and is not an investment, then profits on the disposal of such assets will be subject to corporation tax at 25%. For example, if a company acquired a portfolio of properties with the intention of disposing of non-core assets, then any profits on such disposals would be subject to corporate tax at 25%.

#### Withholding tax

Dividend Withholding Tax (DWT) at 20% will be levied on distributions made to all investors unless the investor is an exempt qualifying investor such as a pension fund and certain investment funds. For non-resident investors, this should be their final liability to tax. Certain non-residents may be entitled under their tax treaties to recover some of this DWT.

## Other taxes

Irish stamp duty of 1% will apply to the purchase of shares in a REIT. The REIT itself will pay stamp duty on the purchase of Irish property. The rate of stamp duty on non-residential property was increased by the Finance Act 2017 from 2% to 6%. Land acquired for residential development is generally treated as commercial land for stamp duty purposes. However, the Finance Act 2017 provides for a stamp duty refund of the difference between 6% and 2% in respect of land acquired for the development of residential property where certain conditions are met. The rate of stamp duty for residential property will be 1% on the first EUR 1 million, and 2% on any amount in excess of EUR 1 million.

## Foreign tax-resident companies

As mentioned above, a foreign tax resident company may be considered part of a Group REIT. Broadly, companies that are tax-resident outside of Ireland should not be within the charge to Irish corporation tax. However, such entities would be subject to the tax regimes in the countries in which they do business and therefore may suffer foreign tax. On repatriation to Ireland, such dividends to the extent paid out of property rental profits should be exempt. Dividends received by an Irish tax resident company that are paid out of non-rental profits including capital gains will be subject to tax in Ireland. A credit for foreign taxation should be available in Ireland to set against Irish tax.

## Accounting rules

As the REIT/Group REIT will be listed on an EU stock exchange, it will be required to prepare consolidated accounts under International Financial Reporting Standards (IFRS).

For periods commencing on or after January 1, 2015, the individual accounts of the parent company and any of its subsidiaries must be prepared under FRS101, FRS102 or IFRS.

The consolidated accounts prepared under IFRS will be used in determining the 75% asset/income test. Thus assets/income such as inter-company debt receivables, interest and dividends should not be taken into account in determining the 75% asset/income test.

## Transition regulations

### Conversion into REIT status

Subject to the below, there is no conversion charge on converting a company to a REIT

However, where the company held property prior to conversion, then that property is deemed to have been sold by the company at market value at the date of conversion. Any gain would be subject to tax at 33%.

Due to the recovering nature of the Irish property market, it may be common that the conversion triggers losses.

## b. Registration duties

### Registration duties

Irish stamp duty of 1% will apply to the purchase of shares in a REIT

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Distributions from an Irish REIT to an Irish corporate shareholder will be chargeable to tax at 25%, with some exceptions</li> <li>- Generally, capital gains tax at 33% will apply on any gains arising on a disposal of shares in a REIT</li> </ul>	<ul style="list-style-type: none"> <li>- Irish resident shareholders will be liable to income tax at marginal rates plus Universal Social Charge (USC) and Pay Related Social Insurance (PRSI)</li> <li>- capital gains tax at 33% will apply on any gains arising on a disposal of shares</li> </ul>	Withholding tax is deducted at 20% on Property Income Dividends

#### Corporate shareholder

Subject to certain exceptions, Irish resident corporate shareholders will be liable to corporation tax at the rate of 25% on income distributions from a REIT.

Capital gains arising on the disposal of shares of an Irish REIT will be taxable at 33%.

#### Individual shareholder

Irish resident individual shareholders in a REIT will be liable to income tax on distributions at their marginal rates together with USC and PRSI. The Irish resident individual shareholders will receive a tax credit in Ireland for the withholding tax deducted by the REIT on payment of the dividend.

Capital gains arising on the disposal of shares of an Irish REIT will be taxable at 33%.

#### Withholding tax

Withholding tax is deducted at 20% on Property Income Dividends. Irish resident individuals and corporates will be able to credit this withholding tax against their final tax liability.

Non-Property Income Dividends will be subject to the normal Dividend Withholding Tax (DWT) rules. Thus DWT will be deducted from dividends made to individuals. Generally, DWT will not be deductible on dividends made to corporates subject to certain conditions being met.

Irish resident pension funds, insurance companies and other exempt persons will be exempt from DWT.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- 20% final withholding tax for property income dividends</li> <li>- Disposal of shares in an Irish REIT is outside the scope of Irish capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- 20% final withholding tax for property income dividends</li> <li>- Disposal of shares in an Irish REIT is outside the scope of Irish capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- Certain non-residents may be entitled to recover some or all of the DWT deducted from the Irish Revenue Commissioners</li> <li>- Otherwise, a foreign investor may be in a position to claim credit for DWT against taxes in their country of residence</li> </ul>

## Corporate shareholder

Foreign shareholders will receive property income dividends net of 20% withholding tax.

Certain shareholders may be in a position to claim a refund or part refund of this DWT from the Irish Revenue Commissioners depending on the provisions of the relevant tax treaty. Note in this regard that Ireland deposited its ratification instrument with the OECD for the Multi-Lateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS ('MLI') on 29 January 2019. The MLI, therefore, needs to be considered in conjunction with the relevant double tax treaty when considering tax treaty relief.

Otherwise, a foreign tax credit should be available against the foreign tax charged on those profits (depending on the rules of the country in which the corporate is resident).

Other non-property income dividends will be subject to DWT, but generally, a corporate resident in an EU or treaty country or a corporate not resident in a non-EU/treaty country but under the control of persons resident in an EU or treaty country is exempt from DWT.

Normally, the disposal of shares deriving their value from land and buildings in Ireland would be subject to CGT in Ireland. However, as the REIT will be a public listed company, CGT will not arise on the disposal of such shares.

## Individual shareholders

Foreign shareholders will receive property income dividends net of 20% withholding tax.

Certain shareholders may be in a position to claim a refund or part refund of this DWT from the Irish Revenue Commissioners depending on the provisions of the relevant tax treaty and the MLI.

Otherwise, a foreign tax credit should be available against the foreign tax charged on those profits (depending on the rules of the foreign country in which the individual is resident).

Other non-property income dividends will be subject to DWT, but generally, an individual resident in an EU or treaty country should be exempt from DWT.

Normally, the disposal of shares deriving their value from land and buildings in Ireland would be subject to CGT in Ireland. However, as the REIT will be a public listed company, CGT will not arise on the disposal of such shares.

## Withholding tax

In respect of property income distributions, DWT of 20% will be charged on distributions made to a corporate or individual non-resident shareholder. Treaty relief may be claimed retrospectively.

DWT will apply on distributions made out of other non-property income subject to any of the normal exemptions.



## 5 Tax treatment of foreign REITs and their domestic shareholders

Foreign REIT	Corporate shareholder	Individual shareholder
Taxed under normal Irish tax rules	May be tax-exempt	Subject to income tax, PRSI and USC

### Foreign REIT

A REIT resident outside Ireland and investing in Irish property will be taxable under normal Irish rules as a non-resident landlord. Tenants will be obliged to pay the non-resident landlord rent net of income tax of 20%. The income tax should be paid by the tenant to the Revenue Commissioners.

Alternatively, the non-resident landlord may appoint a local agent. In this case, the tenant will pay the rent gross, but the agent will be assessed to Irish tax on the rental income.

Gains on the disposal of Irish property will be subject to Irish capital gains tax at 33%. However, where a property was acquired in the period from December 7, 2011 to December 31, 2014, and continues in the ownership of the person who acquired that property for a period of at least four years from the date it was acquired, then any uplift in the value of the property during that four-year period will be exempt from capital gains tax. This exemption can be extended to seven years where a relevant property is held for seven years from the date of acquisition. The tapering relief applies to properties held for longer than seven years. This provision has not been extended beyond December 31, 2014.

### Corporate shareholder

Distributions from a foreign REIT will be subject to Irish tax at the rate of 25%. Credit against the Irish tax liability should be available for foreign taxes paid.

Capital gains arising on the disposal of shares of a foreign REIT will be taxable at 33%.

### Individual shareholder

Income distribution from a foreign REIT will be liable to Irish income tax at the tax payer's marginal rate together with PRSI and USC. A credit against the Irish tax liability may be available for foreign taxes paid.

Capital gains arising on the disposal of shares in a foreign REIT will be taxable at 33%. ■

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The Deloitte logo, featuring the word "Deloitte" in a bold, black, sans-serif font, followed by a green dot.

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SIIQ

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
SIIQ/SIINQ	2007	Law No. 296/2006 and subsequently issued Regulations and Guidance Amended by Law Decree No. 133/2014 (converted into Law No. 164/2014)	Corporate entity

The Italian REIT regime was introduced in Italy by the Law No. 296/2006, which provides for a special civil law and tax regime applicable to Italian listed real estate investment companies, that meet certain requirements defined by law and whose main activity is the rental of real estate properties (Società d'Investimento Immobiliare Quotate, SIIQs).

The SIIQ regime is applicable also to non-listed Italian real estate investment companies that are subsidiaries of SIIQs, if certain conditions are met (Società d'investimento immobiliare non quotate, SIINQs).

The SIIQ regime has been subsequently amended by the Law Decree No. 133/2014 (converted into Law No. 164/2014), which entered into force in September 2014 and whose principal purposes were to faster the use of this investment vehicle in the Italian real estate sector and to increase the permeability between SIIQs and Italian real estate investment funds. With such amendment, specific provisions regarding the conversion of real estate investment funds in the liquidation phase into SIIQs have been introduced, allowing the contribution of the real estate assets to SIIQs with almost no tax burdens both for direct and indirect taxes purposes.

The legal framework for SIIQs and SIINQs also includes the secondary legislation (Decree of the Ministry of Finance No. 174/2007), which, at the date hereof, has not been amended yet in order to implement the changes introduced by Law Decree No. 133/2014.

The Revenue Agency provided clarifications regarding the SIIQ regime with the Circular Letter No. 8/E/2008 and with the Circular Letter No. 32/E/2015 (the latter in order to clarify and implement the rules introduced with the Law Decree No. 133/2014). Moreover, with the Regulations of December 18, 2015, the Revenue Agency provided for the form to be filed in order to exercise the option for the SIIQ and SIINQ regime.

## Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
Italy	3	1	EUR 966	0.02%

## Top REITs\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield	% of Global REIT Index
Igd - Immobiliare Grande Distribuzione	EUR 639.98	-8.84%	8.62%	0.02%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Election for the SIIQ and SIINQ regime must be filed with the Revenue Agency  
Certain conditions are required for SIIQ status

An eligible listed real estate investment company must file a specific form with the Italian Revenue Agency by the end of the fiscal year prior to the year in which the company shall apply the SIIQ regime. As anticipated, the form and the relative submission rules have been amended at the end of 2015 in order to take into consideration the changes in the requirements to be met to adopt the SIIQ regime.

SIINQs must opt for the special regime jointly with the SIIQ parent company. In such regard, the Revenue Agency (Circular Letter n. 8/E/2008) clarified that ‘jointly’ must be intended as for the same or for a subsequent tax period to the tax period for which the SIIQ exercised the option.

It is not necessary that all the requirements to obtain the SIIQ status are met at the date of the filing of the form, since specific provisions have been introduced by the Law Decree No. 133/2014 extending the grace period during which such requirements must be met (so-called ‘preliminary SIIQ regime’ – see par. 2.3).

### b. Legal form/minimum share capital

Legal form	Minimum share capital
Joint-stock company	Listing requirements (for SIIQs)

#### Legal form

The SIIQ must be a joint-stock company (Società per Azioni) listed on a regulated market.

Following the entry into the SIIQ regime, the company’s name must include the words ‘Società d’Investimento Immobiliare Quotata’ or ‘SIIQ’; therefore, the company’s by-law must be amended accordingly (together with other amendments required by law).

The same requirements in terms of legal form (Società per azioni) and by-laws, amendments must also be satisfied by the SIINQs.

Moreover, in 2009, the SIIQ regime was amended (by Article 12 of the Law Decree No. 135/2009 converted into Law No. 166/2009) in order to extend the SIIQ regime also to permanent Italian establishments of foreign REITS established in EU/EEA States which allow an adequate exchange of information with Italy.

#### Minimum share capital

The ordinary listing requirements in respect of share capital are applicable to SIIQs.

### c. Shareholders' requirements/listing requirements

Shareholders' requirements	Listing mandatory	Foreign Shareholders' Restrictions
<ul style="list-style-type: none"> <li>- At least 25% of the shares must be 'widely held'</li> <li>- A single shareholder is not allowed to own more than 60% of voting rights and profit participation rights</li> <li>- For SIINQs, at least 95% of voting rights and profit participation rights must be owned by a SIIQ</li> </ul>	<ul style="list-style-type: none"> <li>- Yes for the parent company (SIIQ)</li> <li>- Not for subsidiaries (SIINQ)</li> </ul>	No specific foreign shareholders restrictions has been enacted

#### Shareholders' requirements

No single shareholder should hold, directly or indirectly, more than 60% of voting rights and profit participation rights.

The 60% shareholding requirement must be satisfied without interruption. An exception is provided if such requirement is not satisfied because of M&A transactions or capital market transactions since, in this case, the SIIQ regime is suspended.

At least 25% of the SIIQ shares must be owned by shareholders that individually hold, directly or indirectly, less than 2% of voting rights and profit participation rights. It is worth noting that the 2% threshold is required for access to the SIIQ regime, but it does not affect the SIIQ status after the election. The 25% requirement is not applicable to companies already listed on regulated markets.

It is worth noting that Law Decree No. 133/2014 has increased the maximum holding threshold allowed to a single shareholder from the previous 51% to the current 60% and has decreased the free-floating threshold from the previous 35% to the current 25%.

The aforesaid ownership requirements must be met within the end of the first fiscal year of application of SIIQ regime. The SIIQ regime applies since the beginning of such fiscal year.

However, Law Decree No.133/2014 has introduced a 'preliminary SIIQ regime' extending the timeframe within which the ownership requirements may be satisfied.

In particular, provided that the 25% free-floating threshold is met within the end of the first fiscal year for which the option has been exercised, the 60% shareholding requirement must be met within 24 following months. In this case, the SIIQ regime has effect from the first day of the fiscal year in which the 60% threshold is satisfied.

Until both the ownership requirements are met, the Italian corporate income tax (IRES – standard rate 24%) and Italian regional tax on business activities (IRAP – standard rate 3,9%) are due pursuant to the ordinary rules.

On the contrary, the 'entry tax' due for access to the SIIQ regime (see par. 3.2) and other taxes (substitutive tax for direct taxes purposes and mortgage and cadastral taxes on the contribution of real estate assets to the SIIQ) are applied according to the more favourable rules set forth by the SIIQ regime. In the case that the ownership requirements are not timely met, such taxes are re-determined on the basis of the ordinary rules and the amounts already paid can be offset as a tax credit.

With regard to ownership requirements for SIINQs, a SIIQ must own (also jointly with other SIIQs) at least 95% of the voting rights and profit participation rights of the SIINQ. Moreover, following the access to the special regime, the SIINQs must opt for the consolidation for tax purposes with the SIIQ parent company.

## Listing requirements

SIIQ shares must be listed on the Italian stock exchange (Borsa Italiana) or any other recognized stock exchange of the EU/EEA Countries which allow an adequate exchange of information with Italy.

SIINQ shares must not be listed on a stock exchange.

### d. Asset level/activity test

#### Restrictions on activities/investments

- 80% real estate assets requirement (asset test)
- 80% real estate income requirement (profit test)

At least 80% of the SIIQ's assets must consist of ('asset test'):

- i. real estate properties to be leased (ownership or other rights);
- ii. participations accounted as fixed assets in SIIQs/SIINQs/Italian real estate investment funds whose real estate assets held for lease or participations in real estate investment companies, real estate investment funds, SIIQs, SIINQs are at least 80% of the total assets ('Qualifying REIFs').

At least 80% of SIIQ's positive components of income must be ('profit test'):

- i. proceeds from lease activity;
- ii. dividends from lease activity raising from participations in SIIQs/SIINQs/Qualifying REIFs;
- iii. capital gains realised on the disposal of real estate properties held for lease or of participations in SIIQs/SIINQs/Qualifying REIFs.

Asset test and profit test must be calculated on the basis of the financial statements (balance sheet and income statement), starting from the first year of application of the SIIQ regime. The Decree of the Ministry of Finance No. 174/2007 and the Revenue Agency (Circular Letter No. 32/E/2015) provide for further details regarding the tests (in particular, regarding assets and positive components of income to be excluded from the calculation).

As far as asset test is concerned, both non-Italian real estate properties held for leasing and real estate assets under construction or subject to renovation works are included in the asset test if they are intended to be leased.

Participations into Qualifying REIFs and proceeds from leasing activity deriving from such participations have been included, respectively, into the asset test and profit test by the Law Decree No. 133/2014. In such regard, the Revenue Agency (Circular Letter No. 32/E/2015) clarified that real estate SICAFs (i.e. investment companies with fixed capital, introduced in Italy following the implementation of Directive 2011/61/EU – AIFM Directive) are relevant for the purposes of asset test and profit test if they have the requirements to be considered 'Qualifying SICAFs' under the SIIQ regime (see point (ii) above), since they are subject to the same tax regime provided for real estate investment funds.

Moreover, pursuant to Law Decree No. 133/2014, the profit test calculation has been amended in order to include capital gains on real estate properties and capital gains on participations in SIIQ/SIINQ/Qualifying REIFs/Qualifying SICAFs.

The same tests must be satisfied by the SIINQs.

There are no specific restrictions regarding the activities that may be carried out by SIIQs and SIINQs. However, only the income deriving from the leasing activity would be exempt from taxation. Indeed, with reference to such income SIIQs and SIINQs benefit from a favourable ‘flow-through’ tax treatment (26% withholding tax is applied to distributions). On the contrary, income deriving from activities different from the leasing activity is subject to ordinary income taxes (see par. 3.1).

#### e. Leverage

Leverage
The leverage cannot exceed the ratio resulting from the company’s by-law

The company’s By-law (after the election for the SIIQ regime) shall mandatory include the maximum leverage ratio allowed. This provision is aimed at protecting SIIQ’s investors through the effective control of National Security and Exchange Commission (CONSOB) and of Bank of Italy.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
70% of net profits deriving from the leasing activity	50% of capital gains from the leasing activity	<ul style="list-style-type: none"> <li>- Net profits: annually</li> <li>- Capital gains: in the two years subsequent to the disposal</li> </ul>

#### Operative income

SIIQs, each year, must distribute at least 70% (before the amendments introduced by Law Decree No. 133/2014 such rate was 85%) of the lower of:

- net profits deriving from the leasing activity or from participation in other SIIQs, SIINQs, Qualifying REIFs, Qualifying SICAFs; and
- total profits available for distribution, according to Italian civil law provisions.

Income is calculated by the SIIQ as IFRS adopter and, therefore, no depreciation of assets is admitted pursuant to IAS 40 (such as increasing profit distribution obligations).

#### Capital gains

SIIQs must distribute at least 50% of net capital gains realised on the disposal of real estate properties held for leasing or on the disposal of participations in SIIQs, SIINQs, Qualifying REIFs and Qualifying SICAFs, in the two years subsequent to the disposal. Such an obligation has been introduced by Law Decree No. 133/2014.

The Revenue Agency (Circular Letter No. 32/E/2015) clarified that unrealised capital gains accounted in the income statement according to the application of the ‘fair value model’ under the IAS 40 for real estate properties are not subject to distribution obligations (until they are effectively realised through the disposal of the assets).



The described distribution obligations regarding operative income and capital gains also operate for SIINQs.

#### g. Sanctions

Penalties/loss of status rules
Loss of SIIQ/SIINQ status
No penalties

The withdrawal of the SIIQ/SIINQ status occurs if the company fails: (i) to distribute at least 70% of the nett profits or (ii) to distribute at least 50% of the net capital gains. In these events, the SIIQ status ceases starting from the year in which operative income/capital gains have been accrued.

Furthermore, the SIIQ/SIINQ loses its status if it does not meet the asset test or the profit test for three consecutive years (grace period extended from two to three years by Law Decree No. 133/2014).

Finally, as regards SIIQs, they must uninterruptedly meet the maximum holding requirement of 60% (on the contrary the free-floating requirement may be satisfied only at the moment of the option for the SIIQ regime, as described at par. 2.3).

The forfeiture of the SIINQ status occurs, in addition to the cases mentioned above, if the company ceases to be participated for at least 95% by a SIIQ or ceases to have in place the tax consolidation regime with the controlling SIIQ.

There are no specific penalties in case of withdrawal of the SIIQ or SIINQ status.

## 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Income deriving from rental or leasing activity is tax-exempt</li> <li>- Other income is subject to the ordinary corporate and local taxation</li> </ul>	<ul style="list-style-type: none"> <li>- Capital gains deriving from the disposal of rented real estate properties and of participations in SIIQs, SIINQs, Qualifying REIFs, Qualifying SICAFs are exempt</li> <li>- Other capital gains are subject to the ordinary corporate taxation</li> </ul>	<p>Proceeds from leasing activity distributed by Qualifying REIFs to SIIQs are not subject to withholding tax</p>

#### Current income

The SIIQ income deriving from the leasing activity and from dividends/proceeds from the leasing activity distributed by SIIQs, SIINQs, Qualifying REIFs, Qualifying SICAFs are exempt from corporate income tax (IRES) and from regional tax on business activities (IRAP). The tax exemption applies from the beginning of the fiscal year in which the SIIQ regime is adopted. Such income will be taxed only in the hands of the shareholders upon distribution applying a withholding tax (at 26% rate), as better described below (par. 4).

The same tax exemption also applies to the lease income realised by SIINQs.

Income deriving from activities different from the leasing activity is subject to ordinary corporate income tax and regional tax on business activities (aggregate 27.9%).

With regard to such portion of income, SIIQs are subject to the ordinary corporate income tax provisions limiting the deduction of interest expenses. In particular, following recent amendments introduced by Legislative Decree No. 142/2018, interest expenses (net of interest income) are deductible from IRES taxable base up to 30% of the gross operative income determined for tax purposes (risultato operativo lordo della gestione caratteristica – ROL, approximately, equal to the EBITDA) of the relevant tax period. This provision may not apply to interest expenses on loans secured by a mortgage on real estate assets held for leasing under certain conditions that should be verified on a case by case basis.

## Capital gains

Capital gains on the disposal of rented real estate properties and of participations in SIIQs, SIINQs, Qualifying REIFs and Qualifying SICAFs are exempt from corporate income tax (IRES) and from regional tax on business activities (IRAP).

Capital gains different from those deriving from leasing activity are fully taxable according to the ordinary capital gains provisions.

## Other taxes

Excluding income taxes, other taxes (e.g. property taxes (IMU and TASI)) ordinarily apply.

## Withholding tax

No withholding tax is levied on dividends received by the SIIQ from other SIIQs and SIINQs deriving from rental activities.

Moreover, according to the amendments introduced by the Law Decree No. 133/2014, the 26% withholding tax ordinarily applied on proceeds distributed by Italian real estate investment funds is not applicable on proceeds from leasing activity distributed by Qualifying REIFs and Qualifying SICAFs to SIIQs or SIINQs.

Dividends distributed to SIIQs or SIINQs by other entities are subject to the ordinary regime.

## Accounting rules

Since SIIQs are Italian public listed companies, they must adopt IFRS standards. In addition, SIIQs shall set-up two different sets of accounts with the purpose to distinguish the net profits deriving from the 'exempt' activity (i.e. the activities which can benefit from the tax flow-through treatment), and any other activities carried on.

Moreover, pursuant to the special regime, also SIINQs are required to adopt the IFRS standards for their financial statements.

## b. Entry tax

### Conversion into REIT status

- 20% substitute tax on real estate properties contributed to SIIQs
- 20% 'entry tax'

Real estate properties contributed to a SIIQ can be subject to a 20% substitute tax on realised capital gains instead of the ordinary taxation (by the option of the conferrer), provided that the SIIQ retains the assets for a minimum three-year period.

Moreover, companies opting for the SIIQ regime are required to align the fiscal value of their real estate assets to their fair value, determined at the beginning of the first fiscal year in which the SIIQ regime applies (step-up of the fiscal value). Such increase of the fiscal value may be alternatively subject to a 20% substitutive tax (so-called 'entry tax') or included in the taxable income for corporate income tax (IRES) and from regional tax on business activities (IRAP) purposes (under the ordinary rules).

If the capital gains are subject to the 20% entry tax (which is payable in five equal annual instalments), the higher fiscal value of the assets will be effective from the fourth period following that in which the company opted for the SIIQ regime. If the assets are sold before such date, capital gains are taxed at the ordinary tax rate (i.e. IRES and IRAP at an aggregate rate of 27.9%) while the 20% entry tax already paid can be offset as a tax credit. Thus, applying for the SIIQ regime offers the opportunity of reducing the tax burden on latent capital gains.

On the contrary, if capital gains are included in the taxable income, they are subject to the ordinary IRES and IRAP rules for the taxation of capital gains.

In addition, tax losses realised before the election for the SIIQ regime can be used to offset the tax base for the calculation of the 20% entry tax under the ordinary limits (i.e. within the limit of 80% of the taxable income, as clarified by the Revenue Agency in the Circular Letter No. 32/E/2015).

The same provisions also apply to SIINQ.

## c. Registration duties

### Registration duties

- Commercial buildings: VAT exempt (or subject to a 22% or 10% VAT under certain circumstances), EUR 200 registration tax, 2% mortgage and cadastral taxes
- Residential buildings: (i) if the transfer is subject VAT (22% or 10% under certain circumstances), registration tax and mortgage and cadastral taxes are due at the fixed amount (EUR 200 each); (ii) if the transfer is VAT exempt, registration tax is due at the rate of 9%, mortgage and cadastral taxes are due at the fixed amount of EUR 50 each

Indirect taxes are applied to the transfers of real estate properties to a SIIQ as follows:

- Commercial buildings are exempt from VAT, but it is possible to opt for the VAT application (22% or 10%). In addition, the registration tax is applied at the lump sum of EUR 200 and, irrespective of the VAT application or not, 1.5% mortgage tax and 0.5% cadastral tax are levied. In the case that commercial buildings are transferred to a SIIQ from the companies which built them or carried out some restructuring works in the preceding five years VAT compulsorily applies (at the rate of 22% or 10%).

- Residential buildings are exempt from VAT, registration tax is applicable at 9% (in any case the amount cannot be lower than EUR 1,000); mortgage and cadastral taxes are applicable at a lump sum of EUR 50 each. Registration, mortgage and cadastral taxes applies at the lump sum of EUR 200 if VAT compulsorily applies (since the residential buildings are transferred by the companies which built them or carried out some restructuring works over the preceding five years) or if VAT applies by option (at a rate of 22% or 10% under certain conditions).

The contribution to a SIIQ of a portfolio consisting mainly of rented real estate properties falls out of the scope of VAT and is subject to registration, mortgage and cadastral taxes at the fixed amount (EUR 200 each).

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholders

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Full taxation of dividends from exempted income</li> <li>- Dividends from non-exempted income subject to ordinary dividend taxation rules</li> <li>- Full taxation of capital gains (participation exemption not applicable)</li> </ul>	<ul style="list-style-type: none"> <li>- A final withholding tax is levied on SIIQ exempted income</li> <li>- Dividends from non-exempted income are subject to ordinary dividend taxation rules</li> <li>- Full taxation of capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- 26% withholding tax on the distribution of exempted SIIQ income</li> <li>- Corporate and business shareholders can credit the withheld taxes</li> </ul>

#### Corporate shareholder

Dividends deriving from the SIIQ's non-exempted income are subject to the ordinary tax regime; therefore, they are subject to corporate income tax (IRES at 24%) on the limited amount of 5% of such dividends (i.e. effective IRES rate of 1.20%).

Dividends deriving from the SIIQ's exempted income are fully taxable in the hands of corporate shareholders at IRES ordinary rate (24%), and the 26% tax withheld upon distribution (on account) is offset against corporate income tax.

Capital gains resulting from the disposal of SIIQ shares are fully subject to IRES at the ordinary tax rate (24%) since the participation exemption regime is not applicable by law on SIIQs shares.

#### Individual shareholder

Dividends deriving from the SIIQ's non-exempted income are subject to the ordinary tax regime.

In case the individual holds the SIIQ shares in the course of a business activity, dividends from the SIIQ's non-exempted income are subject to individual income tax (IRPEF) at progressive rates on the limited amount of 49.72% of such dividends for dividends paid out of profits realized before 2017 and of 58.14% for dividends paid out of profits realized from 2017.

In case the individual holds the SIIQ shares not in the course of business activity, following the amendments introduced by Art. 1(999-1006) of Law No. 205/2017, dividends from the SIIQ's non-exempted income are subject to a final 26% withholding tax (for dividends paid from 1 January 2018). However, a transitional regime is provided if (i) the dividends are paid out from profits realised until the

fiscal year ending on December 31, 2017 and (ii) the profit distribution resolution is adopted between January 1, 2018 and December 31, 2022 and (iii) the participation involves voting rights >2% and participation rights >5% (i.e. ‘affiliated shareholding’). In this case, dividends are subject to individual income tax (IRPEF) at progressive rates on a limited amount (49.72%/58.14%).

Dividends deriving from the SIIQ’s exempted income are subject to a specific regime provided for by Law No. 296/2006.

In case the individual holds the SIIQ shares in the course of business activity, dividends from the SIIQ’s exempted income are fully taxable in the hands of the shareholder at IRPEF progressive rates, and the 26% tax withheld at distribution (on account) is offset against individual income taxes.

In case the individual holds SIIQ shares not in the course of business activity, dividends from the SIIQ’s exempted income are subject to a final 26% withholding tax upon distribution.

Capital gains realised on the disposal of SIIQ shares by individuals in the course of business activity are fully subject to IRPEF at progressive rates.

Capital gains realised on the disposal of SIIQ shares by individuals not in the course of business activity are subject to a 26% substitute tax (from January 1, 2019, following the amendments introduced by Art. 1(999-1006) of Law No. 205/2017).

As a final remark, the Law No. 145/2018 has recently amended the exemption from income taxes for resident individuals investing in special long-term savings schemes (piani di risparmio a lungo termine – PIR). In particular, a PIR is validly established if specific requirements and parameters provided by the law are met. Inter alia, at least 70% of the investments must be Italian companies of which (i) 5% must be invested in financial instruments traded on multilateral systems issued by small or medium-sized enterprises (piccole medie imprese – PMI), as defined by the Recommendation 2003/361/CE; (ii) 30% must be companies whose shares are not listed in the Italian index FTSE MIB or in similar indexes of other regulated markets and (iii) 5% must be invested in shares of Venture Capital Funds resident in Italy or in EU/EEA Countries. In this respect, also interests in Italian entities investing in real estate assets are considered eligible investments for the PIR regime.

## Other taxes

No other taxes are levied.

## Withholding tax

As anticipated, a 26% withholding tax applies on dividends paid out of the SIIQ’s tax-exempted income upon distribution.

The withholding tax is applied as final for individual shareholders not carrying out a business activity. While it is applied on account for corporate shareholders and individual shareholders carrying out a business activity (they credit the withheld taxes to offset corporate income tax and individual income tax).

Distributions to pension funds and collective investment funds established in Italy are exempt from the withholding tax.

The withholding tax is levied by the financial intermediaries where the SIIQ shares are deposited.

## b. Non-resident shareholders

Corporate shareholder	Individual shareholder	Withholding tax
Final withholding tax	Final withholding tax	<ul style="list-style-type: none"> <li>- Double tax treaty benefits apply</li> <li>- Parent-Subsidiary Directive not applicable</li> </ul>

### Corporate shareholder

Dividends paid out of the SIIQ's non-exempted income are subject to the ordinary tax regime that foresees a 26% final withholding tax (provided that non-residents do not have a permanent establishment in Italy). This withholding tax rate may be reduced to 1.20% rate if the dividends are paid to companies that are resident in EU or in EEA Countries, provided that an adequate exchange of information with Italian Tax Authorities exists.

Dividends deriving from the SIIQ's exempted income are subject to a final 26% withholding tax upon distribution. Double tax treaties apply.

Capital gains deriving from the sale of shares in SIIQs are subject to the tax regime ordinarily applicable to the sale of Italian shares (including certain domestic and Double tax treaty exemptions available to non-residents). Double tax treaty protection applies in most circumstances.

### Individual shareholder

Dividends paid out of SIIQ's non-exempted income are subject to the ordinary applicable tax regime which provides a 26% final withholding tax. Dividends deriving from SIIQs exempted income will be subject to a final 26% withholding tax when distributed under the SIIQ regime. Double tax treaties apply.

### Withholding tax

Withholding taxes on dividends paid to non-resident shareholders are final, provided that the shares are not assets of a permanent establishment in Italy.

Non-resident shareholders may claim the Double tax treaties relief on the dividends (after amendments introduced by the Law Decree No. 133/2014).

The applicability of the Parent-Subsidiary Directive under the SIIQ regime is not allowed for the portion referring to dividends from the SIIQ exempt income. The Parent-Subsidiary Directive is only applicable to the portion of dividends from the SIIQ non-exempt income.

## 5 SIIQ/REIT cross-border investments

Foreign REIT	Corporate shareholder	Individual shareholder
It follows the ordinary taxation rule at a rate of 24%	1.20% taxation may apply; an analysis of the foreign REIT is required	In principle, ordinary taxation rules for investments in non-resident entities; foreign tax credit may be available, but an analysis of the foreign REIT is required

## Foreign REIT

It follows the ordinary income tax rule applicable to non-residents. As a consequence, any income deriving from immovable property situated in Italy will be subject to the general 24% corporate income tax rate applicable to non-resident entities, if not covered by the provisions of any double tax treaty.

Moreover, as regards foreign investors, the Law Decree No. 133/2014 amended the provision which extends the SIIQ regime to foreign REITs resident in EU/EEA white-list countries and having in Italy a permanent establishment. In particular, access to the SIIQ regime is also allowed to foreign REITs operating through a permanent establishment which carries out the leasing activity in Italy exclusively through investments in Italian SIIQs. Consequently, starting from the fiscal year for which the option is effective, the lease income connected with the permanent establishment in Italy is subject to a 20% substitute tax. Under the new provisions, the permanent establishment may carry out its real estate activity in Italy only through subsidiaries (SIIQs).

## Corporate shareholder

Subject to taxation in Italy. Domestic corporate shareholder receiving dividend income from certain foreign REIT may benefit from a 95% exemption (if certain conditions are met). The remaining 5% would be taxed at the ordinary 24% corporate income tax rate. Thus, the effective domestic taxation of dividends received from a foreign REIT would be equal to 1.20%. An exception is made for REITs resident in a black-listed Country. In this case, the 95% exemption would not apply, and the full amount of the dividends distributed would be subject to a 24% ordinary corporate tax rate. The foreign tax credit will be limited to the taxable amount.

## Individual shareholder

Subject to taxation in Italy. In principle, the ordinary taxation rules provided for individual shareholders investing in non-resident entities apply (26% withholding tax or taxation on a limited amount of 49.72% or 58.14%). A foreign tax credit may be available. An analysis of the foreign REIT is required. ■

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A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction/history/REIT type

REIT objective	Enacted year	Citation	REIT type	REIT market
REIT for non-professional investors	2008	Law on Collective Investment Undertakings	Investment Company/ Investment Fund	1 existing fund
REIT for informed investors	2013	Law on Collective Investment Undertakings for Informed Investors	Investment Company/ Investment Fund	22 existing funds
REIT for professional investors	2013	Law on Alternative Investment Fund Managers	Investment Company/ Investment Fund	0 existing funds

On November 11, 2007, Lithuanian Parliament amended the Law on Collective Investment Undertakings, which came into force on March 1, 2008. The law regulates the activities of collective investment undertakings which shares/units may be traded to non-professional investors. According to the law, a non-professional investor is an investor that does not have sufficient investing experience, therefore, subject to additional investors' protection measures.

The Law on Collective Investment Undertakings regulates the activities of special collective investment undertakings for non-professional investors, including the activities of Real Estate Investment Trusts (the REIT) for non-professional investors.

On June 18, 2013, the Law on Collective Investment Undertakings for Informed Investors was introduced into Lithuanian legislation, which came into force on July 1, 2013. The law regulates the activities of collective investment undertakings for informed investors. According to the law, an informed investor is (1) a professional investor (as described in MiFID); (2) a natural person who has confirmed that he understands his status and (i) invests at least EUR 125,000 or (ii) receives a confirmation from a financial institution that he understands the risks; or (3) a legal person who has confirmed that he understands his status and invests at least EUR 125,000.

The Law on Collective Investment Undertakings for Informed Investors regulates the activities of collective investment undertakings for informed investors, including the activities of REIT for informed investors.

On July 1, 2013, the Law on Management Companies of Collective Investment Undertakings for Professional Investors was introduced into Lithuanian legislation (on February 1, 2019, the name of the law was changed to Law on Alternative Investment Fund Managers). The law regulates the activities of collective investment undertakings by which shares/units may be traded only to professional investors (as described in MiFID).

The Law on Alternative Investment Fund Managers regulates the activities of collective investment undertakings for professional investors, including the activities of REIT for professional investors.

Since the Law on Collective Investment Undertakings, the Law on Collective Investment Undertakings for Informed Investors and the Law on Alternative Investment Fund Managers do not provide for a new form of entity, REITs for non-professional investors as well as for informed investors or professional investors are incorporated as a legal entity or an investment fund, managed by a management company or without management company (investment company may manage itself and is called investment company-manager).

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Approval from the Bank of Lithuania

In order to become eligible to the regime, entities are required to have special collective investment undertaking status, which could be either (1) open-ended (variable capital investment company or open-ended investment fund), or (2) closed-ended (closed-ended investment company or closed-ended investment fund).

A variable capital investment company/open-ended investment fund is defined as an entity whose shareholders/co-owners have the right to request at any time that their shares/investment units be issued or redeemed. Also, the amount of capital of variable capital investment company varies depending on the issue and redemption of shares.

A closed-ended investment company/closed-ended investment fund is defined as an entity with a fixed number of shares/investment units that are redeemed at the end of its activity or at any other time indicated in the articles of incorporation and are not redeemed upon the request of the investor.

In order to have the status of REIT, the investment company or fund's management company has to obtain a license (permit) from the Bank of Lithuania. The application for the license shall be accompanied by the information about the company, its shareholders, members of the management bodies, the company's program of their development and activities, initial capital and other documents, information and explanations specified in the licensing regulations approved by the Bank of Lithuania.

The bylaws or rules of the REIT must contain a number of specific provisions that are verified by the Bank of Lithuania during the procedure of granting a license for the activities.

The Bank of Lithuania shall notify the applicant of its consent or refusal to grant the license within 3-6 months from the filing of all documents, depending on the type of the REIT.

## Legal form/minimum share capital

REIT objective	Legal form	Minimum share capital	Net asset value (NAV)
REIT for non-professional investors	An investment company or an investment fund managed by a management company	EUR 125,000 for the management company	EUR 300,000 for the investment fund
	An investment company-manager	EUR 300,000 for the investment company-manager	EUR 600,000 for the investment company
REIT for informed investors	An investment company or an investment fund managed by a management company	EUR 2,500 for the management company	EUR 1,000,000 for the investment fund
	An investment company-manager	EUR 1,000,000 for investment company	EUR 1,000,000 for the investment company
REIT for professional investors	An investment company or an investment fund managed by a management company	EUR 125,000 for the management company	Not stated in the law
	an investment company-manager	EUR 300,000 for the investment company	

## Legal form

The REIT for non-professional investors, REIT for informed investors and REIT for professional investors may be organised in different legal forms.

The REIT for non-professional investors should have the form of (1) an investment fund or an investment company managed by a management company or (2) an investment company-manager. Additional statutory and management seat requirements apply.

The REIT for informed investors should have the form of either (1) an investment fund or (2) an investment company that has the form of (1) a joint-stock company or (2) a limited liability company or (3) a partnership. An investment company can be managed by the management company, or it can manage itself. Additional statutory and management seat requirements apply.

The REIT for professional investors should have the form of either (1) an investment fund or (2) an investment company that has the form of (1) a joint-stock company or (2) a limited liability company or (3) a partnership. An investment company can be managed by a management company, or it can manage itself. Additional statutory and management seat requirements apply.

## Minimum share capital

The REIT for non-professional investors, REIT for informed investors and REIT for professional investors are subject to different share capital (monetary contributions of founders) requirements under Lithuanian legislation. Please see paragraph 2.2.

## b. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
Requirements for shareholders and investors	No

### Shareholder requirements

There are specific requirements for those who wish to become shareholders of a licensed entity (management company or investment company), e.g. unquestionable reputation and experience, financial stability.

### Listing requirements

Listing is not a mandatory requirement.

## c. Asset level/activity test

### Asset level/ activity test for non-professional investors

Restrictions on activities/investments of REIT for non-professional investors
<ul style="list-style-type: none"> <li>- No more than 20% of its net assets in securities of other companies</li> <li>- No more than 30% of its net assets in a separate real estate asset or real estate company (exceptions under certain circumstances may apply)</li> <li>- No more than 20% of its net assets in real estate under development</li> <li>- No more than 40% of its net assets in a single real estate property and any assets required for its maintenance</li> <li>- No more than 30% of its net assets in securities issued by a single real estate company including liabilities arising from the transactions with real estate company involving derivatives</li> <li>- No more than 30% of its net assets in the securities in a single real estate company and in the assets that such real estate company has invested in</li> <li>- Further restrictions apply</li> <li>- May invest in real estate abroad</li> </ul>

The REIT for non-professional investors is allowed to invest in the following real estate assets: land, buildings and/or premises constituting separate real estate objects, registered in the name of the investment company, and other tangible assets that are necessary for the operations related to real estate.

Following the provisions of the Law on Collective Investment Undertakings, the assets of the REIT for non-professional investors must consist from of at least four separate real estate objects, i.e. the investment into a single real estate is not allowed. For the purposes of the diversification of assets, the REIT is allowed to invest:

- no more than 20% of its net assets in securities of other companies or other liquid assets;
- no more than 30% of its net assets in a separate real estate asset or real estate company (exceptions under certain circumstances may apply);
- no more than 20% of its net assets in real estate under development;

- no more than 40% of its net assets in a single real estate property and any assets required for its maintenance;
- no more than 30% of its net assets in securities issued by a single real estate company including liabilities arising from the transactions with real estate company involving derivatives;
- no more than 30% of its net assets in the securities in a single real estate company and in the assets that such real estate company has invested in.

If the investments are made through an SPV controlled by the REIT, the diversification requirement should be met at the level of the SPV.

The REIT investments for non-professional investors are not permitted in:

- real estate assets whose ownership is restricted and this may result in the loss of the ownership; or
- real estate assets not registered in the real estate or any other comparable registry.

Specific cases where the investments are allowed to:

Investments abroad	Allowed directly and indirectly*
Investments in residential properties	Allowed
Investments in developments	Allowed
Investments in subsidiaries	Allowed

*\* In case of indirect investment, investments into units of other REITs registered in other EU or EEA member states where they are regulated at as strictly as in Lithuania*

The investment portfolio of a newly incorporated REIT for non-professional investors is allowed, for four years from the approval of its instruments of incorporation, to not comply with the diversification requirements mentioned above. However, in all cases, this should not waive the obligation of a management company and a REIT to invest the assets of a REIT in compliance with the requirements set in the Law on Collective Investment Undertakings.

Restrictions apply regarding investment in the securities of foreign companies incorporated in non-EU or non-EEA member states.

The REIT for non-professional investors is allowed to invest in real estate objects in development if their development is to be finished during an acceptable timeframe.

The REIT for non-professional investors is allowed to invest in:

- securities of companies whose primary business activity is purchase, reconstruction, lease, trade or development of real estate;
- shares or units of other REITs registered in other EU or EEA member states;
- other securities (including shares), money market instruments dealt on regulated markets.

The net assets of REIT for non-professional investors of the investment fund after a six-month period from the beginning of its activities should reach a level of EUR 300,000. The net assets of the REIT as an investment company should reach a level of EUR 600,000 within 12 months from the receipt of the license from the Bank of Lithuania.

The value of real estate assets of REIT shall be calculated every six months (or in the event of essential economic developments or changes in the market price of real estate assets).

Starting February 1, 2019, units of REIT may be settled by a non-cash contribution (assets conforming to the investment policy of a REIT).

### Asset level/ activity test for informed investors

Following the provisions of the Law on Collective Investment Undertakings for Informed Investors, the assets of the REIT for informed investors has to be invested in objects indicated in REITs establishment documents.

REIT for professional investors is not permitted to provide loans to its participants, except for the members of partnership provided that it is stipulated in REITs establishment documents.

The net assets of REIT for informed investors should reach a level of EUR 1,000,000 within one year from the receipt of the license from Bank of Lithuania. The assets and liabilities of REIT for informed investors should reach a level of EUR 2,000,000 within two years from the receipt of the license from Bank of Lithuania.

### d. Leverage

#### Leverage for REIT for non-professional investors

Limited to 50% of the value of real estate

REIT for non-professional investors may borrow up to 50% of the NAV of REIT for the period defined in REIT establishment documents.

Leverage for REIT for informed and professional investors is not regulated by the laws and should be defined in the REIT incorporation documents.

### e. Profit distribution obligations

Operative income	Capital gains	Timing
No requirement	No requirement	No requirement

There is no legal requirement for profit distribution. The procedure of payment of dividends to the investors (periodicity, the share of income allocated for dividends) must be defined in the bylaws or rules of investment of the REIT.

### f. Sanctions

#### Penalties/loss of status rules

- No tax penalties
- Administrative penalties
- Revoking of the license

There are no tax penalties. However, the Bank of Lithuania shall have the right to apply the following measures to a REIT:

- warn about the shortcomings and set a term for their elimination;
- impose administrative penalties:
  - for non-professional investors, up to EUR 5,000,000;
  - for informed investors, up to 10% from annual income for legal person and up to EUR 50,000 for management; and
  - for professional investors, up to 10% from annual income for legal person and up to EUR 50,000 for management.
- temporarily suspend the license for the provision of one or more services;
- revoke the license for the provision of one or more services;
- instruct the management company or investment company to change the manager;
- suspend the distribution or redemption of shares/units;
- prohibit, for periods not longer than three months, the purchase of securities or money market instruments;
- appoint an interim representative of the Bank of Lithuania for the supervision of the activity.

### 3 Tax treatment at the level of the REIT<sup>1</sup>

#### a. Corporate tax/ withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Investment income (e.g. rental income, capital gains upon disposal of property and shares) is tax-exempt</li> <li>- Dividend income or any other income from distributed profits are tax-exempt under certain conditions; otherwise, corporate income tax at a rate of 15% applies</li> </ul>	Tax-exempt	Not creditable for an investment fund

#### Current income

According to the provisions of the Law on Corporate Income Tax, investment income of the REIT with a status of an investment company or investment fund (i.e., dividends, capital gains and other income from distributed profits) are treated as not taxable income, except if received from target territories.

#### Capital gains

The treatment is the same as for current income.

<sup>1</sup> If not specified, the tax treatment of the REIT for professional investors describes situations where REIT is established in a form of a joint stock company. Please note, that depending on the legal status of the REIT, tax treatment might be different.

## Withholding tax

Dividends distributed by the REIT to corporate recipients are exempt from withholding tax.

## Accounting rules

Financial statements of the REIT should be drawn up in compliance with the Lithuanian GAAP, which is very close to IFRS. However, REITs whose securities are traded on regulated markets should draw up financial statements according to IFRS. Lithuanian laws make a distinction between group and single financial statements; therefore, single statements must always be prepared, whereas those of the group only in case of mandatory consolidation.

The REIT whose securities are not traded on regulated markets has an option between Lithuanian GAAP and IFRS.

For the purposes of corporate income tax calculation, the financial result of the REIT (calculated according to IFRS or Lithuanian GAAP) would be decreased by non-taxable income, i.e., investment income, and increased by non-deductible expenses, i.e., expenses related to the non-taxable income etc.

### b. Transition regulations

#### Conversion into REIT status

N/A

### c. Registration duties

#### Registration duties

- Land registration and real estate registration fees apply
- Notary fees are 0.45% of the value of property capped at approx. EUR 5,792

Land ownership registration and real estate ownership registration fees apply. They are calculated based on the value of the property. For example, when registering a building valued at EUR 300,000, the fee is approximately EUR 150.

Notary fees are 0.45% of the value of the real estate but not less than EUR 28.96 and not more than EUR 5,792.40.



## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- No withholding tax on dividends or other distributed profits</li> <li>- No capital gain taxation</li> </ul>	<ul style="list-style-type: none"> <li>- Final withholding tax of 15% on dividends</li> <li>- Capital gains exceeding EUR 500 are subject to a 15% or 20% income tax (progressive taxation)</li> </ul>	Creditable

#### Corporate shareholder

Dividends distributed to domestic corporate shareholders are exempt from withholding tax.

Capital gains realised on the sale of the REIT's shares are generally exempt from corporate income tax.

#### Individual shareholder

Dividends distributed to domestic individual shareholders are subject to the final withholding tax at a rate of 15%.

Capital gains realised by an individual resident shareholder on the sale of the REIT shares are tax-exempt if the amount is less than EUR 500. The exceeding amount of capital gains is subject to a 15% or 20% residents' income tax (depending on the total income of the individual).

Return of capital distribution due to the redemption of shares shall be treated as capital gains from share sale and taxed accordingly. However, no exemptions apply.

#### Withholding tax

The obligation to calculate and pay the tax falls on the REIT. It is possible to credit withholding tax against the taxes payable on the same income; however, the credit should not exceed the tax due.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- No withholding tax on dividends or other distributed profits</li> <li>- No capital gain taxation</li> </ul>	<ul style="list-style-type: none"> <li>- Final withholding tax of 15% on dividends</li> <li>- Capital gains are tax-exempt</li> </ul>	Treaty benefits are available

#### Corporate shareholder

Dividends paid to foreign shareholders are generally exempt from withholding tax.

Capital gains from the sale of shares are not subject to corporate income tax in Lithuania.

Return of capital distribution is not subject to profit tax in Lithuania.

### Individual shareholder

Dividends paid to foreign shareholders are subject to a 15% withholding tax.

Capital gains from the sale of shares are not subject to the resident's income tax in Lithuania.

Return of capital distribution is not subject to the resident's income tax in Lithuania.

### Withholding tax

The obligation to calculate and pay the tax on dividends paid to corporate shareholder falls on the REIT.

A non-resident shareholder may be entitled to a withholding tax reduction under the Treaty on Avoidance of Double Taxation.

## 5 Tax Treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Non-taxable at the level of domestic shareholder	<ul style="list-style-type: none"> <li>- Dividends are subject to a 15% profit tax</li> <li>- Generally, capital gains are subject to a 15% profit tax</li> </ul>	<ul style="list-style-type: none"> <li>- Residents income tax of 15% on dividends</li> <li>- Generally, capital gains are subject to a 15% or 20% income tax</li> </ul>

### Foreign REIT

Foreign REIT is generally non-taxable at the level of domestic shareholder.

### Corporate shareholder

Dividends received by domestic corporate shareholders from foreign REIT are tax-exempt.

### Individual shareholder

Dividends received by domestic individual shareholders from foreign REITs are subject to a 15% Lithuanian residents' income tax. ■

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GLOBAL  
REIT SURVEY

EUROPE

# Luxembourg

SIF

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
SIF	2007	Law relating to specialised investment funds	<ul style="list-style-type: none"> <li>- Contractual type</li> <li>- Corporate type</li> <li>- Other type</li> </ul>
RAIF	2016	Law relating to Reserved Alternative Investment Funds	<ul style="list-style-type: none"> <li>- Contractual type</li> <li>- Corporate type</li> <li>- Another type</li> </ul>

Although Luxembourg has not yet enacted a REIT regime per se, the specialised investment fund (SIF) regime enacted on February 13, 2007 has developed into a specialised property fund regime for years.

A SIF shall be any undertaking for collective investment situated in Luxembourg (i) the exclusive object of which is the collective investment of its funds in assets in order to spread the investment risks and to ensure for the investors the benefit of the results of the management of its assets, and (ii) the securities or partnership interests of which are reserved to one or several well-informed investors, and (iii) the constitutive documents or offering documents or partnership agreement of which provide that it is subject to the provisions of the law of February 13, 2007, as amended, relating to specialised investment funds (the SIF Law).

In 2016, the Reserved Alternative Investment Fund (RAIF), a new type of investment fund was launched, as further detailed below. This new type is almost in every respect similar to a SIF, with the most important difference being that a RAIF is not directly supervised by the Luxembourg Commission de Surveillance du Secteur Financier (CSSF), but indirectly regulated via its mandatorily appointed authorized alternative investment fund manager (AIFM).

In addition, there are plans to enact a separate REIT regime comparable to those of other European countries. This new REIT regime is currently under discussions amongst the authorities and the market players

Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPS Regulation) entered into force on January 1, 2018. According to the PRIIPS Regulation, manufacturers must issue a PRIIPs Key Investor Document (KID) before retail investors may invest in the relevant PRIIP, including investment funds. In particular, SIFs and RAIFs are required to issue PRIIPS KID in accordance with the PRIIPS Regulation.

Moreover, the CSSF indicates in its FAQ that manufacturers of Luxembourg AIFs the units of which are being advised on, offered or sold to retail investors need to have in place a PRIIPs KID as of January 1, 2018, unless they benefit from the exemption expressly provided under the PRIIPS Regulation.

Luxembourg has implemented a law regarding the PRIIPS Regulation that was published on 19 April 2018 (PRIIPS Law). The PRIIPS Law provides that the CSSF and the Commissariat aux Assurances (CAA) are designated as the authorities competent for the supervision of the compliance with the PRIIPS Regulation at a national level.

In the context of Brexit, it is also worth mentioning the Luxembourg law of April 8, 2019, which provides for specific transitional measures applicable to undertakings for collective investments in transferable securities (UCITS), undertakings for collective investment regulated by part II of the UCI Law and SIFs (the 'Brexit Law'). The Brexit Law will apply in any scenario of withdrawal of the UK from EU (whether or not a no-deal Brexit).

In essence, The Brexit Law grants a 12-month remedy period to redress any breach of the investment policy or investment restrictions in a UCITS, Part-II Funds or SIF resulting from Brexit. This requirement only covers positions taken prior to the exit date of the United Kingdom. The Brexit Law provision shall be read as follows:

*“When the investment rules of a specialised investment fund are no longer respected by the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union, a maximum period of 12 months is granted to the specialised investment fund for the regularisation of non-compliance resulting from this withdrawal. This regularisation must take into account the stability of the financial markets and the interests of unitholders. This regularisation period is only granted if compared to the overruns resulting from positions taken before the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union.”*

## 2 Requirements regarding the SIF

### a. Formalities/procedure

#### Key requirements

- Authorisation and ongoing supervision by the Luxembourg supervisory authority
- Requirement for a depositary

Every SIF must be authorised by the supervisory authority of the financial sector, the CSSF. The CSSF will review and authorise the SIF's (i) constitutive documents (i.e. the Articles of Association for the corporate form of SIF, or the management regulations for the contractual SIF) and (ii) offering document and (iii) approve the various intervening parties in the SIF (e.g. depositary, central administration, portfolio managers), its risk management process and other internal procedures (conflict of interest policy, etc.). The CSSF will also look at the identity of the persons in charge of the management of the SIF (members of the board of directors, day-to-day managers, where applicable, etc.). Where the SIF qualifies as an Alternative Investment Fund (AIF) under Directive 2011/61/EC (AIFMD) transposed into Luxembourg legislation by the law of July 12, 2013 on alternative investment fund managers (AIFM Law), the CSSF will review compliance with the regulatory regime deriving from and in particular the appointment of an authorized or registered alternative investment fund manager.

Upon authorisation, each SIF is entered on the official SIF list maintained by the CSSF. Registration on this list signals that the SIF is subject to ongoing prudential supervision by the CSSF.

A SIF must entrust the custody of its assets to a depositary bank that is either (i) a credit institution having its registered office in Luxembourg, (ii) the Luxembourg branch of a credit institution having its registered office in another member state of the European Union, or (iii) for closed-ended real estate SIFs (i.e. SIFs that do not foresee redemption rights for a period of five years from the date of the initial investment), a Luxembourg entity having the status of professional depositary of assets other than financial instruments. The duties of the depositary of a SIF depend on the SIF qualifying as AIF or not:

- In respect of SIFs qualifying as AIFs, the depositary rules derive from the AIFMD (assets safekeeping, cash flow monitoring and oversight duties); and
- In respect of SIFs which do not qualify as AIFs, the depositary's duties should be understood in the sense of 'supervision', which implies that the depositary must have knowledge at any time of how the assets of the SIF have been invested and where and how these assets are available.

For property investments, the depositary will monitor the acquisition and disposition process of either the property or property rights directly in an asset transaction or of the intermediate special purpose vehicle(s) if the property is held via special purpose vehicles.

Since January 1, 2019, the depositary of a SIF (qualifying as a SIF or not) must comply with the provisions of the CSSF circular 18/697 which, in particular, provides the organisational arrangements that need to be complied by the depositary.

## b. Legal form/minimum share capital

Legal form	Minimum share capital/Net Assets*
<ul style="list-style-type: none"> <li>- Contractual form (FCP)</li> <li>- Corporate form (SICAV)</li> <li>- Other form (e.g. SICAF)</li> </ul>	EUR 1.25 million

### Legal form

A SIF may be organised under any of the following three categories:

#### i. Common Fund (*Fonds Commun de Placement* or FCP):

The contractual type fund is a co-ownership of assets with no legal personality, which is managed, on behalf of the joint owners, by a management company based in Luxembourg. An investor in an FCP receives, as a counterpart for its investment, units of the FCP, which may be issued in registered or in bearer form and which represent a portion of the net assets of the FCP. Unlike shares of a corporate type fund, units of an FCP do not offer statutory 'shareholder' rights (unless expressly provided for in the management regulations of the FCP). Unitholders are only liable up to the amount contributed by them.

#### ii. Investment Company with Variable Capital (*Société d'Investissement à Capital Variable* – SICAV):

A SIF may be incorporated in the form of a public limited company (*société anonyme-SA*), a corporate partnership limited by shares (*société en commandite par actions-SCA*), a limited partnership (*société en commandite simple-SCS*), a special limited partnership (*société en commandite spéciale-SCSp*), a private limited liability company (*société à responsabilité limitée-Sàrl*) or as a cooperative company organised as a public limited company (*société cooperative organisée sous forme de société anonyme-SCoopSA*). The SICAV acronym only refers to the variable capital concept, whereby the variations in the capitalisation of the SIF are organised without any specific formal requirements.

#### iii. SIF that are neither FCPs nor SICAVs

This third category is a residual category allowing the formation of a SIF under other legal forms or arrangements such as an association or even a fiduciary contract or any of the corporate forms mentioned under item (ii) though with fixed capital (and then referred to as a SICAF).

All of the above fund types may furthermore be organised as single funds or as umbrella (multi-compartment) funds. An umbrella fund (which merely exists through its compartments or sub-funds) is segregated into one or more compartments or sub-funds, each of which corresponds to a separate pool of assets and liabilities. Each compartment or sub-fund is linked to a specific pool of properties or property rights, which are ring-fenced from the properties or property rights in other compartments/sub-funds.

Although the umbrella fund constitutes a single legal entity (if a SICAV or SICAF) or a single contractual arrangement (if an FCP), unless otherwise provided for in the fund documentation, the assets of a compartment or sub-fund are exclusively available to satisfy the rights of investors and creditors existing in relation to that compartment or sub-fund only.

The umbrella structure and its terms must be detailed in the constitutive documents of the SIF. In addition to the umbrella structure, it is also possible to create various classes of units or shares in a SIF or within each compartment or sub-fund. Such classes of units or shares may differ, inter alia, as to their fee structure, distribution policy and type of target investors.

### Minimum capitalisation

The minimum capitalisation for a real estate SIF is EUR 1.25 million. This minimum must be reached within 12 months from the authorisation by the CSSF of the SIF and may be constituted by the subscribed capital increased by the share premium or the value of the amount constituting partnership interest. In the case of an umbrella SIF, this minimum capital requirement applies to the SIF as a whole and not to a single compartment.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
Well-informed investors	No

#### Shareholder requirements

Units, shares and other securities issued by SIFs are reserved to ‘well-informed’ investors. ‘Well-informed’ investors are institutional investors, professional investors as well as any other investor that:

- a. has declared in writing his adhesion to the status of the well-informed investor and
- b. (i) invests a minimum of EUR 125,000 in the SIF, or
  - (ii) has obtained an assessment from a credit establishment as defined in directive 2006/48/CE, from an investment firm as defined in directive 2004/39/CE, or from a management company as defined in directive 2009/65/CE, certifying his expertise, his experience and his knowledge to appraise in an appropriate manner an investment in a SIF.

#### Listing requirements

There are no mandatory listing requirements to fulfil in order to achieve SIF eligibility.

### d. Asset level/activity test

Restrictions on activities/investments
Principle of risk-spreading

A SIF may invest in any (transferable) real estate asset or right, and more particularly in (i) real estate (i.e. lands and buildings) registered in the name of the SIF, (ii) participation in real estate companies (including



loans to such companies) the exclusive object and purpose of which are the acquisition, development and sale together with the letting and tenancing of real estate, and (iii) various long-term real estate-related interests such as rights to ground rents, long-term leases and option rights over real estate investments.

By and large, a SIF may invest in any type of real estate assets and pursue any type of real estate investment strategy subject to compliance with the principle of risk-spreading. Although the SIF Law does not provide for quantitative investment restrictions, the CSSF has issued further guidance in Circular 07/309.

In general, the CSSF considers that the risk-spreading principle is complied with if a SIF does not invest more than 30% of its assets or subscription commitments into (i) a single property or (ii) the same property right or (iii) the same issuer of property rights. Property whose economic viability is linked to another property is not considered a separate item of property for this purpose.

However, the CSSF may provide exemptions from the restrictions laid out in Circular 07/309 on a case-by-case basis (e.g. the 30% rule may not apply during a start-up period). The CSSF may also request that additional restrictions are adhered to, in cases of SIFs with specific investment policies.

#### e. Leverage

Leverage
No quantitative restrictions

Though the SIF Law does not provide for quantitative borrowing restrictions, the CSSF requires clear disclosure of the contemplated borrowing ratio in the offering document. The CSSF will typically review borrowing ratios in light of market trends and may object to those ratios which are clearly outside those trends.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
No obligation	No obligation	N/A

There are no profit distribution obligations or restrictions applicable to SIFs for as long as the minimum capitalisation is complied with. The net assets may, in principle, not fall below the legal minimum of EUR 1.25 million.

#### g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Withdrawal from the official list</li> <li>- Dissolution and liquidation</li> <li>- Criminal penalties</li> </ul>

The non-compliance with the SIF Law, applicable CSSF Circulars and certain other rules or regulations, may result in the striking of the fund from the official SIF list by the CSSF, subsequently triggering a liquidation of the SIF. Criminal penalties may apply to those involved with the management or administration of a real estate SIF, although not to the fund itself.

### 3 Tax treatment at SIF level

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt	Tax-exempt	Tax-exempt

#### Current income, capital gains and withholding tax

Luxembourg specialised real estate funds are fully exempt from corporate income, municipal business and net wealth tax on the profits derived from investments, whether such profits constitute current income or capital gains. They are also exempt from withholding tax upon dividend distribution, capital reduction, interest payment, etc.

#### Other taxes

##### Annual subscription tax

Specialised real estate funds are subject to a 0.01% annual subscription tax (taxe d'abonnement), which is payable quarterly and is calculated on the aggregate net assets of the fund as valued on the last day of each quarter.

##### Examination fees

As from 1 January 2018, Specialised real estate funds are subject to an instruction tax (taxe d'instruction) amounting to EUR 4,000 due for the examination by the CSSF of the application for authorisation. In case of a SIF with multiple compartments, the instruction tax amounts to EUR 8,000 and EUR 15,000 for in-house managed SIF qualified as an alternative investment fund.

##### Capital duty

As such, no capital duty will be levied on the issuance of shares or increase in capital. That said, a fixed registration duty of EUR 75 would be applicable on transactions involving Luxembourg notaries (i.e. incorporation, amendments of by-laws and transfer of seat to Luxembourg).

##### Withholding tax

Dividend distributions made by a specialised real estate fund are not subject to dividend withholding tax.

## Real estate tax

Specialised real estate funds owning Luxembourg real property may be subject to certain real estate taxes and transfer taxes in Luxembourg.

## VAT

Based on established Luxembourg VAT administrative practice, Luxembourg regulated funds are considered as VAT-able persons carrying out VAT exempt operations without being entitled to recover input VAT incurred on expenses. They are released from the obligation to be VAT registered in Luxembourg, unless they are liable to declare and pay Luxembourg VAT on services received from foreign suppliers and owning and letting immovable property subject to Luxembourg VAT and/or performing intra-community acquisitions of goods exceeding EUR 10,000 per year (VAT excluded).

Management services provided to a Luxembourg specialised real estate fund in principle are exempt from Luxembourg VAT.

## Accounting rules

Specialised real estate funds may either apply Luxembourg generally accepted accounting standards or IFRS.

### b. Transition regulations

#### Conversion into REIF (SIF) status

Taxation of underlying assets or properties

The conversion may be a realisation event for tax purposes, and thus trigger the taxation of any underlying properties or assets provided that Luxembourg has the right to tax according to the relevant double tax treaties. Each conversion thus requires a detailed analysis of the potential tax implications.

### c. Registration duties

#### Registration duties

Luxembourg real estate transfer tax (max. 10%)

Luxembourg specialised real estate funds are subject to registration duties such as real estate transfer tax (droit de mutation à titre onéreux) on real estate acquisitions and transfers located in Luxembourg (i.e. 7%/10% depending on the municipality and the type of real property). If real property is contributed to a Luxembourg company against the issuance of shares, a reduced rate of 1.4% (for Luxembourg City) is applicable.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Corporate income tax (max. 18.19%) combined with municipal business tax (max combined rate of 24.94% for Luxembourg city in 2018)</li> <li>- Net wealth tax (0.5% and 0.05% for the net wealth tax basis exceeding EUR 500 million)</li> </ul>	Income tax (max. 42%)	N/A

### Corporate shareholder

A corporate domestic shareholder will be fully subject to tax on any income derived from a Luxembourg specialised real estate fund in the form of a SICAV or SICAF. Therefore, dividends, capital gains and return of capital received by such shareholder are fully subject to Luxembourg corporate income tax (max. 18.19%) and municipal business tax, which may lead to an aggregate tax burden of up to 24.94% (for Luxembourg-City for 2019). Income received from a Luxembourg specialised real estate fund in the form of an FCP or SCS (inclusive of SCSp), in principle, is also taxable unless the corporate shareholder could apply the participation exemption or a double taxation treaty in relation to the fund's underlying investments, if applicable.

A corporate domestic shareholder will also be subject to net wealth tax levied on its net assets. A digressive scale of net wealth tax rate applies as follows:

- 0.5 % of the unitary value up to EUR 500 million; and
- 0.05 % of the unitary value exceeding EUR 500 million.

By the way of derogation from net wealth tax rates above, minimum net wealth tax charges apply as follows:

- (a) EUR 4,815 if the sum of financial assets, receivable by affiliated companies, transferable securities and cash at bank exceeds 90 % of the total gross assets and EUR 350,000 (based on the closing balance sheet of the preceding year); and
- (b) For all other entities, the minimum net wealth tax charge should range from EUR 535 to EUR 32,100 (including the solidarity surtax) depending on the entity's total gross assets based on the closing balance sheet of the preceding year) as follows:

Total gross assets in EUR	Minimum tax in EUR
Up to 350,000	535
From 35,001 to 2,000,000	1,605
From 2,000,001 to 10,000,000	5,350
From 10,000,001 to 15,000,000	10,700
From 15,000,001 to 20,000,000	16,050
From 20,000,001 to 30,000,000	21,400
As from 30,000,001	32,100

Shares and units in a Luxembourg specialised real estate fund in the form of a SICAV or SICAF are fully subject to net wealth tax. Units in FCP or SCS (including SCSp) in the form of a specialised real estate fund are in principle also subject to net wealth tax, unless the corporate shareholders could apply the Luxembourg participation exemption or a double taxation treaty to the fund's underlying investments, if applicable.

### Individual shareholder

Income and profit received by an individual domestic shareholder from a Luxembourg specialised real estate fund will be fully subject to Luxembourg tax, and borne by the recipient (max. 42%).

Interest paid by the fund to an individual domestic shareholder managing his or her own private wealth is subject to a final 20% withholding tax at the level of the fund and is not included in the taxpayer's income tax return.

Capital gain on the disposal of shares of a Luxembourg specialised real estate fund earned by an individual domestic shareholder in the management of his or her own private wealth, is not subject to tax if the gain was realised at least six months after the acquisition of the shares, and provided that the investment in the fund does not represent a substantial (< 10%) shareholding in the fund.

## b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
No taxation	No Taxation	N/A

Income derived by foreign shareholders who have neither a permanent establishment nor a permanent representative in Luxembourg to which or to whom the shares or units of the Luxembourg fund are attributable are not subject to taxes in Luxembourg.

## 5 Tax treatment of foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Net wealth tax	Fully taxed	Fully taxed

### Corporate shareholder

A corporate domestic shareholder will be fully subject to tax on any income derived from a foreign REIT unless the foreign REIT would qualify under the Luxembourg participation exemption. Therefore, dividends, capital gains and return of capital received by such shareholder should be fully subject to Luxembourg corporate income tax (max. 18.19%) and municipal business tax, which may lead to an aggregate tax burden of up to 24.94% (for Luxembourg-City for 2019). Income received from a foreign REIT which is considered tax transparent from a Luxembourg tax perspective in principle is also taxable, but not to the extent the corporate shareholder could apply the participation exemption or a double taxation treaty in relation to the fund's underlying investments, if applicable.

For instance, it is interesting to note that upon entry into force of the new double tax treaty concluded between Luxembourg and France, dividends paid out of income derived from immovable property by certain French investment vehicles (e.g., French OPCIs) that distribute most of this income annually, and whose income and gains derived from immovable properties are exempt from taxation in France, will be taxable in Luxembourg, while up until today these were often exempt under certain conditions (25% holding threshold). In addition, France will be allowed to withhold a 15% withholding tax when the resident of Luxembourg who is the beneficial owner of the dividend holds less than 10% of the capital of said investment vehicle. When the 10% or more threshold is met, the French domestic provisions will apply (i.e., 30% in 2019, 28% in 2020, 26.5% in 2021 and 25% as from 2022 onwards). The elimination of double taxation is achieved through the credit method.

A corporate domestic shareholder will also be subject to net wealth tax levied on its net assets at the rates described above in section 4 of this survey; in principle, shares and units in a foreign REIT are fully subject to net wealth tax. Units in a foreign REIT which is considered as tax transparent from a Luxembourg tax perspective are in principle also subject to net wealth tax, but not to the extent the corporate shareholders could apply the Luxembourg participation exemption or a double taxation treaty to the fund's underlying investments if applicable.

### Individual shareholder

Income and profit received by an individual domestic shareholder from a foreign REIT should be fully subject to Luxembourg tax in the hands of the recipient (max. 42%) unless a specific exemption under a double taxation treaty exists.

## 6 The Reserved Alternative Investment Fund (RAIF)

The Luxembourg law on the reserved alternative investment funds (RAIF Law) was published on 28 July 2016.

The new RAIF regime is substantially based on the regime for Specialised Investment Funds (SIFs) previously described, and the RAIF Law has therefore been drafted by adopting many provisions from the SIF Law. The main similarities concern (i) the various legal forms (corporate and contractual) which are available, (ii) the absence of limitation as regards eligible assets or investment policies, (iii) the possibility to set up an umbrella structure with multiple compartments and share/unit classes as well as (iv) in terms of flexible subscription, redemption and distribution features. In addition, in principle, RAIFs will be subject to a 0.01% subscription tax (or a zero rate in certain circumstances). However, the main difference is that RAIFs will not be subject to either prior CSSF approval or ongoing supervision by the CSSF. Once formed, the RAIF units can immediately be marketed to the AIFMD passporting requirements.

The RAIF regime is applicable:

- to Luxembourg AIFs managed by an authorised and fully licensed AIFM (which can also be based in an EU Member State other than Luxembourg), which must be an external entity (contrary to a SIF-AIF, a RAIF cannot be managed internally);
- that invest in accordance with the principle of risk-spreading (except for exclusive SICAR-like investments);
- whose securities or partnership interests are reserved for well-informed investors; and
- whose incorporating documents (i.e. articles of association, management regulations or partnership agreement) expressly provide that they are subject to the provisions of the RAIF Law (therefore the RAIF regime is optional).

Being managed by an authorised and fully licensed EU-based AIFM, the RAIF will also benefit from all EU AIFMs' passporting advantages through a regulator-to-regulator notification regime. Consequently, the RAIF's units/shares and interests will be distributed by way of the marketing passport across Europe to professional investors only. Subject to an opinion and positive advice from the European Securities and Markets Authority (ESMA), the EU Commission may decide to extend the passport to non-EU AIFMs, which may then, subject to compliance with the AIFMD requirements, also manage RAIFs and benefit from the passport. A Luxembourg approved statutory auditor (Réviseur d'entreprises agréé) must audit the RAIF's annual accounts.

It should be noted that several investment regimes available in Luxembourg can be combined in order to comply with differing investor needs. In a first stage, a RAIF could be set up in a limited amount of time without prior CSSF approval in order to quickly organise a first closing for investors that do not compulsorily need a directly supervised structure. At a later stage, the RAIF could be converted into a SIF with prior CSSF approval in order to attract further investors who wish or are required to invest in a directly supervised investment vehicle. ■

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GLOBAL  
REIT SURVEY

EUROPE

# Netherlands

FBI

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
FBI	1969	FBI (art. 28 CITA)	In principle corporate type (only for corporate taxpayers)

The Netherlands introduced the Fiscal Investment Institution regime (fiscale beleggingsinstelling: FBI) in 1969. An FBI is in principle subject to Dutch Corporate Income Tax, albeit at a rate of zero per cent (0%) (a de facto full exemption). The FBI regime has been incorporated in the Dutch Corporate Income Tax Act 1969 (Wet op de vennootschapsbelasting 1969: CITA) and should be considered a tax facility. It may also apply to passive, portfolio investments other than real estate.

The FBI regime was amended to comply with EU law regulations in 2007. From that moment on, it has become possible for a foreign entity to apply for the regime. Further, certain restrictions which prohibited foreign shareholders from investing in an FBI have been abolished.

In October of 2017, the incoming Dutch government announced its intention to abolish the Dutch FBI regime for direct investments in real estate as of 2020 as an accompanying measure to the abolition of the Dutch dividend withholding tax. However, as a result of extreme scrutiny by the industry and by opposition parties, the Dutch government ultimately decided not to abolish the dividend tax and consequently to maintain the FBI regime for direct investments in real estate.

In response to questions raised in Parliament, the Dutch Ministry of Finance is currently investigating whether a targeted amendment of the FBI regime is required in order to prevent undesired situations in which the Netherlands cannot (fully) exercise its taxing rights with regards to income derived from Dutch real estate held via FBIs. The outcomes of the research are expected to be published on or around Budget Day (Prinsjesdag) 2019.

## Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
The Netherlands	5	5	EUR 21,514	1.83%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
WFD Unibail-Rodamco**	EUR 18,223	-27.57%	8.20%	1.55%
EuroCommercial Ppty	EUR 1,168	-30.84%	9.15%	0.10%
Wereldhave	EUR 928	-25.15%	10.94%	0.08%
NSI	EUR 692	10.21%	5.80%	0.06%
Vastned Retail	EUR 508	-25.45%	7.22%	0.04%

\* All market caps and returns are rebased in EUR and are correct as at 29 July 2016. The Global REIT Index is the FTSE EPRA/NAREIT Global REITs Index. EPRA, August 2016.

\*\* Main listings done on Euronext Amsterdam. For Index purposes, classified as a Dutch company.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Application in the corporate income tax return

In the Netherlands, an eligible investment company may elect to apply for the FBI regime by making the appropriate election in its corporate income tax return, which is filed after the end of the relevant tax year.

The FBI regime is a corporate income tax regime, and its application is not contingent on the satisfaction of regulatory requirements for purposes of for instance the Financial Supervision Act (Wet op het financieel toezicht: FSA). However, less restrictive shareholder requirements apply if the FBI is under supervision of the Netherlands Authority for the Financial Markets (see 2.3 below).

### b. Legal form/minimum share capital

Legal form	Minimum share capital
<ul style="list-style-type: none"> <li>- Dutch private limited liability company (BV)</li> <li>- Dutch public limited liability company (NV)</li> <li>- Open-ended mutual investment fund (FGR)</li> <li>- Comparable foreign legal entity</li> </ul>	<ul style="list-style-type: none"> <li>- BV: None</li> <li>- NV: EUR 45,000</li> <li>- FGR: none</li> </ul>

#### Legal form

A Dutch public liability company (NV), a private limited liability company (BV), an open-ended mutual investment fund (fonds voor gemene rekening: FGR) or comparable foreign legal entities are eligible for the FBI regime. Comparable foreign legal entities are not required to have Dutch residency, but they should be liable to Dutch corporate income tax.

If an FBI takes the legal form of an FGR – an entity which in itself does not have legal personality – it is required to have a management company. An FBI can only be self-managed if it is in the form of a company, although a management company could also be used in that situation.

#### Minimum share capital

The FBI regime does not impose any requirements as to minimum share capital. However, minimum capital requirements do follow from Dutch company law and are as follows for the various Dutch entities:

- BV: None
- NV: EUR 45,000
- FGR: None

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<p>If listed or regulatory licensed:</p> <ul style="list-style-type: none"> <li>- One single corporate entity may stand-alone – or together with affiliates – not hold 45% or more of the shares</li> <li>- One single individual may not hold 25% or more of the shares</li> </ul> <p>If not listed or licensed:</p> <ul style="list-style-type: none"> <li>- The shares in the FBI must for at least 75% being owned by individuals/non-taxable corporate entities/regulated FBIs</li> <li>- One single individual may not hold 5% or more of the shares</li> </ul> <p>Further, in both cases:</p> <p>Dutch corporate entities may not own 25% or more of the shares in the FBI through the interposition of foreign entities</p>	None

#### Shareholder requirements

The FBI shareholder requirements are more lenient if either the FBI is listed on any recognised stock exchange, it (or its manager) has a licence pursuant to the FSA or it (or its manager) benefits from an exemption of a license requirement as a result of being subject to regulatory supervision by another EU member state (hereinafter referred to as a ‘regulated FBI’). If the FBI does not meet any of these requirements (hereinafter referred to as a ‘non-regulated FBI’) more stringent shareholder requirements must be met.

In case of a non-regulated FBI, the shareholder requirements are as follows:

- a single corporate entity (a regulated FBI excluded) which is subject to any form of profit tax or an entity whose profits are taxed in the hands of its participants (i.e. a transparent entity) may not own 45% or more of the shares together with affiliated entities; and
- a single individual may not own 25% or more of the shares.

In case of a non-regulated FBI, the shareholder requirements are as follows:

- at least 75% of the shares must be held by any combination of: (i) individuals; (ii) corporate entities which are not subject to any form of profit tax or which are exempt therefrom and whose profit is not taxed in the hands of the beneficial owner of those profits; and (iii) directly or indirectly by regulated FBIs; and
- a single individual may not own 5% or more of the shares.

Irrespective of whether the FBI is regulated or not, all FBIs must meet the condition that their shares are not owned for 25% or more by Dutch resident entities through the interposition of non-Dutch entities which have a capital divided into shares or of non-Dutch mutual funds.

However, it is approved by the Dutch Ministry of Finance that non-regulated FBIs, having a non-regulated FBI as a shareholder who owns more than 25% of the shares, will meet the shareholder requirements, provided the non-regulated FBI distributes 95% of the available profits before closing its financial year. Therefore, multi-layer FBI structures are possible to a certain extent.

#### Listing requirements

Listing is not required, but it does offer access to less restrictive shareholders requirements.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- FBIs are only permitted to invest in passive, portfolio investments
- FBIs are allowed to invest abroad

The statutory purpose and the actual activities of an FBI must be exclusively restricted to portfolio investing. As such, the FBI is in principle prohibited to be engaged in activities which go beyond that scope. This means that investments must have the objective of realising a return in terms of yield derived from investment and appreciation in value which one may reasonably expect from regular investment management (i.e. investments in shares, bonds and real estate).

An FBI investing in real estate must restrict its activities to the ‘passive’ renting out of and investing in real estate. The permitted activities of an FBI itself include: (i) the granting of guarantees for the benefit of affiliated companies whose assets comprise at least 90% of real estate (and associated rights); and (ii) financing such companies with external loans.

Furthermore, real estate development is, in principle, not regarded as a ‘passive’ investment activity. However, development activities on behalf of the FBI’s own investment portfolio itself are specifically permitted. These activities should be carried out by a subsidiary which is subject to tax at the standard statutory corporate income tax rate (the taxable amount up to EUR 200,000 will be subject to a rate of 19%; in excess thereof, the rate is 25%)<sup>1</sup>. This ‘development subsidiary’ is not allowed to carry out any other activity than development activities for the FBI’s portfolio of properties and it should charge the FBI an at arm’s length (development) fee. For practical purposes, the law provides for a safe harbour rule to avoid discussions about the nature of relatively small investment activities: improving and expanding existing real estate objects will not be considered ‘development activities’ as long as the investments involved do not exceed 30% of the relevant property’s market value determined under the Value of Immovable Property Act (Wet waardering onroerende zaken: ‘WOZ’).

In addition, ancillary business activities are permitted if they are related to the FBI’s portfolio of properties. These activities should also be carried out via a regularly taxable subsidiary (standard corporate tax rates of 19/25% (in 2019)). This subsidiary should charge the FBI an at arm’s length (service) fee. The allowed ancillary business services may not exceed certain statutory qualitative and quantitative limits.

An FBI is allowed to invest in foreign assets. It would, however, still be subject to the same restrictions. It may hold shares and/or interests in subsidiary corporations and/or in partnerships.

#### e. Leverage

##### Leverage

- 60% of the tax book value of directly/indirectly held real estate
- 20% of the tax book value of all other investments

The debt of the FBI may not exceed:

- 60% of the tax book value of directly/indirectly held real estate; or
- 20% of the tax book value of all other investments.

<sup>1</sup> The government intends to further reduce the statutory corporate income tax rate to 16.5% and 22.55% respectively in 2020 and 15% and 20.5% respectively as of 2021.

Debt is defined as the total amount borrowed by the FBI, which is, in principle, calculated on a non-consolidated basis.

The 60% leverage ratio for investments in real estate also applies to equity investments through shares in affiliated companies whose assets comprise at least 90% of real estate (and associated rights). Further, intra-group loans to such real estate subsidiaries of an FBI may be externally funded up to 100%. Therefore, intra-group loans to real estate subsidiaries effectively fall outside the FBI's leverage restriction. Consequently, an FBI will be able to attract external financing in order to provide back-to-back financing to real estate group subsidiaries without deteriorating its leverage limitations.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
100% of taxable profit	Capital gains/losses can be allocated to a tax-free reserve	Within eight months after the end of its financial year

#### Current income

Dutch tax law requires that an FBI distributes all (100%) of its profits to its shareholders within eight months after the end of its financial year. The amount of taxable profit is calculated on the basis of the regular rules applicable to corporate income taxpayers, with some exceptions especially provided for FBIs. In accordance with the regular rules, depreciation on passively held real estate is limited<sup>2</sup>.

#### Capital gains

The net balance of unrealised capital gains on securities and realised capital gains on all other investments may be added to a so-called reinvestment reserve (herbeleggings-reserve). These capital gains are excluded from the taxable profit of the FBI and are not subject to the profit distribution obligation (see 3.1 below).

#### g. Sanctions

Sanction
Cancellation of FBI status

If at any point in time an FBI fails to meet any of the requirements to qualify as an FBI, the FBI status will be cancelled as from the start of the financial year during which such failure occurred, except for a failure of the profit distribution obligation which will cancel the FBI status as from the start of the accounting year of which the profits should have been distributed under this requirement.

The main consequence of a loss of the FBI status is that the relevant entity will become a regular taxpayer for Dutch corporate income tax purposes so that its profits, determined in accordance with the regular Dutch tax accounting principles, will be subject to Dutch corporate income tax at the standard rates (19/25% in 2019). Prior to the day on which the FBI becomes (or returns to be) a regular taxpayer for Dutch corporate income tax purposes, i.e. at the end of the preceding accounting year, its assets are revalued to fair market value. Consequently, any capital gain realised as a result of this revaluation is still subject to the FBI-regime (i.e. taxed at 0%).

<sup>2</sup> As of 2019, depreciation of real estate in own use is, similarly to let out real estate, limited to 100% of the WOZ-value (previously 50%).

### 3 Tax treatment at the REIT level

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Real estate income is part of the taxable profit and is subject to a corporate income tax rate of 0% (effective exemption)	Capital gains/losses can be allocated to a tax-free reserve and are thus effectively exempt from corporate income tax	Withholding taxes incurred are not refunded; FBIs are granted a Dutch dividend tax remittance rebate instead

#### Current income

An FBI is subject to corporate income tax in the Netherlands at a rate of 0%. The taxable profits of an FBI are in principle determined on the basis of the same tax accounting principles which apply to taxpayers regularly subject to Dutch corporate income tax. The taxable profits typically include the direct investment result and, if the reinvestment reserve is not applied, the net balance of capital gains and losses. However, some exceptions on the determination of the taxable profit apply to an FBI. Without being exhaustive, the main exceptions are:

- the participation exemption does not apply to investments in entities made by an FBI;
- subject to conditions and limitations, an FBI can elect to apply a rounding-off reserve (afroundingsreserve);
- subject to conditions and limitations, an FBI can elect to apply a reinvestment reserve (see 2.6 above);
- certain particular items which are not deductible for regular corporate income taxpayers are taken into account in calculating the taxable profit of an FBI (e.g. the earnings stripping interest deduction limitation); and
- income that would be included in the tax base of regular corporate income taxpayers under the controlled foreign company (CFC) rules.

#### Capital gains

The FBI can elect to apply a reinvestment reserve. By doing so, the balance of capital gains and losses is excluded from the taxable income and allocated to the reinvestment reserve. The remainder of taxable income represents the annual distribution obligation (see 2.6 above).

#### Withholding tax

Given that an FBI is liable to Dutch corporate income tax at a rate of 0%, the FBI is effectively unable to credit Dutch or foreign withholding taxes suffered against its Dutch corporate income tax liability. Moreover, unlike taxpayers who are regularly subject to Dutch personal income tax or corporate income tax, the FBI is not entitled to a refund of Dutch dividend withholding tax upon request.

However, subject to certain conditions and limitations, the FBI is allowed to apply a rebate to its obligation to remit the amount of Dutch dividend withholding tax which the FBI has to withhold in respect of its recurrent compulsory distribution of profits, in an amount equal to the amount of withholding taxes suffered by the FBI (afdrachtvermindering). As such, the FBI can impute the domestic and foreign withholding tax it suffered on the obligation to pay Dutch dividend withholding tax which it withholds from distributions it makes to its shareholders.

With respect to such a rebate in respect of foreign withholding taxes suffered (on interest and dividend only), certain limitations apply. Such limitations are:

- a maximum underlying tax rate of 15% may be taken into account with respect to foreign source tax on dividends and interests; and
- the rebate is further reduced if and to the extent the FBI has shareholders who are entitled to a reduction or rebate of Dutch dividend withholding tax under a prevailing arrangement for the avoidance of double taxation or by virtue of the Dutch Dividend Withholding Tax Act.

## Accounting rules

There are no special commercial accounting rules for FBIs. A listed FBI is required to follow IFRS rules, just like any other listed company.

### b. Transitional regulations

#### Conversion into REIT status

- All assets and liabilities are assessed at market value
- Tax recognised reserves must be realised and should be added to the taxable profits
- Hidden capital gains and losses must be recognised and are subject to corporate income tax at regular rates

At the end of the year immediately prior to the year as of which the entity converts to an FBI, all its assets and liabilities must be revalued to market value. Hidden capital gains are therefore realised and subject to Dutch corporate income tax in accordance with the regular rules. Tax-free reserves must also be realised and added to the taxable profits. The final tax charge prior to conversion is levied at the regular Dutch corporate income tax rates (19/25% in 2019), i.e. a special conversion regime is not available.

A loss of FBI status also leads to a revaluation to a fair market value of the assets (see 2.7 above).

### c. Registration duties

#### Registration duties

- No capital duties
- A real estate transfer tax of 6% applies if the FBI acquires Dutch real estate or shares of Dutch real estate companies (a 2% rate applies to residential real estate)

A 6% real estate transfer tax (overdrachtsbelasting) applies if the FBI acquires Dutch real estate (a 2% rate applies to residential real estate). In addition, an acquisition leading to an interest of at least one third in a real estate company is subject to real estate transfer tax as well. Real estate transfer tax is levied from the acquirer of Dutch real estate (or the shares of the Dutch real estate company).



## 4 Tax treatment at shareholder level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Dividends and capital gains are taxable	The taxpayer is typically taxed on the basis of a deemed income	<ul style="list-style-type: none"> <li>- In principle, a withholding tax of 15%</li> <li>- Creditable</li> </ul>

#### Corporate shareholder

A Dutch corporate investor's investment in shares of an FBI in principle disqualifies for the Dutch participation exemption regime. Therefore, any benefits derived from this shareholding in terms of dividends and capital gains will be included in the taxable profits subject to corporate income tax at the standard rates (19/25% in 2019).

In principle, Dutch corporate investors can credit the Dutch dividend withholding tax which they have suffered on dividends distributed by the FBI against their Dutch corporate income tax liability (full credit). Any excess of dividend withholding tax is refundable. Application of the dividend tax remittance rebate (afdrachtvermindering) by the FBI does not affect the entitlement to a credit for such Dutch shareholder.

#### Individual shareholder

The income tax consequences of a Dutch individual shareholder depend on the qualification of the FBI participation for the investor. In most cases, income from the investment will be taxed annually as a 'benefit from savings and investments' (voordeel uit sparen en beleggen). The benefit is calculated as a deemed return on the fair market value of a taxpayer's net assets ('yield basis' or rendementsgrondslag) at the beginning of the year in excess of the 'exempt net asset amount' (heffingvrije vermogen) of EUR 30,360 (2019). The benefit is deemed to be 1.935% per annum of the yield basis up to EUR 71,650. For a yield basis from EUR 71,650 up to EUR 989,736, the deemed benefit will be 4.451% of the yield basis and, finally, the yield basis exceeding EUR 989,736 will be deemed to realise a benefit of 5.60%. These benefits are taxed at a rate of 30%. The fair market value of the investment in the FBI forms part of the total yield basis of an individual taxpayer. Actual benefits derived from the participation in the FBI, including any gains realised on the disposal of the shares therein, are not as such subject to Dutch income tax.

If an individual owns, alone or together with certain family members, an interest of 5% or more in an FBI (only possible if the FBI is regulated), the dividend distributions and capital gains are subject to the so-called 'substantial interest' taxation rules (aanmerkelijk belang). Basically, all results from a substantial interest (dividends and capital gains included) are taxed at a flat rate of 25% (26.25% in 2020 and 26.90% as of 2021), if and when received.

If an individual owns FBI shares in the course of his enterprise, the results from the interest could be subject to tax at progressive income tax rates (up to 51.95%).

Individual shareholders are allowed to credit the Dutch dividend withholding tax which they have suffered on dividends distributed by the FBI against their personal income tax liability in the Netherlands (full credit). Application of the dividend tax remittance rebate (afdrachtvermindering) by the FBI does not affect the entitlement to a credit for such Dutch shareholder.

## Withholding tax

Distributions of profits in whatever name or form made by an FBI are subject to 15% Dutch dividend withholding tax. Distributions made from the reinvestment reserve (herbeleggingsreserve) are considered capital repayments for withholding tax purposes and therefore are not subject to Dutch dividend withholding tax (if certain formalities are complied with). The repayment of nominal share capital is generally not subject to Dutch dividend withholding tax. However, the redemption of share premium is only free from Dutch dividend withholding tax if the FBI does not have any net profit (zuivere winst), such as available profit reserves or hidden reserves.

As stated above, Dutch taxable corporate and individual shareholders are allowed to credit the Dutch dividend withholding tax against their corporate income tax or personal income tax liability in the Netherlands.

A Dutch entity which is not subject to Dutch corporate income tax (e.g. pension funds), can claim a refund of Dutch dividend withholding tax suffered on distributions by an FBI.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Generally speaking, should not be subject to corporate income tax	Generally speaking, should not be subject to personal income tax	<ul style="list-style-type: none"> <li>- In principle, a withholding tax of 15%</li> <li>- Tax treaty relief might apply</li> <li>- Parent-Subsidiary Directive does not apply</li> </ul>

### Corporate shareholder

Generally speaking, foreign corporate investors should not be subject to Dutch corporate income tax with respect to their investment in an FBI. However, a foreign corporate investor which owns a so-called ‘substantial interest’ in a Dutch FBI (generally speaking 5% or more of the FBI’s aggregated nominal share capital) may be liable to Dutch corporate income tax on the dividends received and capital gains realised in respect of this substantial interest (standard rates of 19/25%). Conventions for the avoidance of double taxation concluded by the Netherlands, may limit the Netherlands in fully exercising those taxing rights.

### Individual shareholder

Generally speaking, foreign individual investors should not be liable to Dutch personal income tax with respect to their investment in an FBI. However, a foreign individual investor who owns a so-called ‘substantial interest’ in a Dutch (regulated) FBI (generally speaking 5% or more of the FBI’s aggregated nominal share capital) may be liable to Dutch personal income tax at a flat rate of 25% (26.25% in 2020 and 26.90% as of 2021) on the dividends received and capital gains made in respect of this substantial interest. Conventions for the avoidance of double taxation concluded by the Netherlands, may limit the Netherlands in fully exercising those taxing rights.

## Withholding tax

Distributions of profits in whatever name or form made by an FBI are subject to 15% Dutch dividend withholding tax.

Distributions made from the reinvestment reserve (herbeleggingsreserve) are considered capital repayments for withholding tax purposes and therefore are not subject to Dutch dividend tax (if certain

formalities are complied with). The repayment of nominal share capital is generally not subject to Dutch dividend withholding tax. However, the redemption of share premium is only free from Dutch dividend withholding tax if the FBI does not have any net profit (zuivere winst), such as available profit reserves or hidden reserves.

A corporate shareholder that is neither subject to corporate income tax in its country of residence nor would be subject to Dutch corporate income tax if the entity were established in the Netherlands can file a request to the Dutch tax authorities for a refund of Dutch dividend withholding tax. For non-EU/EEA investors, it is required that their investment falls within the scope of the EU free movement of capital.

Furthermore, a partial reclaim of Dutch dividend withholding tax is possible under certain conditions following the European Court of Justice case law which has meanwhile been incorporated into Dutch tax law. Such may be the case if the foreign shareholder is confronted with a levy (i.e. the withheld dividend tax, potentially up to 15%) which is more burdensome (i.e. higher) than the tax treatment of that shareholder would have been if it had been a Dutch resident. For the treatment of Dutch domestic shareholders, reference is made to 4.1 above.

## 5 Tax treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
A foreign REIT should be tax-exempt	No specific tax privileges	No specific tax privileges

### Foreign REIT

A foreign entity which is comparable in nature, form and behaviour to the qualifying Dutch FBI and that complies with all the FBI requirements (shareholder, leverage, distribution obligation, etc.) can obtain FBI status in respect of its qualifying Dutch sources of income (Dutch real estate, etc.). In that case, qualifying FBI income derived from Dutch taxable sources will be subject to a corporate income tax rate of 0%.

It is the view of the Dutch tax authorities that foreign REITs that are not subject to Dutch dividend withholding tax are not comparable to a qualifying Dutch FBI. However, in a recent judgment by a Dutch District Court, a foreign REIT was found to be comparable to such an FBI, provided all qualification conditions are satisfied. The case is expected to be challenged before the Court of Appeal and the Supreme Court.

### Corporate shareholder

The participation exemption in principle does not apply to participation in a Dutch resident or foreign resident company which qualifies as an FBI. Hence, a Dutch corporate shareholder owning participation in a foreign entity which qualifies as an FBI cannot apply for the participation exemption in respect of income and capital gains derived from the participation in the FBI.

The participation of a Dutch corporate taxpayer in a foreign REIT is, in principle, eligible for the participation exemption, provided certain conditions are met. However, under anti-hybrid rules, the Dutch tax authorities take the position that the participation exemption does not apply to received dividends if the foreign REIT applied a mechanism of deductible dividends.

## Individual shareholder

There is no specific tax privilege. General rules apply (see 4.1 above). ■

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major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
SIGI	2019	Decree-Law no. 19/2019, of January 28 (Note: As amended by decree approved in Parliament on July 19, 2019, which should come into force as law upon signing by the President of the Republic and publication in the Official Journal)	Corporate type

Following international trends, Decree-Law no. 19/2019, of 28 of January (which entered into force on the 1st of February 2019) introduced a model of REIT into the Portuguese legal framework, by creating the so-called Real Estate Investment and Asset Management Companies (Sociedades de Investimento e Gestão Imobiliária) or ‘SIGI’.

Upon subsequent parliamentary review, the legislation originally enacted by the Portuguese Government has been confirmed by the Parliament by majority vote taken on 19 July 2019, however with certain amendments that are currently pending the final decision of the President of the Republic. Should the parliamentary decree be signed by the Head of State, such amendments will become law and shall come into force upon publication in the Official Journal, which is expected to occur in July or August 2019. This survey already takes into account and reflects the amendments approved by the Parliament.

SIGIs are vehicles designed for real estate investment, with the particularity that the shares representing their share capital must be listed and subject to specific free-floating requirements. SIGIs also need to comply with strict requirements as regards the composition of portfolios, limits on indebtedness and mandatory distribution of profits. From a tax perspective, SIGIs benefit from the express reference to the favourable tax regime currently applicable to real estate investment funds/companies, although they are not subject to the legal framework applicable to collective investment vehicles nor to the supervision of the Portuguese Securities Market Commission (CMVM).

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Within one year after incorporation (or the effects of the conversion of already existing companies), SIGIs' shares must be admitted to trading in a regulated market or in a multilateral trading facility in Portugal or in the EU/EEA

SIGIs must be listed in a regulated market in Portugal or in other members of the European Union (or within the European Economic Area). Listing in alternative multilateral trading facilities also qualifies for the purposes of the application to a company of the legal framework of SIGIs. The listing process shall be completed within one year after the incorporation of the company, or the effects of the conversion in the case of already existing companies.

In Portugal, there is a single regulated market which is Euronext Lisbon, managed by Euronext. Euronext Access and Euronext Growth are two alternative multilateral trading facilities also managed by Euronext that are also eligible for trading shares representing the share capital of a SIGI.



In addition to newly incorporated SIGIs, which can be set up through private or public placement, the conversion into SIGIs of existing private limited liability companies by shares is also permitted and regulated, as well as the conversion of real estate collective investment vehicles provided that these take corporate form already. It should be noted that for the purposes of incorporating a SIGI by way of a demerger from an existing company, the branch of activity comprising one or more real estate assets or holdings is considered from a legal perspective as an economic unit.

Limited liability companies by shares may be converted into SIGIs subsequently to a resolution of its shareholders' meeting taken by the qualified majority applicable to the amendment of the by-laws and provided that all legal requirements applicable to SIGIs are met. In these cases, the conversion into SIGI is effective as from the first day of the financial year immediately after the registration of the amendments to the by-laws of the company.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Limited liability company by shares ( <i>Sociedade Anónima</i> )	EUR 5 million

SIGIs must take the form of private limited liability companies by shares (*sociedades anónimas*) with a minimum share capital of EUR 5 million represented by ordinary and nominative shares, having head offices in Portugal.

Besides, it is compulsory that their corporate name includes the name or acronym by which they are known in Portugal; i.e. '*Sociedade de Investimento e Gestão Imobiliária, S.A.*' or '*SIGI, S.A.*'.

The SIGI's main corporate purpose must consist of:

- i. the acquisition of freehold rights, surface rights or other rights over property of similar nature, to be allocated to leasing or other atypical contractual models that include the provision of services required for the utilisation of property, including leases under the form of agreements for the use of units or spaces in shopping centers or offices which are very common in Portugal. Among others, SIGIs can also invest in development and urban regeneration projects, as well as on land that will qualify as urban land for construction purposes within three years from the acquisition;
- ii. the holding of participations in other SIGIs, or in companies with registered offices in Portugal or in another Member State of the European Union or European Economic Area subject to the exchange of tax information equivalent to the standards applicable within the EU (in this case, provided that such resident or non-resident companies meet the requirements applicable to SIGIs as regards corporate purpose, composition of portfolio and profits distribution); and
- iii. the holding of stakes in Portuguese real estate collective investment vehicles regulated under the Portuguese Collective Investment Schemes 16/2015 Act or residential letting real estate investment funds that have a similar income distribution policy.

Both real estate assets and participations must be held by the SIGI for a minimum period of three years.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- Until the end of the 3rd complete calendar year upon admission to trading, at least 20% of the shares representing a SIGI's share capital must be spread across investors with holdings corresponding to less than 2% of voting rights</li> <li>- Until the end of the 5th complete calendar year upon admission to trading, at least 25% of the shares representing a SIGI's share capital must be spread across investors with holdings corresponding to less than 2% of voting rights</li> <li>- Certain limitations apply to banks</li> </ul>	Yes

#### Shareholder requirements

Until the end of the third complete calendar year upon admission to trading, at least 20% of the shares representing a SIGI's share capital must be spread across investors with holdings corresponding to less than 2% of voting rights. This minimum free float requirement is increased to 25% by the end of the fifth complete calendar year upon admission to trading.

Credit institutions such as banks are only allowed to hold participations above 25% in SIGIs for a maximum period of three or five years (consecutive or cumulative).

Additional free float requirements may apply depending on the specific rules of the stock exchange on which the shares are admitted to trading (see below).

There are no restrictions on foreign shareholders under SIGI's regime.

#### Listing requirements

Within one year after incorporation or effects of conversion, SIGI's shares must be listed in Portugal, in the EU or in the European Economic Area in (i) an official regulated market (e.g. Euronext Lisbon) or (ii) a multilateral trading facility (e.g. Euronext Access Lisbon or Euronext Growth Lisbon). In the case of admission to trading in multilateral trading facilities such as Euronext Access Lisbon or Euronext Access Growth, the rules applicable by virtue of the admission to trading of the shares are simplified.

SIGI's regime sets out specific free float requirements for SIGI's shares (see section Shareholder requirements), although additional free float requirements may apply depending on the specific rules of the stock exchange on which the shares are admitted to trading. As a general rule, the minimum free float for listing in Euronext Lisbon (regulated market) is 25%. In the case of listing in Euronext Growth Lisbon, SIGI's shares having a value of, at least, EUR 2.5 million shall be spread across the public. No free float requirements apply for listing in the standard segment of Euronext Access.

Only in specific cases will SIGIs have 'public company status' (i.e. being subject to the supervision of the Portuguese Securities Market Commission and to a wide and stricter set of obligations, notably information obligations), in particular in the case of incorporation through public placement or in the case that its shares have been, inter alia, subject of public offering or admitted to trading in a regulated market, which is not the regime generally applicable.



#### d. Asset level/activity test

##### Restrictions on activities/investments

- The composition of the portfolio of the SIGI must comply with 2 cumulative limits, starting from the 2nd year upon incorporation (or conversion into SIGI): (a) at least 80% of the total value of SIGI's assets must correspond to rights over real estate assets (free of liens or encumbrances) and holdings, (b) at least 75% of the total value of SIGI's assets must correspond to rights over real estate assets (free of liens or encumbrances) subject to lease or other atypical contractual models that include the provision of services required for the utilisation of the properties
- Both real estate assets and participations must be held by the SIGI for a minimum period of 3 years; otherwise the company loses its status as a SIGI

##### Asset level/activity test

The composition of the portfolio of a SIGI must comply with two cumulative limits, starting from the second year upon incorporation (or conversion into a SIGI):

- i. the value of rights over real estate assets (free of liens or encumbrances) and holdings (comprised in SIGI's main corporate purpose, as per the limitations set out above) shall represent at least 80% of the total value of the assets of the SIGI; and
- ii. the value of rights over real estate assets (free of liens or encumbrances) subject to lease or other atypical contractual models that include the provision of services required for the utilisation of the properties shall represent at least 75% of the total value of the assets of the SIGI.

These limits are assessed in accordance with the individual accounts or, in the case that the SIGI has subsidiaries, in the consolidated accounts.

Guarantees obtained in the framework of financing for the acquisition, construction or rehabilitation do not affect the value of the real estate.

There is no asset diversification rule, and SIGIs are entitled to hold a single property asset.

SIGIs may invest not only in urban property but also in rural land that is capable of autonomous economic exploitation, including for forestry industry.

Real estate assets and holdings must be subject to valuation every 7 years at least, by an independent external appraiser registered with the CMVM.

##### Minimum holding period

Both real estate assets and holdings (comprised in SIGI's main corporate object, as per the limitations set out above) must be held by the SIGI for a minimum period of three years; otherwise the company loses its status as a SIGI.

#### e. Leverage

##### Leverage

SIGI's indebtedness shall not exceed, at any time, 60% of the SIGI's total assets

SIGI's indebtedness shall not exceed, at any time, 60% of the SIGI's total assets. This limit is assessed in accordance with the individual accounts or, in the case that the SIGI has subsidiaries, in the consolidated accounts.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
<ul style="list-style-type: none"> <li>- 90% of the profits of the financial year that result from dividends on shares or income from participation units</li> <li>- 75% of the remaining distributable profits of the financial year</li> </ul>	<ul style="list-style-type: none"> <li>- No requirement</li> <li>- However, 75% of the net proceeds deriving from the sale of assets allocated to the core corporate purpose shall be reinvested within 3 years in other assets to be allocated to the development of such corporate purpose</li> </ul>	<p>Within nine months after the end of the financial year</p>

SIGIs are obliged to distribute their profits to shareholders in the form of dividends as set out below. It should also be noted that the legal reserve of SIGIs shall not exceed 20% of their share capital.

#### Operating income

It is compulsory to distribute at least 90% of the profits of the financial year that result from dividends on shares or income from participation units.

#### Other profits

No requirement. However, at least 75% of the net proceeds deriving from the sale of assets allocated to the core corporate purpose shall be reinvested within three years in other assets to be allocated to the development of such corporate purpose.

#### Timing

Within nine months after the end of each financial year.

#### g. Sanctions

Sanction
<ul style="list-style-type: none"> <li>- Loss of SIGI status</li> <li>- No specific monetary penalties are foreseen</li> </ul>

Companies lose their SIGI status upon the occurrence of any of the following events:

- ceasing to be private limited liability companies by shares, changing their corporate purpose or reducing their share capital below EUR 5,000,000;
- not requiring the admission to trading of their shares within one year after incorporation or effects of conversion;

- iii. not complying for more than six months with (a) free-float requirements of 20% following the end of the third complete calendar year upon listing (or 25% following the 5th complete calendar year upon listing); or (b) 2% minimum voting rights;
- iv. not complying with the requirement of holding the real estate assets and holdings (comprised in SIGI's main corporate object, as per the limitations set out above) for a minimum period of three years;
- v. simultaneously not complying with the portfolio composition and minimum holding period requirements for more than six months;
- vi. not complying with either the requirement on portfolio composition or the minimum holding period requirement for two consecutive years; or
- vii. failing to meet indebtedness limits.

The loss of SIGI status prevents the company from reacquiring such status in the following three years.

The management and supervisory board members are accountable before the shareholders for direct damages caused as a result of the loss of SIGI status.

### 3 Tax treatment at the REIT level

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Income derived from rental/lease activity is tax-exempt</li> <li>- Other income may subject to corporate taxation</li> </ul>	Capital gains deriving from the disposal of rented real estate properties and of participations are exempt	Proceeds from lease activity are not subject to withholding tax

#### Corporate taxes

From a tax perspective, the SIGIs benefit from an express reference to the tax regime already in force for real estate investment funds/companies (collective investment vehicles or CIVs), meaning that there is no specific and separate tax regime for the SIGIs.

As a general rule, a SIGI is therefore liable to Corporate Income Tax (CIT) at the rate of 21% but not subject to Municipal and State Surtaxes.

At the level of the SIGI, the regime set out for real estate investment funds/companies is characterised, in summary, by a corporate income tax exemption on income received by the SIGI considered as passive, with other income being liable to tax at general CIT rules.

Income qualified under the following three categories, as defined by the Personal Income Tax Code, is excluded from taxation at the level of the SIGI:

- Investment income (e.g., dividends and interest);
- Rental income (e.g., rental/lease income);
- Capital gains (e.g., derived from the disposal of real estate or from the sale of shares or units).

A specific provision was included on the tax regime of SIGIs, which provides that capital gains from the disposal of real estate by a SIGI will only be tax-exempt (under the said regime of the CIVs) to the extent that the property disposed has a lease or service agreement in place for at least three years.

This provision is relevant as the informal position of the Portuguese Tax Authorities (PTA) for real estate investment funds/companies has been that income derived from the sale of real estate may be qualified as falling within the category of ‘business income’ rather than ‘capital gains’, whenever the business activity of CIV entails a trading/development activity (e.g., real estate promotion) since only passive income (i.e. income derived from an asset held for investment) should be considered for the purposes of the exclusion of taxation.

All expenses directly connected to the categories of income excluded from taxation should not be tax-deductible when computing the taxable profit of the SIGI, namely expenses incurred with the acquisition (e.g., depreciation) and disposal of real estate, insurances, as well as interest and other financial expenses obtained for acquiring, maintaining and repairing assets generating exempt income.

The taxable income of a SIGI is obtained by offsetting tax losses (if any) to the taxable profit. A SIGI may carry forward tax losses during 5 years which may only be offset against 70% of the entity’s taxable profit, in any given year.

SIGIs are not obliged to make any payments on account or special payments on account of future CIT in any given year.

A SIGI remains subject to autonomous corporate taxation (levied at different rates) on certain qualifying expenses, such as car expenses, per diem allowances, representation expenses, management employee bonus exceeding certain thresholds, among others.

## Withholding tax

Income derived or accrued by a SIGI is not subject to any Portuguese withholding tax.

## Other taxes

Currently, the tax law specifically states that CIVs are also subject to Stamp Tax at a tax rate of 0.0125% on the global net asset value (due on a quarterly basis). SIGIs do benefit from tax regime currently applicable to real estate investment funds/companies despite the fact that they are formally not CIVs. Therefore, SIGIs should, in principle, not be subject to the Stamp Tax over the global net asset value of CIVs.

## Accounting rules

The SIGIs may choose to follow Portuguese GAAP or IFRS until it is officially listed on a regulated market. Then, it must follow IFRS.

### b. Subsidiaries

Holdings in other entities are subject to the limitations set out above in section [2.2]. Only if the Portuguese subsidiaries are deemed as a CIV or as SIGI may they benefit from the same tax regime. Portuguese subsidiaries not qualifying as CIV or SIGI are taxed under the general CIT regime for companies.

### c. Transitional regulations

#### Conversion into REIT status

Possible

There is no special transitional tax regime applicable to the conversion of a regular company into a SIGI. In the framework of CIVs, the PTA has already confirmed that the conversion of a legal entity in a CIV should not be treated as a taxable liquidation or liable to real estate transfer tax. The SIGI obtains tax-exempt status at the beginning of the following taxable year in which the company has been registered as SIGI.

There are nevertheless specific tax rules put in place to clarify tax aspects in the event of loss of quality of SIGI. In such cases, the favourable tax regime ceases as from that fact (loss of status) and the period onwards until the end of the calendar year will be considered a taxable period under the general CIT regime. In addition, any income paid to shareholders post-termination of SIGI regime will be taxed under the general regime (depending on the individual shareholder or corporate shareholder).

### d. Registration duties

#### Registration duties

- No tax is due upon the incorporation of the SIGI
- Real estate transfer tax

No tax is due upon incorporation and capital increases.

The transfer of real estate to and from a SIGI is not exempt from real estate transfer taxes. Real estate transfer tax is due by the purchaser on the higher of the purchase price or cadastral tax value at a rate up to a 6.5%. Stamp Tax is also due on the acquisition of real estate at a 0.8% tax rate unless the acquisition is subject to VAT. Even if the purchase or sale is subject to VAT, real estate transfer tax is always levied.

## 4 Tax treatment at shareholder level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Dividends and capital gains are generally fully taxable, but if participation exemption could apply for qualified shareholders	28% on the distribution of income and capital gains	<ul style="list-style-type: none"> <li>- 25% for resident corporate shareholders (unless participation exemption)</li> <li>- 28% for resident individual shareholders</li> </ul>

#### Corporate shareholder

In the case of resident corporate investors, any income derived from the SIGI (including income distributed by the SIGI and capital gains from the disposal of the shares) will be subject to CIT on the general terms (21% CIT plus applicable surtaxes).

In Portugal there is a participation exemption regime which applies to dividends received (and capital gains derived) by resident corporate entities subject to CIT – which is the case of a SIGI, provided some conditions are met, namely participation of 10% for more than one year.

Since the option was to apply the CIV tax regime to SIGIs, it is important to mention that the law for those CIVs provides that “income from units in real estate investment funds and holdings in real estate investment companies, including capital gains arising from their transfer, redemption or liquidation, shall be deemed as immovable property income”. Due to the potential domestic qualification of income paid by SIGIs, it remains unclear if the participation exemption regime is applicable for qualifying corporate shareholders.

### Individual shareholder

Distribution of income and capital gains will be subject to general rules, meaning income received from the SIGI will be taxed at a flat rate of 28%. Dividend distributions may be subject to withholding tax, which may be treated as a payment on account of the final tax.

#### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Withholding tax on dividends and share redemptions is the final levy for foreign corporate shareholder	Withholding tax on dividends and share redemptions is the final levy for a foreign individual shareholder	<ul style="list-style-type: none"> <li>- A 10% withholding tax for dividends and share redemptions</li> <li>- Capital gains from transfer subject to self-assessment by a foreign shareholder</li> </ul>

### Distributions of income

In the case of a non-resident investor without a permanent establishment in Portugal, a final 10% is withheld on any distributions (and share redemption) made by the SIGI.

The 10% reduced rate will depend on foreign shareholder proving non-resident status towards the paying agent by no later than the last day to deliver the withholding tax to the PTA. Non-residency status may be verified by tax residence certificate (or an equivalent document) issued by foreign tax authorities attesting the respective residency.

In the same way as for domestic shareholders, it remains unclear if, for tax purposes, the distribution of income by a SIGI should be qualified as income from immovable property for purposes of applying the participation exemption regime (i.e., if real estate qualification overrides the dividend qualification a qualifying participation by a shareholder of more than 10% will not access the 0% withholding tax).

### Capital gains

Capital gains arising from the disposal of shares of the SIGI will be subject in Portugal to an autonomous taxation of 10%. The domestic exemption for the sale of shares by non-residents does not apply as we are dealing with a real estate entity (with more than 50% of its asset value composed of real estate).

As the domestic law provides that also capital gains arising from the sale of real estate investment companies are qualified as income from immovable property, the application of tax treaties, which may in some cases restrict Portugal ability to tax, may be questioned.

### c. Anti-abuse Measures

#### Foreign shareholders

The increased rate is applicable to certain foreign shareholders

The 10% rate is not applicable when the shareholders are deemed residents in a blacklisted jurisdiction mentioned in a list approved by the Portuguese Government unless EU/EEA Member State subject to administrative cooperation on a tax matter or third country with a tax treaty in force with Portugal with tax exchange of information provision. In those cases, a 35% rate is due on distributions and a 25% or 28% on capital gains derived by corporate or individual shareholders. The 10% reduced rate will also not be applicable in the case beneficiaries are non-resident entities either directly or indirectly held in more than 25% by Portuguese residents (individuals or entities). In those cases, those non-resident entities are taxed as resident entities.

## 5 Tax treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Taxed under normal Portuguese tax rules	A foreign REIT distribution to a Portuguese shareholder is likely to be treated as a normal dividend from the non-resident company (will depend on the structure of the foreign REIT)	A foreign REIT distribution to a Portuguese shareholder or gains from the disposal is taxed under the general tax rules

### Foreign REIT

A foreign REIT will be taxable under normal Portuguese rules and taxed as non-resident on the income directly derived from real estate assets located in Portugal at 25% rate or as a resident company if there is a permanent establishment.

The Portuguese regime was drafted so that the SIGI regime only applies to entities incorporated and effectively managed in accordance with the Portuguese legislation. If the foreign REIT is investing in Portugal through a Portuguese subsidiary or permanent establishment, the tax regime of the SIGI is not applicable to that entity or permanent establishment. Portuguese subsidiary requires full qualification as SIGI (including free float requirements at Portuguese level) to apply the tax regime.

### Corporate shareholder

A foreign REIT distribution to a Portuguese corporate shareholder (and gains from the disposal of shares) is likely to be treated as a dividend (or gain), which may be fully exempt under certain conditions and subject to the structure of foreign REIT.

### Individual shareholder

As a general rule, dividends and gains will be subject to taxation in Portugal at a 28% tax rate. Double taxation relief may be available, subject to the nature of foreign REIT. ■

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2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction/history/REIT type

	Enacted year	Citation	REIT type	REIT market
SOCIMI	2009	Act 11/2009	Corporate type	Spanish Alternative Stock Market ('MAB') segment and Spanish continuous market (only to the main SOCIMI)

Act 11/2009 governing the '*Sociedades Anónimas Cotizadas de Inversión en el Mercado Inmobiliario*' (known as 'SOCIMI') introduced the REIT vehicle to the Spanish real estate market. However, a substantial change of the SOCIMI regime was enacted in December 2012, with effects as of January 1, 2013. As a result, the new SOCIMI system has been assimilated to other European REITs, in which the main feature is the elimination of direct taxation on the SOCIMI, transferring such taxation to the final investors. Specifically, the SOCIMI will be taxed at a 0% rate. Furthermore, and like in other European REIT systems (i.e. SIICs or UK-REITs), a special levy of 19% has been introduced with the aim of avoiding schemes in which profits distributed by the SOCIMI are free or subject to low taxation at the investor level.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Spain	71	3	EUR 22,954	0.67%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
MERLIN Properties SOCIMI SA	EUR 5,656	3.02%	3.30%	0.35%
Inmobiliaria Colonial SA	EUR 4,972	5.66%	2.04%	0.28%
Lar Espana Real Estate SOCIMI SA	EUR 635	-19.76%	10.70%	0.04%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- To be listed on regulated or alternative markets
- The decision to apply the special tax regime

SOCIMIs must be listed on a regulated market in Spain, in the European Union (or within the European Economic Area) or on a regulated market of any country or territory which there is an actual exchange of tax information uninterruptedly for the entire tax period. Furthermore, after the amendment of the SOCIMI Act in December 2012, listing on alternative multilateral trading markets is also permitted. Likewise, this alternative multilateral trading listing is allowed not only on the Spanish alternative market (Mercado Alternativo Bursátil, 'MAB') but also on any alternative multilateral trading market of the European Union (i.e. Alternative Investment Market), the European Economic Area or any country or territory with which there is an actual exchange of tax information. In this sense, 73 SOCIMIs have been admitted to the MAB, and four SOCIMIs have been admitted to the Euronext Access Paris. Finally, six SOCIMIs are listed on the Spanish Continuous Market (Mercado Continuo) (e.g. Merlin Properties Socimi, S.A.).

Furthermore, the decision to apply this special tax regime must be adopted by the general shareholders meeting and notified to the Tax Authorities prior to the final quarter of the financial period in which it is intended the special tax regime be applied (for example for financial year January 1, 2019 – December 31, 2019, the decision must be adopted before October 01, 2019). This tax regime will take effect as from that financial period (2019) until notification is given to stop applying this special regime. The communications notified to the Tax Authorities after this deadline shall prevent the application of this special tax regime in the said tax period.

### b. Legal form/minimum share capital

Legal form	Minimum share capital
Listed joint stock corporation ( <i>Sociedad Anónima</i> )	EUR 5 million

SOCIMIs must take the form of a listed joint-stock corporation with a minimum share capital of EUR 5 million. Furthermore, the SOCIMI's shares must be nominative, and only one single class of shares is permitted.

Besides, it is compulsory that their corporate name include the name or acronym by which they are known in Spain; i.e. 'Sociedad Anónima Cotizada de Inversión en el Mercado Inmobiliario, Sociedad Anónima' or 'SOCIMI, S.A.'.

Lastly, the SOCIMI's main corporate object must consist of:

- The acquisition and development (refurbishment included) of urban real estate for rental purposes;
- The holding of shares of other SOCIMI or other REITs which are not resident in Spain but which have a similar corporate purpose and similar income distribution requirements; and
- The holding of registered shares in the capital stock of Sub-SOCIMI: non-listed companies –

regardless of whether or not they are tax resident in Spain – whose primary corporate purpose is the acquisition of urban real estate for rent, and who are subject to equivalent investing, income distribution and leverage requirements.

- iv. This Sub-SOCIMI may not hold shares in the capital stock of other entities. Furthermore, the Sub-SOCIMI's shares must be nominative. Only a SOCIMI or other entity as defined in point ii above may be the sole shareholder of the Sub-SOCIMI's share capital.
- v. The holding of shares/participations in real estate collective investment schemes regulated under the Spanish Collective Investment Schemes 35/2003 Act.

Please note that foreign SOCIMIs or REITs had to be tax residents of countries or territories with which there is an actual exchange of tax information in accordance with the First Additional provision of the 36/2006 Act. The real estates located abroad owned by non-resident entities described in point ii above shall be of a similar nature to the real estates located in Spain.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- No threshold of ownership percentage</li> <li>- Minimum free float depending on the listing system</li> </ul>	Yes

#### Shareholder requirements

There is no prohibition on the acquisition of a holding exceeding a certain percentage of the share capital. However, different free float requirements would apply depending on the listing system (see below).

#### Listing requirements

Listing is mandatory, but there is a two-year grace period as of the date of the application for the SOCIMI regime to become listed.

The SOCIMI's shares must be listed in Spain, in the EU or in the European Economic Area on (i) an official regulated secondary market (e.g. Spanish Continuous Market (Mercado Continuo or Bolsa)); or (ii) a multilateral alternative market (e.g. MAB, EURONEXT). Furthermore, the SOCIMI's shares can be listed on a regulated market of any country or territory with which there is an actual exchange of tax information.

As a general rule, the minimum free float for listing on the Spanish Continuous Market is 25%. In the case of MAB listing, shareholders holding a percentage of less than 5% of the share capital must own a number of shares which, as a minimum, represents either (i) an estimated market value of EUR 2 million; or (ii) 25% of the SOCIMI's issued shares. Such calculation will include the shares made available to the liquidity provider to carry out its liquidity duties.

Notwithstanding the above, and according to the MAB Regulations, prior to July 31, 2017, a SOCIMI would have a maximum term of 12 months as from its listing to ensure that its shares are effectively distributed within several shareholders throughout the market (i.e. after a 12 months period the free float requirement would not be fulfilled anymore by making available the free float shares at the disposal of the Liquidity Provider). As from August 1, 2017, this provision shall cease to be applicable.

Finally, the MAB Regulations provide for a lock-up period of one year as from the 'listing date', only applicable to reference shareholders.

On the other hand, it should be noted that the requirements and the procedure applicable to the inclusion and exclusion in the MAB of shares issued by SOCIMI will be subject by the consolidated text approved by the Circulate 9/2017 from January 1, 2018.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- Asset test: at least 80% of their assets must be invested in (a) urban real estate (acquired or developed) for rental or, (b) other SOCIMIs, (c) foreign REITs and (d) Spanish or foreign qualifying subsidiaries ('Sub-SOCIMI') and real estate collective investment schemes
- Revenue test: at least 80% of the SOCIMI's revenue must derive from (i) the lease of qualifying assets, and/or (ii) the dividends distributed by qualifying subsidiaries
- Minimum holding period: qualifying assets are subject to a minimum three-year holding period owned by the SOCIMI

#### Asset test

At least 80% of the SOCIMI's assets shall consist of 'qualifying assets':

- i. Urban real estate for rental purposes, plots destined to the development of the real estate for rental purposes (so long as the development starts within three (3) years period following to the purchase date);
- ii. Shares in similar entities (i.e. other SOCIMI, Sub-SOCIMI, international REITs);
- iii. Shares in real estate Collective Investment Schemes.

This percentage (i.e. 80% of the SOCIMI's assets) shall be calculated on the consolidated balance sheet, if so.

There is no asset diversification rule, and SOCIMIs are entitled to hold a single property asset.

Please note that for the purpose of the provisions of the Spanish SOCIMI regulation, the following shall not be considered as real estates:

- i. the real estates with special features to cadastral effects according to the Spanish Cadastral Act; and
- ii. the real estates assigned to third parties in virtue of agreements equivalent to leasing for the purposes of the Spanish Corporate Income Tax (*Ley del Impuesto sobre Sociedades*).

The real estates acquired shall be owned by the SOCIMIs (including, for these purposes, surface rights, elevation rights and rights to build under the existent building which are filed in the Land Registry, as well as the real estates assigned by third parties to the SOCIMIs in virtue of agreements equivalent to leasing for the purposes of the Spanish Corporate Income Tax (*Ley del Impuesto sobre Sociedades*)).

#### Activity test

Furthermore, at least 80% of the SOCIMI's revenues must derive from the lease of qualifying assets, or from dividends distributed by qualifying subsidiaries (Sub-SOCIMI, foreign REITs and real estate collective investment schemes). Therefore, SOCIMIs are able to develop ancillary activities which represent less than 20% of the total SOCIMI's revenues during the tax-period.

Lease agreements between related entities would not be deemed a qualifying activity and, therefore, the rent deriving from such agreements cannot exceed 20% of the SOCIMI's total revenue.

Capital gains derived from the sale of qualifying assets are in principle excluded from the 80/20 revenue test. However, if such qualifying asset is sold prior to the minimum three year holding period, then (i) the capital gain would compute as non-qualifying revenue; and (ii) it would be taxed at the standard corporate income tax rate, currently set at 25%. Furthermore, the entire rental income derived from this asset would also be subject to the standard corporate income tax rate (25%).

### Minimum holding period

Finally, qualifying assets must be owned by the SOCIMI for a three-year period since (i) the acquisition of the asset by the SOCIMI, or (ii) the first day of the financial year that the company became a SOCIMI if the asset was owned by the company before becoming a SOCIMI. In the case of urban real estate, the holding period means that these assets should be rented; the period of time during which the asset is on the market for rent (even if vacant) will be taken into account, with a maximum of one year.

However, if such qualifying asset is sold prior to the minimum three-year holding period, then (i) the capital gain would compute as non-qualifying revenue; and (ii) it would be taxed at the standard CIT rate, currently set at 25%. Furthermore, the entire rental income derived from this asset would also be subject to the standard CIT rate (i.e. 25%).

### e. Leverage

Leverage
No restrictions

The reform of the SOCIMI Act enacted in 2012 eliminated the leverage restrictions.

Recently approved tax limitations by the Spanish Government (tax deduction of financial expenses and annual depreciation, carrying-forward of tax losses and tax credits) should have no practical impact provided that the SOCIMI is taxed at 0% CIT rate on all income.

### f. Profit distribution obligations

Operative income	Capital gains	Timing
<ul style="list-style-type: none"> <li>- 80% as a general rule (i.e. profits obtained from rental income and ancillary activities)</li> <li>- 100% of profits stemming from dividends distributed by qualifying entities</li> </ul>	<ul style="list-style-type: none"> <li>- 50% of profits derived from the transfer of qualifying property and holdings where the holding period has been met</li> <li>- The remaining 50% must be reinvested in qualifying assets in three years</li> </ul>	<ul style="list-style-type: none"> <li>- In a maximum of six months from the financial year-end</li> <li>- Dividends must be paid to the SOCIMI's investors within one month</li> </ul>

The SOCIMIs that have opted for the SOCIMI special tax regime, are obliged to share their profits in the form of dividends to their shareholders, once the required obligations have been duly completed, as follows:

### Operating income

It is compulsory to distribute 100% of profits stemming from dividends distributed by qualifying entities.

### Capital gains

At least 50% of the profit corresponding to income derived from the transfer (where the holding period has been met) of real estate assets and qualifying holdings must be distributed. The other 50% of that profit must be reinvested in qualifying assets in a period of three years or, otherwise, distributed to the SOCIMI's shareholders. If the object of the reinvestment (i.e. the new qualifying assets) is transmitted before the period of three years, the profit must be distributed to the SOCIMI's shareholders.

### Other profits

At least 80% of the rest of the profits must be distributed.

### Timing

All income must be effectively paid to the shareholders in the month following the date of the distribution resolution. The distribution resolution needs to be adopted within six months of the financial year-end.

## g. Sanctions

#### Penalties/loss of status rules

- Loss of SOCIMI status (i.e. loss of the SOCIMI special tax regime)
- Penalties of between EUR 1,500 and EUR 30,000 in the event of failure to comply with information obligations

The recent reform of the SOCIMI Act has softened the circumstances in which the SOCIMI can be sanctioned with the loss of the SOCIMI status (as regards SOCIMI special tax regime). In particular, such circumstances are:

- i. loss of listed status;
- ii. substantial failure to comply with the information and reporting obligations, unless such failure is remedied in the annual accounts;
- iii. failure to adopt the dividend distribution resolution or the failure to effectively pay the dividends within the deadlines established in the SOCIMI Act. In this case, the loss of SOCIMI status would have effects in the tax year in which the profits not distributed were obtained;
- iv. waiver of the SOCIMI regime by the taxpayer; and
- v. failure to meet the requirements established in the SOCIMI Act unless such failure is remedied the following year. However, the failure to observe the minimum holding period of the assets would not give rise to the loss of SOCIMI status, but (i) the assets would be deemed non-qualifying assets; and (ii) income derived from such assets would be taxed at the standard corporate income tax rate (i.e. 25%).



Should the SOCIMI fall into any of the above scenarios, the SOCIMI special tax regime will be lost and it will not be eligible for the special tax regime for three years.

On the other hand, in the event of non-compliance with information obligations stated by the SOCIMIs Act, the SOCIMIs Act establishes penalties of between EUR 1,500 and EUR 30,000 depending on the kind of information not provided.

### 3 Corporate tax/withholding tax

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- 0% of corporate income tax rate (general rule)</li> <li>- A special levy of 19% on dividend paid to certain shareholders may be imposed on the SOCIMI</li> </ul>	Same rules apply	General withholding tax rules

The SOCIMIs that fulfil the legal requirements may opt for the SOCIMI special tax regime, which will also be applicable to SOCIMI shareholders. The decision to apply this special tax regime must be adopted by the general shareholders meeting and notified to the Tax Authorities prior to the final quarter of the financial period in which the special tax regime is intended to apply.

The SOCIMI special tax regime is incompatible with the implementation of the special regime provided for Title VII of the Spanish Corporate Income Tax (*Ley del Impuesto sobre Sociedades*), except for mergers, divisions, transfers of assets, exchanges of shares and change of registered office of a European company or a European cooperative society from one Member State to another, the international fiscal transparency system and certain leasing.

Furthermore, in case a SOCIMI generates negative tax bases, are not applicable: (i) Article 25 of the Spanish Corporate Income Tax (*Ley del Impuesto sobre Sociedades*) and (ii) the deduction or exemption regime provided for Chapter II, III y IV of the Title VI of the Spanish Corporate Income Tax (*Ley del Impuesto sobre Sociedades*).

#### Current income

As per January 1, 2013, all the income received by a SOCIMI will be taxed under the Spanish Corporate Income Tax ('CIT'), at a 0% rate. Nevertheless, rental income stemming from qualifying assets being sold prior to the end of the minimum holding period (three years) would be subject to the standard CIT rate (i.e. 25%).

#### Capital gains

As a general rule, a SOCIMI will be taxed under CIT, with a 0% flat rate being applicable.

Nevertheless, a SOCIMI will be taxed at the standard CIT rate of 25% if the relevant asset has been sold prior to the end of the minimum holding period (three years), in the circumstances described above.



## Other taxes

The incorporation/share capital increase of a SOCIMI, as well as the contribution of assets to the latter, are eligible for a capital duty exemption. See also section 3.3.

## Withholding tax

General withholding tax rules normally apply in connection with payments made by a SOCIMI. However, dividend payments within a SOCIMI group would be exempt from withholding taxes.

## Anti-abuse measures

The SOCIMI will be taxed at a 19% rate over the full amount of dividends distributed to shareholders representing 5% or more of the total share capital, when the mentioned dividends, at the shareholder level, are exempted from taxes or will be taxed at a rate lower than 10%. This rate shall be considered as CIT.

The preceding paragraph shall not apply when the shareholder is a company which be applied SOCIMI Act. See also section 4.3.

## Accounting rules

SOCIMIs will apply Spanish GAAP. Furthermore, according to the SOCIMI Act, the SOCIMI will be obliged to keep separate accounts for each of the properties held. Additionally, the SOCIMI will be obliged to report some information in the descriptive memorandum (e.g. reserves from financial years preceding, distributed dividends, etc.).

### b. Sub-SOCIMI

Current income	Capital gains	Withholding tax
0% of the corporate income tax rate (general rule)	Same rules apply	General withholding tax rules; no withholding tax over the dividends paid within a SOCIMI group

Some qualifying subsidiaries resident in Spain for tax purposes could, even if not listed, enjoy the same special tax regime as a SOCIMI. In particular, such Sub-SOCIMI must:

- i. be wholly owned by (i) a Spanish SOCIMI (ii) a foreign REIT or (iii) a foreign company assimilated to a SOCIMI;
- ii. have a main corporate object consisting of the acquisition and development (refurbishment included) of urban real estate for rental purposes;
- iii. not hold a stake in other subsidiaries (two levels of subsidiaries are not permitted); and
- iv. meet the same SOCIMI mandatory dividend distribution requirements and the 80/20 asset/revenue tests.

If the above conditions are met, the Sub-SOCIMI could apply for the special tax regime within the same terms and deadlines as the ones described above.

### c. Registration duties

#### Registration duties

95% exemption on Transfer Tax and Stamp Duty

A 95% rebate of Transfer Tax (tax rate between 6% and 11%) and Stamp Duty (tax rate between 0.75% and 2.5%) is applicable to residential real estate acquired for rental purposes, provided that the assets acquired are maintained during the three-year holding period.

Likewise, the incorporation and increase of capital operation in relation to SOCIMIs, as well as non-cash contributions, will be exempted of Transfer and Stamp Duty (ITP and AJD), in the modality of company operations.

Please note that there are some special provisions in relation to the Spanish Value Added Tax (VAT) and the Canary Islands tax system (special regime similar to VAT) as regards SOCIMIs.

### d. Transition regulations

#### Conversion into REIT status

- No exit tax payment
- Tax losses carried forward generated before becoming a SOCIMI are maintained
- The requirements of the SOCIMI regime must be met in the two years following the decision to opt for this tax regime

No exit tax payment is due as a result of the conversion into a SOCIMI. However, upon the transfer of a real estate asset, the stake of the capital gain that corresponds to period pre-SOCIMI under the general tax regime (currently set at 25%).

Tax losses existing prior to the application of the special tax regime can be offset with future positive tax bases of SOCIMI taxable income. This is a scenario that would only arise in cases where the asset maintenance requirements (three years) are breached or where it finds itself in any of the scenarios where it would lose its special tax regime (de-listing, failure to distribute dividends, etc.).

Even if a SOCIMI does not meet all the necessary requirements, it can apply the special tax regime provided that the requirements are met in the following two years after the decision to opt for this tax regime is made.

## 4 Tax treatment at the shareholder level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
General rules, but without the possibility to apply deductions for double taxation on dividends	General rules, but without the possibility of to apply exemption on dividend income	General rules apply

## Corporate shareholder

- i. Dividends will be subject to general taxation. Consequently, dividends received from the SOCIMI will be included in the taxable base of the shareholder and will, in principle, be taxed at the standard 25% CIT rate. No deductions are allowed (i.e. deduction for double taxation).
- ii. Capital gains will be taxed at the standard 25% tax rate. Deduction or exemption to avoid double taxation does not apply. As from January 1, 2017, the exemption to avoid double taxation (art. 21 of Spanish Corporate Income Tax 27/2014 Act) does not apply to the positive incomes obtained.

## Individual shareholder

- i. Dividends will be subject to general taxation. Consequently, dividends received from the SOCIMI will be taxed at the fixed Personal Income Tax rate (currently, between 19% and 23%). No exemptions are allowed.
- ii. Capital gains will also be subject to general taxation. Consequently, dividends received from the SOCIMI will be taxed at the fixed rate (currently between 19% and 23%). No deductions are allowed (i.e. deduction for double taxation).

## Withholding tax

Dividends distributed to shareholders are subject to general rules regarding withholding taxes.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
General rules apply, but without the possibility to apply exemption on capital gains for listed investment funds	General rules, but without the possibility to apply exemption on dividend income and on capital gain for listed investment funds	<ul style="list-style-type: none"> <li>- General rules apply</li> <li>- EU Parent-Subsidiary Directive and double taxation treaties could apply provided that the relevant conditions are met</li> </ul>

## Corporate shareholder

The following relates to foreign corporate shareholders not acting in Spain through a permanent establishment (if the foreign corporate shareholders were acting in Spain through a permanent establishment, the applicable tax treatment would be the same as for Spanish resident corporate shareholders). In this respect we should highlight the following:

- i. Dividends will be subject to Non-Resident Income Tax, at the standard withholding tax rate (currently, 19%). This standard rate can be reduced or eliminated as per the application of the EU Parent-Subsidiary Directive or the relevant double taxation treaties that may be applicable;
- ii. Capital gains will also be subject to Non-Resident Income Tax, at the standard rate for capital gains (currently, 19%). Again, this standard rate can be reduced or eliminated as per the application the relevant double taxation treaties. The exemption on capital gains derived from the transfer of shares of listed investment funds regulated would not be applicable. However, capital gains obtained by those shareholders owning a percentage lower than 5% in the listed SOCIMI would be exempt from Spanish taxation.

## Individual shareholders

The tax treatment for foreign individual shareholders would be similar to the tax treatment applicable to corporate foreign shareholders, with the following specialities.

- i. The foreign shareholder will not be entitled to exemptions;
- ii. The foreign shareholder will not be eligible under the EU Parent-Directive.

## Withholding tax

Dividends distributed to non-resident shareholders are subject to general withholding tax provisions. Thus, non-resident corporate shareholders could be eligible under the EU Parent-Subsidiary Directive, and the relevant double taxation treaties provided that the relevant conditions were met.

### c. Anti-abuse Measures

#### Specific levy of 19%

Applicable to the dividends paid by the SOCIMI to domestic or foreign shareholders under certain circumstances

A special levy regime applies to the dividends paid by the SOCIMI to domestic or foreign shareholders under certain circumstances.

The SOCIMI must assess and pay a 19% levy in respect of the dividends distributed if the beneficiary of the dividends is a Spanish or foreign taxpayer (i) which holds at least 5% of the financial rights of the SOCIMI, and (iii) which is either exempt from any corporate tax on the dividends or subject to tax on the dividend received (i.e. a rate lower than 10%). However, this special levy shall not be applicable to the beneficiary of the dividends that (i) is a company regulated by the SOCIMIs Act (although this company meets both previous points) or (ii) is a company non-resident in Spain (but is resident of countries or territories with which there is an actual exchange of tax information in accordance with the First Additional Provision of the 36/2006 Act) provided that the dividends or profits are subject at least a 10% charge rate.

This special levy will be accrued on the date in which the dividend distribution is formally approved by the SOCIMI. Payment to the Tax Authorities will be due within the two months following the distribution resolution.

## 5 Tax treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
<ul style="list-style-type: none"> <li>- Taxed in Spain, as a non-resident, for the income derived from real estate assets located in Spain</li> <li>- Potential application of the SOCIMI regime to the Spanish subsidiary of the foreign REIT</li> </ul>	Subject to taxation in Spain; specific analysis of foreign REIT is required	Subject to taxation in Spain; specific analysis of foreign REIT is required

## Foreign REIT

The foreign REIT could be subject to taxation in Spain, as a non-resident, on the income derived from the real estate assets located in Spain.

If the foreign REIT is investing in Spain through a Spanish subsidiary, such Spanish subsidiary could enjoy, under certain circumstances, the Sub-SOCIMI regime described above.

## Corporate shareholder

Subject to taxation in Spain. Double-taxation relief credit or participation exemption may be available, specific analysis of foreign REIT is required though.

## Individual shareholder

Subject to taxation in Spain. Double-taxation relief credit may be available, specific analysis of foreign REIT is required though. ■

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UK-REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
UK-REIT	2007	<ul style="list-style-type: none"> <li>- Finance Act 2006, and subsequently issued regulations</li> <li>- Legislation re-written with enactment during Spring 2010</li> <li>- Subsequent amendments made 2012-2019</li> </ul>	Corporate entity

The UK REIT was introduced in the UK with effect from January 1, 2007 by the Finance Act 2006. On January 01, 2007 nine companies elected to become REITs – a number which grew significantly within the first year of the regime. Since then the increase has been small each year, although it has increased more recently due to the changes introduced in 2012 (see further below).

Amendments to the REIT rules were introduced and came into effect in Finance Act 2012. Such changes have made the UK REIT regime more attractive. Entry to the REIT regime is now cheaper – the entry charge has been abolished, new REITs can list on AIM, and there is a three-year grace period for REITs to become widely held and not ‘close’. Furthermore, certain institutions are encouraged to invest in REITs given their shareholdings in a REIT will be treated as widely held. In the Finance Act 2013 and 2014, the Government introduced further amendments in relation to UK REITs investing in other UK REITs. The measure allows the income from UK REITs investing in other UK REITs to be treated as income of the investing REIT’s tax-exempt property rental business, and REIT shareholders to be ignored when considering ‘close’ status. These changes provide three benefits to the REIT sector: investment diversification, cash management flexibility and tax simplification.

From April 6, 2019, changes have been made which exempt a REIT from corporation tax on sales of shares in UK property rich companies (i.e. which derive at least 75% of their value from UK land).

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
UK	55	33	EUR 63,988	4.79%

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Segro	EUR 8,907	11.90%	2.57%	0.78%
Land Securities Group	EUR 6,904	-8.17%	5.47%	0.58%
British Land Co	EUR 5,712	-15.29%	5.76%	0.50%
Derwent London	EUR 3,888	2.46%	2.11%	0.30%
Tritax Big Box REIT	EUR 2,944	4.42%	4.12%	0.26%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)
UK – AIM	6	4	EUR 1,749

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of EPRA AIM Index
Secure Income REIT	EUR 1,291	8.49%	3.93%	61.01%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The EPRA AIM Index is the FTSE EPRA Nareit AIM Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

- An election must be filed prior to conversion
- Certain conditions for REIT status

An election must be filed prior to conversion. In order to become a UK REIT, a group of companies has to confirm that the parent company:

- is UK resident and not resident elsewhere;
- has shares which are admitted to trading on a recognised stock exchange; and
- in addition, has shares which meet the definition of 'listed' on the London Stock Exchange (or foreign equivalent main market exchange) or are traded on a recognised stock exchange (does not apply for first three years);
- is not an open-ended investment company;
- is not a close company (does not apply for the first three years);
- only has shares which are either ordinary shares (of which there can only be one class) or non-voting restricted preference shares;
- has no performance-related loans; and
- that the parent company will produce financial statements.

Strictly, two tax returns (relating to property rental business and residual business of the UK REIT group) should be filed annually. Three sets of financial statements (which demonstrate that the UK REIT group fulfils the various qualifying tests and conditions) need to be filed annually.



## b. Legal form/minimum share capital

Legal form	Minimum share capital
Listed closed-ended company	GBP 700,000 (if listed in the UK on London Stock Exchange)

### Legal form

The parent company of a UK REIT must be a (non-openended) company which meets the listing requirements in 2.3 below. However, there is no requirement as to where it is incorporated. It must be a tax resident in the UK and must not be a tax resident in another country.

Subsidiary entities can be tax resident outside the UK, but such entities may be subject to the local tax regime in that overseas jurisdiction and may suffer tax.

Management may be internal or external.

### Minimum share capital

There are no specific requirements regarding share capital and the normal listing requirements in respect of share capital in relation to the stock exchange on which the shares are listed are applicable.

For example, a UK company that lists on the London Stock Exchange must have a share capital of at least GBP 700,000.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- Not a 'close company'</li> <li>- There are potential penalties if a single corporate shareholder owns 10% or more of the shares/voting rights</li> <li>- No restriction on foreign shareholders</li> </ul>	Yes, must be admitted to trading on a recognised stock exchange and either listed on the London Stock Exchange (or foreign equivalent main market exchange) or traded on any Stock Exchange recognised by the UK tax authorities (within three years)

### Shareholder requirements

A UK REIT cannot be a 'close company'. A company is 'close' where it is controlled by five or fewer shareholders. A listed company will not be close if at least 35% of the shares are owned by the public. 'Public' for this purpose includes shareholders owning less than 5% and pension funds (who do not provide pensions for the employees of that REIT) but excludes non-close companies. Broadly, shares held by institutional investors will count towards those shares treated as widely held. Institutional investors include charities, registered providers of social housing, sovereign wealth funds, pension funds, managers/trustees of authorized unit trusts and OEICs and, since 2014, UK REITs and overseas equivalents to UK REITs. HMRC guidance on what constitutes an overseas equivalent is currently being drafted.

If a corporate shareholder, wherever tax resident, holds 10% or more of the shares or voting rights in a UK REIT, a penalty tax charge will arise (on the REIT) if the REIT pays any dividend to such a corporate shareholder without having taken reasonable steps to prevent the payment of such a dividend. UK REITs therefore usually have restrictions in their Articles of Association that prevent distributions from being

made to corporate shareholders who hold 10% or more of share capital or voting rights and allow a UK REIT to force shareholders to sell stock if they are in danger of breaching the 10% limit.

There are no restrictions on foreign shareholders under the REIT rules.

## Listing requirements

Admission to trading on a recognised stock exchange and, within three years, either listing on the LSE (or foreign equivalent main market exchange) or trading on any other ‘recognised stock exchange’ (which includes AIM ) are required. HM Revenue & Customs maintain a list of recognised stock exchanges across the world.

### d. Asset level/activity test

#### Restrictions on activities/investments

- At least 75% of a REIT’s net profits must be derived from the property rental business (measured using financial statements)
- At least 75% of a REIT’s assets must be used in the property rental business (measured using financial statements)
- The REIT must hold at least three separate property assets
- No one property asset may exceed 40% of the total assets
- May invest outside the UK in real estate wherever located

Restrictions are imposed by the balance of business tests, which limit the amount of investment permitted in non-rental generating assets and the amount of non-rental income. However, other activities are permitted subject to these restrictions. Essentially, only rental profits and capital gains realized on the direct (or qualifying indirect) disposal of properties used in the UK property rental business will be exempt from UK tax.

The balance of business tests state that:

- at least 75% of a UK REIT’s net profits must be derived from the property rental business (wherever located); and
- at least 75% of a UK REIT’s assets must be used in the property rental business (wherever located).

A UK REIT must hold at least three separate assets directly, and no one asset can exceed 40% of the market value of the total portfolio. (Note that a single property which can be multi-tenanted, or is capable of having multiple tenants) will count as more than one asset). Qualifying properties may be residential or commercial and in any location worldwide.

Cash counts as a good asset for the balance of business test, although interest is still taxable and is an income of the residual business.

Owner-occupied assets (that is property used by the UK REIT, e.g. a head-office building) are not qualifying rental assets for the purposes of the balance of business test.

Development by the UK REIT for investment on its own account is permitted, and any direct (or qualifying indirect) disposals are generally included within the property rental business unless development costs exceed 30% of the acquisition cost (or the property’s value at the time of entry to the UK REIT regime if higher) and the property (or the shares in the company holding the property) is sold within three years of completion). Property trading is permitted but is taxable, and falls outside of the property rental business for the purpose of the balance of business restrictions.

The parent company must own at least 75% of the nominal value of the share capital of a subsidiary company for the subsidiary to be a member of the UK REIT group; such members can, in turn, own at least 75% subsidiaries but the parent must ultimately more than 50% of the economic rights attaching to the shares of all the subsidiaries in a group. Where a UK REIT has the right to at least 40% of the profits of a joint venture company, then the proportion of rental exempt income and gains that are attributable to the UK REIT will be exempt from tax, if an election is made.

Where UK REITs are partners in a partnership with a share of 20% or less, the share of assets and income are treated as part of the residual business for the balance of business tests although the share of income and gains in relation to qualifying assets will be treated as tax-exempt. Similar provisions apply where the UK REIT has an interest of 20% or less in a unit trust such as a Jersey Property Unit Trust which is a 'Baker trust' (where the income belongs to the investor, but the capital is under the control of the trustees), and where a transparency election is made for capital gains purposes.

## e. Leverage

Leverage
Interest cover test

Interest expense is limited by the Financing Cost Ratio. The ratio is defined as 'property profits' that is, profits of the property rental business before a deduction for interest, losses from a previous accounting period and tax depreciation (capital allowances) divided by the property financing costs (that is finance related to the property rental business which is broadly defined). Finance costs are limited to interest costs and amortisation of discounts relating to financing. They do not include SWAP break costs but do include periodic SWAP payments. The property profits must be at least 1.25 times the property financing costs. Where income cover is less than 1.25 times, a tax charge will arise based on the amount of the property financing costs that cause the ratio to fall below 1.25 times.

As the test looks only at the relationship between rental income and interest costs, a sudden unexpected increase in interest rates or a drop in income may result in a tax penalty. HMRC has the power to waive this penalty charge if the UK REIT is in severe financial difficulty, the ratio is breached due to unexpected circumstances, and the UK REIT could not reasonably have taken action to avoid the ratio falling below 1.25 income cover.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of tax-property rental profits 100% of PIDs from other REITs	Not included in the distribution obligation	Within 12 months of the end of the year

A distribution out of the property rental business of the REIT (i.e. exempt rental income and capital gains) is called a Property Income Distribution – a 'PID'.

### Operative income

90% of the (tax-exempt) income from the property rental business must be distributed within 12 months of the end of the accounting period (however profit from the residual business income does not have to be distributed). REITs can pay stock dividends (i.e. with the option to issue new shares to shareholders) in lieu

of cash dividends, and these are treated as qualifying distributions.

Where a REIT invests in another REIT, 100% of the PID dividends received by the investing REIT must be distributed within 12 months of the end of the accounting period.

## Capital gains

Tax-exempt capital gains arising from the disposal of real estate used in the property rental business do not have to be distributed.

## g. Sanctions

### Penalties/loss of status rules

Tax penalties and the potential loss of the REIT status

The legislation makes provision for penalties or the withdrawal of UK REIT status where certain requirements are breached. These provisions are complex. There are different remedies and time limits, plus some breaches may occur a number of times whereas others may be only breached once before UK REIT status is lost. Consequently, care needs to be exercised to determine how a particular breach may be dealt with. Here is an outline of the rules which will be applied.

Where the parent company of a group UK REIT or a single company UK REIT loses its stock exchange listing or becomes close, then its UK REIT status may be withdrawn with effect from the end of the previous accounting period. In certain circumstances, there will not be a breach, for example:

- if the loss of a stock exchange listing arises from the takeover by another group or single UK REIT; or
- where the group UK REIT or single company UK REIT becomes close as the result of the action of others, but this is remedied by the end of the next accounting period.

Failure to meet the property rental business tests (at least three properties must be held by the REIT, and no property can be worth more than 40%) is a breach which can occur more than once.

Failure to distribute 90% of the taxable profits of a property rental business and 100% of any PIDs received from other UK REITs is a breach. Where the profit distribution obligation is not complied within three months after the point at which the group's results are agreed with HMRC, then a tax charge (currently 19% but reducing to 17% by 2020) will arise on the UK REIT and will be based on the shortfall of the distribution.

It is possible to breach the balance of business test for assets at the beginning of the first accounting period of a UK REIT so long as the test is complied with at the beginning of the next accounting period.

Thereafter, failure to meet the 75% assets test is assessed as a minor breach if more than 50% of the assets are qualifying assets at the beginning of the accounting period, but a major breach if less than 50% of the assets are qualifying assets at that time. Similar provisions apply to the balance of business tests when considering what proportion of the UK REIT's income is rental income.

The UK REIT will incur a 20% tax charge on the amount equivalent to a PID paid to a corporate shareholder which holds 10% or more of the shares in UK REIT. It is therefore usual for the REIT to take steps to discourage such a level of investment (e.g. by amending the company's Articles of Association to prevent such distributions).

There are special rules to deal with multiple breaches which are too detailed to deal with here, but note that in the event of breaches of a number of different requirements in a ten-year period, HMRC can require the group UK REIT or single company UK REIT to leave the REIT regime.

HMRC has significant powers which permit them to make a UK REIT group or single UK REIT company leave the UK REIT regime and can also levy additional taxes if they consider that the UK REIT has entered into arrangements with the sole or main purpose of obtaining a major tax advantage.

Where HMRC issues a notice to leave the UK REIT regime, the UK REIT rules will cease to apply from the start of the current accounting period and for future years; however, the taxpayer can appeal.

### 3 Tax treatment at the REIT level

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Income from a property rental business is exempt from corporation tax</li> <li>- Residual business income is taxable at the current rate of corporation tax (19%)</li> </ul>	<ul style="list-style-type: none"> <li>- Gains realised on disposals of assets used in the property rental business are not subject to tax</li> <li>- Since April 6, 2019, a REIT is also exempt from corporation tax on sales of shares in UK property rich companies (i.e. which derive at least 75% of their value from UK land). The exemption applies to the proportion of the gain that relates to the company's property rental business assets</li> </ul>	<ul style="list-style-type: none"> <li>- In principle, no withholding tax levied on distributions that are made out of the residual business income</li> <li>- Distributions out of the property rental business profits (PIDs) are generally subject to 20% withholding tax unless the recipient is a UK corporate, UK charity or UK pension fund</li> <li>- Withholding tax suffered by a UK REIT on its property rental income from directly held non-UK real estate will be deducted in the calculation of the required PID</li> <li>- Withholding taxes suffered on distributions in respect of shares will be part of the REIT's residual business, and tax credit relief may be available</li> </ul>

#### Current income

Income from the property rental business is not subject to UK corporation tax. Investment by a UK REIT in another UK REIT will be included as an asset of the investing REIT's property rental business. PIDs received will be included as part of the property rental business and tax-exempt, but 100% of PIDs received must be distributed. Non-rental business income (residual income) is taxable in the ordinary manner at the current rate of corporation tax, which is 19%. Corporation tax rates are due to reduce to 17% by 2020. Since April 1, 2017, REITs have been subject to the finance cost restrictions introduced in the UK in line with the OECD's BEPS Action 4 recommendations, subject to certain modifications to take account of the REIT regime. The starting point of the rules is to restrict finance cost deductions to 30% of tax EBITDA. There is also a GBP 2 million de minimis and the option of using an alternative group ratio or a Public Infrastructure Exemption if this will provide a better result. The property rental business of the UK REIT is ring-fenced for corporation tax purposes, which means that it is not possible to offset profits and losses of the property rental business against profits and losses of its residual activities.

#### Capital gains

Capital gains or losses that arise on the disposal of property used in a UK REIT's property rental business are not chargeable to tax. The sale of 'developed properties' may be subject to tax if they are disposed

of within three years of the completion of any development activities conducted by the UK REIT. Any property whose cost of development (where the development is conducted by the UK REIT) exceeds 30% of the fair value of the property's acquisition cost (or value at entry, if later) is deemed to be a 'developed property'. The disposal of property which is used for non-eligible business is taxable. Gains realised on a property used partly for the rental business, and also for taxable business, may be partially exempt from tax.

From April 6, 2019, a REIT is also exempt from corporation tax on sales of shares in UK property rich companies (i.e. which derive at least 75% of their value from UK land). The exemption applies to the proportion of the gain that relates to the company's property rental business assets. This can therefore include companies which have developed UK property unless the development costs exceed 30% of the acquisition cost of the property (or its value at the time of entry to the UK REIT regime if higher) and the shares are sold within three years of completion.

## Withholding tax

The UK does not levy dividend withholding taxes in case of a normal distribution to any investor, regardless of tax residence, but in the case of a distribution by a UK REIT out of its exempt property rental business profits (a PID), tax of 20% will be withheld by the UK REIT and paid to HMRC (although PIDs can be paid to UK companies, UK charities and UK pension funds gross). Overseas investors may be entitled to treaty relief, or sovereign immunity but have to reclaim tax from HMRC.

If an overseas jurisdiction levies a withholding tax on payment of a dividend to a UK REIT, the UK REIT is unlikely to be able to obtain credit for such tax if the income is exempt in the UK. If, however, the income is taxable, it may be possible for the UK REIT to credit this against any UK tax due.

## Other taxes

Stamp duty, stamp duty land tax, employee taxes, uniform business rates and value-added tax apply to UK REITs in the same way that they apply to ordinary property companies.

## Accounting rules

A UK REIT is taxed based on UK entity accounts for each group company (either UK GAAP or IFRS). Group UK REITs are required to consolidate each company's financial statements under IFRS for the purposes of calculating the balance of business tests.

### b. Transition regulations

#### Conversion into REIT status

No conversion charge

Companies entering the UK REIT regime are no longer subject to an entry charge equal to 2% of the gross market value of properties; abolished by FA 2012. For UK tax purposes only, a new accounting period begins at the time of conversion, and the base cost of property rental assets are re-based to market value. Any latent capital gains on property within the UK REIT at the date of conversion are extinguished, but in certain circumstances, the rebasing may be reversed.

### c. Registration duties

#### Registration duties

- Stamp Duty Land Tax (SDLT) of between 1% and 5% for commercial property and 0%-15% for residential property
- Scotland has a Land and Buildings Transactions Tax with rates of between 3% and 4.5% for commercial property and between 0% and 15% for residential property
- Wales has a Land Transaction Tax with rates of between 1% and 6% for commercial property and between 0% and 15% for residential property

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Distributions out of property rental business income (PIDs) are treated as rental profits currently taxable at 19% (for a large company)</li> <li>- Distributions out of residual business profits (non-PIDs) will be tax-exempt</li> <li>- Capital gains on the disposal of UK REIT shares are taxable under normal capital gains rules</li> </ul>	<ul style="list-style-type: none"> <li>- A 20% tax on PIDs (collected by way of the withholding tax)</li> <li>- Higher rate taxpayers pay an additional tax (the amount of which depends on their personal tax position) through their tax returns</li> <li>- Capital gains on the disposal of REIT shares taxable in the normal manner</li> </ul>	<ul style="list-style-type: none"> <li>- A withholding tax is deducted at 20% on PIDs to individual shareholders</li> <li>- Where the distribution is a PID, there is a withholding tax exemption where the REIT has a reasonable belief that the person entitled to the PID is a UK corporate, UK charity or UK pension fund</li> <li>- UK REIT shares held via a 'tax wrapper' such as an ISA can be paid gross</li> </ul>

#### Corporate shareholder

Distributions relating to property rental business (PIDs) are treated as rental profits in the hands of the recipient. These are taxed at the corporation tax rate applying to that company, currently 19%. Distributions of taxed profits (distributions out of the residual business) are likely to be tax-exempt in the hands of UK corporate shareholders.

Distributions of gains from UK REITs are taxed as if they were a distribution of property rental business income.

Capital gains on disposal of shares of a UK REIT are taxable under normal capital gains tax rules.

#### Individual shareholder

PIDs are taxed as rental profits received from direct property, whether the PID represents distributed rental profits or capital gains. The shareholder will be taxed at either 20% (already levied with the withholding tax) or at 40% or 45% for higher rate taxpayers and additional higher rate taxpayers. In this case, the shareholder will pay 20% via withholding tax and the remaining amount through his tax return. Individuals are not entitled to an imputed tax credit, as was the case with normal dividends. Distribution

of taxed profits (distributions out of the residual business) will be taxable in the same way as ordinary dividends, that is, individual shareholders receiving total dividends above GBP 2,000 will be taxed at the marginal rates of 7.5%, 32.5% and 38.1%. These changes do not impact the taxation of PIDs.

Capital gains on the disposal of UK REIT shares are fully taxable in the ordinary manner. The rate of tax on capital gains on shares for individuals is 10% rising to 20% for higher rate taxpayers.

A share buy-back will be a disposal for capital gains purposes and taxable in the ordinary manner.

### Withholding tax

Withholding tax is not deducted where a PID payment is made to a UK corporate shareholder, UK charity or a UK pension fund. A withholding tax of 20% is levied on PIDs to individual shareholders by the UK REIT.

#### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- A 20% final withholding tax for PIDs</li> <li>- The disposal of shares in a UK REIT is within the scope of UK capital gains tax from April 2019 as a result of the 2019 immovable property gains rules (subject to the terms of any relevant Double Tax Treaty)</li> <li>- A REIT falls within the definition of 'Collective Investment Vehicle' and so will not benefit from the exemption from the 2019 immovable property gains rules where the shareholding is less than 25%</li> </ul>	<ul style="list-style-type: none"> <li>- A 20% final withholding tax for PIDs</li> <li>- The disposal of shares in a UK REIT is within the scope of UK capital gains tax from April 2019 as a result of the 2019 immovable property gains rules (subject to the terms of any relevant Double Tax Treaty)</li> <li>- A REIT falls within the definition of 'Collective Investment Vehicle' and so will not benefit from the exemption from the 2019 immovable property gains rules where the shareholding is less than 25%</li> </ul>	<ul style="list-style-type: none"> <li>- Tax treaty relief is available if claimed following receipt</li> <li>- Will be treated as a dividend distribution under most treaties</li> <li>- The Parent-Subsidiary Directive is not applicable</li> </ul>

### Corporate shareholder

Foreign shareholders receive dividends from the tax-exempt property rental business (PIDs) net of basic rate income tax (20%).

### Individual shareholders

Foreign shareholders receive dividends from the tax-exempt property rental business (PIDs) net of basic rate income tax (20%).

### Withholding tax

A corporate or individual non-resident shareholder suffers a withholding tax of 20%. However, any tax suffered may be reclaimed if Treaty relief is available. The PID is only taxed as rental income in the UK; it is likely that the PID will be treated as a dividend distribution under most treaties. The EU Parent-Subsidiary Directive is not applicable (see under no. 2.3 above).



## 5 Tax treatment of foreign REITs and its domestic shareholders

Foreign REIT	UK Corporate shareholder	Individual shareholder
Taxed under normal UK tax rules	May be tax-exempt	20%, 40% or 45% tax on foreign income

### Foreign REIT

A REIT resident outside the UK and investing in UK property will be taxable under normal UK rules as a non-resident landlord with tax at 20% on income and 19% on capital gains for commercial property (including shares in UK property rich entities).

### Corporate shareholder

A foreign REIT distribution of income from property in the UK to a UK corporate shareholder is likely to be treated as a normal dividend from an overseas company. This will depend on the structure of the foreign REIT and may benefit from tax exemption.

### Individual shareholder

A foreign REIT distribution of income from property in the UK to a UK individual shareholder is likely to be treated as a normal dividend from an overseas company (this will depend on the structure of foreign REIT). ■

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FII

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A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type	REIT market
FII	1993	Federal Law 8.668/93, amended by Federal Law 9.779/99, and regulated by Rulings (ICVM) 206/94 and 472/08	Fund type	<ul style="list-style-type: none"> <li>- 250 FII (199 listed)</li> <li>- BRL 58 billion NAV (approx. EUR 13 billion as at May 2019)</li> </ul>

In Brazil, an investment fund for real estate endeavours is called a '*Fundo de Investimento Imobiliário*' (FII). This vehicle was introduced in 1993.

The FII is governed by the Federal Law 8.668/93, amended by Federal Law 9.779/99, and regulated by Brazilian Securities Commission (CVM – Brazilian equivalent to US SEC) under Rulings (*Instrução CVM*) 206/94 and 472/08.

As at May 2019, there were 250 FIIs in operation in Brazil with a net asset value in excess of BRL 58 billion, 199 of which are listed on the São Paulo Stock Exchange – BM&FBovespa.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Brazil	22	0	EUR 3,117	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

- Must be approved by the Brazilian Securities Commission (CVM)
- Managed by a financial institution
- Subscriptions for units must be registered with the CVM

The FII is regulated and supervised by the Brazilian Securities Commission – CVM.

The FII must be formed and managed by financial institutions duly authorised by the CVM. Only financial institutions with investment portfolios, real estate assets, credit portfolios or other financial instruments are authorised to manage an FII.

The fund manager should seek CVM approval before setting up the FII by providing the following:

- fund by-laws and regulations;
- information on the fund's records with the Public Notary;

- iii. appointment of an independent auditor and other service providers;
- iv. appointment of a director employed by the fund manager; and
- v. proof of Corporate Taxpayers ID (CNPJ) registry.

The fund operation depends on prior registration with the CVM, which should be filed with the fund's tax reference number (CNPJ), along with the documents above.

#### b. Legal form/minimum initial capital

Legal form	Minimum share capital
Fund (Contractual agreement between investors and fund manager)	No

##### Legal form

The FII is not a legal person but rather a contractual agreement between investors and a fund manager. The FII is close-ended with limited or unlimited duration.

##### Minimum initial capital

There is no minimum initial capital requirement. Investors will be issued with fund units which may be acquired with cash or in exchange for contributions of real estate or in *rem* rights.

#### c. Unit holder requirements/listing requirements

Unit holder requirements	Listing mandatory
Construction companies may not hold more than 25% interest in an FII	No

##### Unit holder requirements

Construction companies involved in the activities invested in by the FII may hold a maximum 25% interest in the FII. Where the 25% threshold is breached, the FII will lose its tax benefits and suffer tax as an ordinary corporation for income tax purposes.

Unitholders may be individuals or legal entities in Brazil or abroad, and there is no discrimination between Brazilian and foreign investors.

##### Listing requirements

FII units are tradable securities and may be traded on the Stock Exchange or the private 'over-the-counter' market.

The FII does not allow redemption of units, so units can only be sold in the open market through the Stock Exchange or over-the-counter.

Where the duration of the FII is not determined, capital can only be returned to unitholders through a unanimous decision of the unitholders.

#### d. Asset level/activity test

### Restrictions on activities/investments

The minimum real estate investment was previously set at 75% of an FII's total assets, although this requirement has been revoked by ICVM 472/08 effective from December 3, 2008

New regulations set out a list of authorised investments

Under the regulatory rules applicable before ICVM 472/08 (which became effective on December 3, 2008), FIIs were required to invest at least 75% of their total assets in real estate. ICVM 472/08 has revoked all previous regulation applicable to FIIs. However, it has not introduced a new requirement of a minimum level of investment into real estate. Instead, it has introduced a comprehensive list of real-estate-related assets in which an FII may invest (see below). Nevertheless, it is not entirely clear whether FIIs may invest in any type of non-real estate assets (e.g. bonds, fixed-income funds, etc.) under the new regulations.

Under ICVM 472/08, an FII can hold the following assets:

- i. any rights in rem on real estate (e.g. freehold or leasehold);
- ii. stock, debentures, subscription warrants, subscription receipts and similar securities, provided their issuance or trade was registered with or authorised by the CVM, as well as any other securities, whose issuers have activities predominantly allowed to the FII;
- iii. shares in companies whose sole purpose fits into the activities allowed to the FII;
- iv. shares in private equity investment funds ('FIP') where the investment policy of the FIP relates only to activities allowed to the FII or shares in stock investment funds ('FIA') which are divided into sectors and exclusively undertakes property development or investment activities;
- v. some types of construction certificates;
- vi. units in other FIIs;
- vii. mortgage-backed securities and shares in CVM-registered investment funds in credit rights ('FIDC') where the investment policy of the FIDC relates only to activities allowed to an FII;
- viii. mortgage bills; and
- ix. real estate credit bills.

A FII which predominantly invests in securities should observe the investment limits per issuer and type of financial assets set out in ICVM 409/2004.

### e. Leverage

#### Leverage

No leverage restrictions applicable



## f. Profit distribution obligations

Operative income	Capital gains	Timing
At least 95% of income arising on a cash basis	At least 95% of capital gains arising on a cash basis	Every six months

### Operative income

At least 95% of the net operating income must be distributed bi-annually (June 30 and December 31).

### Capital gains

At least 95% of the capital gains must be distributed bi-annually (June 30 and December 31). This requirement only applies to capital gains recognised on a cash basis.

## g. Sanctions

Penalties/loss of status rules
Loss of tax exemption

Construction companies involved in the projects invested in by the FII may not hold more than 25% interest in the FII. Where this condition is breached, the FII will be taxed as a corporation for income tax purposes (34%).

Further sanctions by the CVM may be applicable on a case-by-case basis.

# 3 Tax treatment at the level of REIT

## a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Income from real estate activities is tax-exempt</li> <li>- Income from other activities is subject to withholding income tax</li> </ul>	Capital gains are treated as income from real estate activities and therefore tax-exempt	Withholding tax suffered by the FII may be set against tax on distribution to investors

### Current income

Income from real estate activities (e.g. rental income or income from certain real-estate related securities) is tax-exempt.

Income from fixed-income and variable-income investments is subject to withholding income tax. An exception is made to some particular securities such as Mortgage Notes (*Letras Hipotecárias*), Housing Financing (*Letras de Crédito Imobiliário*) and Agricultural Warrants (*Warrant Agropecuário*).

This withholding tax may be offset against the withholding tax payable on profits distribution to unitholders.

## Capital gains

Capital gains are treated as income from real estate activities and, therefore, tax-exempt.

## Withholding tax

Earnings from investments in fixed income are subject to withholding tax at a rate between 15% and 22.5%, depending on the length of the holding of the investment, and it can be set against tax payable on profits distribution from the FII.

Earnings from investments in variable income are taxed at a rate between 15% and 20% and can be offset against tax payable on profits distribution.

## Other taxes

Transfers of real estate to an FII are subject to a real estate transfer tax (ITBI) imposed by the municipality in which the property is located. The rates vary according to the location and value of the property.

The ownership of property in Brazil is also subject to an annual property tax (IPTU) applied by the municipalities. Again, in this case, the rates vary according to the municipality in which the property is located.

## Accounting rules

The FII must produce its own financial statements, and its accounts should be segregated from the fund manager's. The financial statements should be produced under Brazilian GAAP, which is entirely in line with IFRS for accounting periods ended after 2015.

The accounting period must have 12 months and the financial statements must be published within 90 days of the end of the accounting period.

The preparation of financial statements must:

- observe the specific rules provided by CVM;
- be audited annually by an independent auditor; and
- observe the rules governing the exercise of that activity.

## b. Transition regulations

### Conversion into REIT status

N/A

Existing entities cannot be converted into FIIs.

### c. Registration duties

#### Registration duties

Municipal real estate transfer tax (ITBI) applicable

Transfers of real estate to an FII are subject to a real estate transfer tax (IBTI) imposed by the municipality in which the property is located. The rates vary according to the location and value of the property.

## Tax treatment at the unit holder's level

### d. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
Withholding income tax at 20% on distributions from the FII or capital gains on the disposals of units in the FII	Withholding income tax at 20% on distributions from the FII or capital gains on the disposals of units in the FII; income may be exempt from withholding tax if special conditions are met	Corporate unitholders may credit for withholding tax applied by the FII on distributions

#### Corporate unitholder

Withholding income tax at 20% applies to distributions made by the FII to companies resident in Brazil and on capital gains arising from the disposal of units in the FII. The withholding tax can be offset against the unitholder's own corporate income tax liability.

#### Individual unitholder

Final withholding income tax at 20% applies to distributions made by the FII to individuals resident in Brazil and on capital gains arising from the disposal of units in the FII.

The Law 11.033/2004 sets out that individuals may be exempt from withholding tax on income provided:

- units are negotiated exclusively on the stock exchange or over-the-counter;
- the fund has at least 50 unitholders; and
- the individual benefitting from the tax exemption does not hold 10% or more of the fund's units, or is entitled to more than 10% of the fund's earnings.

#### Withholding tax

Corporate unitholders may credit for withholding tax applied by the FII on distributions and capital gains. However, for individual unitholders who do suffer withholding tax (i.e. individual unitholders who are not compliant with Law 11.033/04), there is no tax credit and the withholding tax is final.

## e. Foreign unitholders

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- Withholding tax at 20% as a general rule</li> <li>- Withholding tax at 15% on income, providing some conditions are met.</li> <li>- Capital gains at 0%, providing some conditions are met</li> </ul>	<ul style="list-style-type: none"> <li>- Withholding tax at 20% as a general rule</li> <li>- Withholding tax at 15% on income, providing some conditions are met</li> <li>- Capital gains at 0%, providing some conditions are met</li> </ul>	Questionable whether tax treaty relief available

### Corporate unitholder

A reduced withholding tax rate of 15% applies to income and capital distributions made by the FII where the foreign investment is registered with the Brazilian Central Bank (Resolução 4.373) and the beneficiary is not resident in a low-tax jurisdiction.

Capital gains arising to the foreign unitholder from the disposal of units in the FII are not subject to tax in Brazil provided:

- the unit is traded on the stock exchange;
- the investment is registered with the Brazilian Central Bank; and
- the beneficiary is not resident in a low-tax jurisdiction.

If either of the conditions above is not met, withholding tax will apply at 20%.

### Individual unitholder

The same beneficial tax rates as described above (corporate unitholder) apply to individuals providing the conditions are met.

### Withholding tax

It is still not clear whether non-resident unitholders in a Brazilian FII may be able to rely on double tax treaties to further reduce the rate of withholding tax on distributions made by the FII. As the legal nature of the FII is a contractual relationship between the fund manager and the investors, the Brazilian tax authorities may argue that the FII is not a 'person' for the purposes of applying double tax treaties.

## 4 Tax treatment of foreign REIT and its domestic unitholders

Foreign REIT	Corporate unitholder	Individual unitholder
Taxed with 15% withholding tax on income and capital gains	Income and capital gains arising to a corporate unitholder taxed at 34% (40% if the beneficiary is a financial institution, insurance or related company)	Income and capital gains arising to an individual unitholder taxed at rates from 7.5% to 27.5%

## Foreign REIT

A foreign REIT is only taxable in Brazil in respect of its income arising from a Brazilian source (e.g. rental income or capital gains related to a Brazilian property). Such income will be subject to a 15% withholding tax in Brazil.

## Corporate unitholder

Income (including capital gains) arising from a foreign REIT to a corporate unitholder resident in Brazil is subject to Brazilian tax at a combined rate of 34% (40% if the beneficiary is a financial institution, insurance or related company). Any withholding tax suffered by the Brazilian unitholder on the distribution from the foreign REIT may be set against the Brazilian unitholder's own tax liability in Brazil, limited to the amount of Brazilian tax due on such distribution.

It is not clear whether the Brazilian resident investor may also claim a credit for any other underlying taxes suffered by the foreign REIT (e.g. withholding tax on rental income).

## Individual unitholder

Income (including capital gains) arising from a foreign REIT to an individual unitholder resident in Brazil is subject to Brazilian tax at rates varying from 7.5% to 27.5% (in practice, individual investors in foreign REITs are likely to be higher-rate taxpayers so the 27.5% should apply). Any withholding tax suffered by the Brazilian unitholder on the distribution from the foreign REIT may be set against the Brazilian unitholder's own tax liability in Brazil.

It is not clear whether the Brazilian resident investor may also claim a credit for any other underlying taxes suffered by the foreign REIT (e.g. withholding tax on rental income). ■

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AMERICAS

# Canada

MFT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
MFT	1994	Income Tax Act	Trust type

The specified investment flow-through rules ('SIFT Rules'), enacted in 2007 and amended in 2009, have had a significant negative impact on non-qualifying Canadian real estate investment trusts ('REITs') and their unitholders, by making them subject to entity-level tax. However, qualifying REITs (as specifically defined for this purpose) are exempted from the SIFT Rules.

Canadian REITs may qualify as 'mutual fund trusts' (MFTs) under the Canadian Income Tax Act (ITA) for which there are comprehensive and detailed rules. An MFT provides for a flow-through of income, dividends and capital gains and, in addition, has many tax benefits associated with vehicles that are qualified for distribution to the public that are not available to trusts that do not qualify as MFTs.

The MFT regime is governed by the ITA and is subject to provincial securities legislation. Generally, an MFT that is a REIT is not a mutual fund under applicable securities legislation.

The SIFT Rules generally do not apply to a publicly-traded trust that qualifies as a 'real estate investment trust' (as defined in the SIFT Rules) throughout a taxation year (the 'REIT Exception'). For purposes of the SIFT Rules, a trust will be a 'real estate investment trust' for a particular taxation year if:

- a. The trust is resident in Canada throughout the taxation year;
- b. At each time in the taxation year, at least 90% of the total fair market value of the trust's 'non-portfolio property' is 'qualified REIT properties'. In general, non-portfolio property includes (a) securities of a 'subject entity' (other than a 'portfolio investment entity') that have a total fair market value that is greater than 10% of the equity value of the 'subject entity' or have a total fair market value that is greater than 50% of the equity value of the trust; (b) Canadian real, immovable or resource property, if at any time in the taxation year the fair market value of all such properties held by the trust is greater than 50% of the equity value of the trust; and (c) property that the trust, or a person or partnership with whom the trust does not deal at arm's length, uses in the course of carrying on a business in Canada;
- c. Not less than 90% of the trust's 'gross REIT revenue' for the taxation year is from one or more of the following: (i) 'rent from real or immovable properties' (as defined in the SIFT Rules), (ii) interest, (iii) dispositions of 'real or immovable properties' (as defined in the SIFT Rules) that are capital properties (as defined in the ITA), (iv) dividends, (v) royalties, and (vi) dispositions of 'eligible resale properties' (as defined in the SIFT Rules) (the 'revenue test');
- d. Not less than 75% of the trust's 'gross REIT revenue' for the taxation year is from one or more of the following: (i) 'rent from real or immovable properties', (ii) interest from mortgages, or hypothecs, on 'real or immovable properties', and (iii) dispositions of 'real or immovable properties' that are capital properties;
- e. At all times in the taxation year, an amount that is equal to 75% or more of the equity value of the trust at that time is the amount that is the total fair market value of all properties held by the trust, each of which is 'real or immovable property' that is a capital property, 'eligible resale property', indebtedness of a Canadian corporation represented by a bankers' acceptance, property described by either paragraph (a) or (b) of the definition 'qualified investment' in section 204 (i.e. generally, certain deposits with financial institutions or certain government debt), or a deposit with a credit union; and
- f. At any time in the taxation year, investments in the trusts are listed or traded on a stock exchange or other public market.

For purposes of the REIT Exception, ‘qualified REIT property’ of a trust means a property held by the trust that is:

- a. A ‘real or immovable property’ that is capital property, an ‘eligible resale property’, an indebtedness of a Canadian corporation represented by a bankers’ acceptance, property described by either paragraph (a) or (b) of the definition ‘qualified investment’ in section 204 (i.e. generally, certain deposits with financial institutions or certain government debt), or a deposit with a credit union;
- b. A security of a ‘subject entity’, where all, or substantially all, of the ‘gross REIT revenue’ is from maintaining, improving, leasing or managing real or immovable properties that are capital properties of the trust, or of an entity of which the trust holds a share or interest, including real or immovable properties that the trust, or of an entity of which the trust holds a share or interest, holds together with one or more other persons or partnerships;
- c. A security of a ‘subject entity’ if the entity holds no property other than:
  - i. legal title to ‘real or immovable property’ of the trust or of another subject entity all of the securities of which are held by the trust (including ‘real or immovable property’ that the trust or the other subject entity holds together with one or more other persons or partnerships), and
  - ii. property described in paragraph (d); or
- d. Ancillary to the earning by the trust of rent from, and capital gains from the disposition of, ‘real or immovable property’, other than equity of an entity or a mortgage, hypothecary claim, mezzanine loan or similar obligation.

‘Rent from real or immovable properties’ includes:

- a. rent or similar payments for the use of, or right to use, ‘real or immovable properties’; and
- b. payment for services ancillary to the rental of ‘real or immovable properties’ and customarily supplied or rendered in connection with the rental of ‘real or immovable properties’.

But does not include:

- (a) management fees;
- (b) payments for hotel rooms or similar lodging facilities; or
- (c) rent based on profits.

‘Real or immovable property’ includes a security of an entity held by the taxpayer that would itself satisfy conditions (b) through (e) of the REIT Exception listed above if such entity was a trust or an interest in real property or a right in immovable property but does not include any depreciable property, other than (i) a property included, otherwise than by an election permitted by regulation, in Class 1, 3 or 31 of Schedule II to the Income Tax Regulations (generally buildings); (ii) a property ancillary to the ownership or utilisation of a property described in (i); or (iii) a lease in, or a leasehold interest in respect of, land or property described in (i).

‘Eligible resale property’ includes ‘real or immovable property’ that is not capital property, is contiguous to a particular ‘real or immovable property’ that is either capital or ‘eligible resale property’ of the entity or an affiliated entity, and is ancillary to the holding of that particular property.

For purposes of the REIT Exception, ‘gross REIT revenue’ of a trust means the total of all amounts received or receivable in the year by the entity in excess of total amounts each of which is the cost of property disposed of in the year.



Canadian hotel and senior living REITs generally do not qualify for the REIT Exception due to their operations being active rather than passive in nature, and, accordingly, such REITs are generally subject to entity-level tax.

The REIT Exception includes looking through rules for certain trust revenues, and a re-characterisation rule for certain changes in the value of foreign currency and from certain hedging activities, in respect of the REIT's real or immovable property. Generally, these amounts will be included in 'gross REIT revenue' to the extent they were realised on revenue in respect of 'real or immovable properties' or on debt incurred for the purpose of earning revenue from 'real or immovable properties'. For example:

- Amounts of income payable by a subsidiary entity to its parent, or an affiliated entity, will generally be deemed to maintain their source character for the parent or affiliated entity where it is included in the parent's 'gross REIT revenue';
- Foreign currency gains included in the trust's 'gross REIT revenue' and realised in respect of 'real or immovable property' situated in a foreign country will be treated as having the same character as 'gross REIT revenue' in respect of the 'real or immovable property';
- Foreign currency gains from debt incurred for the purpose of earning revenue from a qualifying source of REIT revenue (e.g. Euro-denominated debt incurred by the REIT to acquire real or immovable property in a European country from which the REIT earns rental revenue) will be deemed to have the same character as the 'gross REIT revenue' to which it relates; and
- Amounts included in the trust's 'gross REIT revenue' and received under, or as a result of, an arrangement that hedges risk stemming from fluctuations in foreign currency related to sources of revenue in respect of 'real or immovable property' situated outside Canada would also be treated as qualifying REIT revenue.

Amendments to the SIFT Rules were enacted on December 12, 2013, in response to the government's concern over certain transactions involving publicly-traded stapled securities (i.e. securities that are legally separate but which must be bought and sold together). With respect to stapled securities to which the rules apply that involve debt stapled to equity, the rules deny a deduction in computing income of the payer for the interest that is paid or payable on the debt. In addition, where, for example, units of a REIT can only be transferred together with an interest in another entity, the rules would cause any amount (including, but not limited to rent) that is paid or payable by the other entity (or its subsidiaries) to the REIT (or its subsidiaries) on or after July 20, 2011 to be non-deductible in computing the income of the payer for income tax purposes. In both of these cases, there does not appear to be any offsetting adjustment with respect to the income earned by the REIT or its subsidiaries that could result in double taxation of the earnings represented by the non-deductible payments.

The legislation included a transitional period for the application of the rules that, in general terms, delayed their application until January 1, 2016, where the stapled securities were issued on October 31, 2006 (when the SIFT Rules were announced), or before July 20, 2012, for other stapled securities that were issued at the date of the announcement of the rules of July 20, 2011. This legislation applies, in particular, to those REITs that attempted to qualify for REIT status by issuing stapled securities. The rules meant that stapled restructurings used by some Canadian hotel and senior living REITs to remain in the REIT regime are no longer effective. Therefore, relevant REITs that have not already reorganised can now no longer do so in order to avoid the application of these rules.

Despite the various amendments to the rules, a number of Canadian publicly-traded REITs have been able to meet the REIT Exception criteria either through purification of operations or through restructuring. Recently, certain newly formed qualifying Canadian REITs have been created based on the sizeable real property holdings of large publicly traded Canadian retail companies. Such companies have decided to transfer their real property to a Canadian REIT in order to monetise some of the inherent value in their property portfolio, which may be undervalued within their operating businesses. Those trusts impacted by the SIFT rules that fail to meet the REIT Exception criteria will be subject to the entity level SIFT tax.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Canada	46	19	EUR 53,170	3.23%

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Riocan REIT	EUR 5,359	16.64%	5.54%	0.47%
Canadian Apartment Props REIT	EUR 4,761	22.22%	2.85%	0.41%
H & R REIT	EUR 4,385	26.34%	6.04%	0.38%
Allied Properties REIT	EUR 3,473	25.10%	3.37%	0.30%
SmartCentres Real Estate Investment Trust	EUR 3,166	20.51%	5.38%	0.24%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

Election in tax return

Generally, a trust will not meet the requirements of an MFT at the time of its formation because of the unitholder requirements discussed below. If a trust qualifies as an MFT before the 91st day after the end of its first taxation year and elects in its tax return for that year, the trust will be deemed to be an MFT from the beginning of its first taxation year.

## b. Legal form/minimum initial capital

Legal form	Minimum share capital
Unit trust	No

## Legal form

In Canada, the MFT has developed into the most popular publicly traded investment vehicle for Canadian real estate investment. While other tax-efficient vehicles have been considered, the MFT provides the most favourable tax treatment. As such, a Canadian REIT is typically structured as a unit trust that qualifies as an MFT for Canadian income tax purposes.

A unit trust is simply a type of *inter vivos* trust under which the interest of each beneficiary is described by reference to units of the trust. A trust refers to a specific legal relationship created when a person (trustee) holds property for the benefit of another person (beneficiary). The unitholders are the beneficiaries of the trust, and their units represent their right to participate in the income and capital of the trust. The exercise by the trustee of the trustee's duties and powers under the trust is subject to fiduciary and statutory obligations.

The trust indenture or agreement for a REIT will generally provide that no unitholder will be subject to any liability in connection with the REIT or its obligations and affairs and, in the event that a court determines unitholders are subject to any such liabilities, the liabilities will be enforceable only against, and will be satisfied only out of, the REIT's assets. All Canadian provincial jurisdictions, with the exception of the Maritimes, Nunavut, Northwest Territories and the Yukon, have enacted statutes providing a statutory limitation on the liability of unitholders of MFTs (including REITs), as discussed below.

The Income Trusts Liability Act (Alberta) came into force on July 1, 2004. The legislation provides that a unitholder of a trust created by a trust instrument governed by the laws of Alberta, and that is a 'reporting issuer' under the Securities Act (Alberta), will not be, as a beneficiary, liable for any act, default, obligation or liability of the trustee of the Alberta income trust that arises after the legislation came into force. Ontario's Trust Beneficiaries Liability Act, which came into force on December 16, 2004, has a substantially similar provision. The Investment Trust Unitholders' Protection Act (Manitoba), which came into force on June 16, 2005; the Income Trust Liability Act (British Columbia), which came into force on March 30, 2006; and the Income Trust Liability Act (Saskatchewan), which came into force on May 19, 2006, contain similar provisions.

The Civil Code of Quebec also provides the limitation of beneficiary liability for the acts of the trustees of a trust in the absence of fraud.

## Minimum initial capital

No minimum initial capital required.

### c. Unitholder requirements/listing requirements

Unitholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- Minimum of 150 unitholders each of whom holds not less than one 'block of units' and having an aggregate fair market value of no less than CAD 500</li> <li>- Generally, MFTs cannot be established or maintained primarily for the benefit of non-residents of Canada</li> </ul>	Required to avoid redemption right of unitholders

## Unitholder requirements

The Canadian rules applicable to MFTs require that there be at least 150 unitholders each of whom holds not less than one 'block of units' that has a fair market value of no less than CAD 500. The number of units required in a block will depend on its fair market value (e.g. 100 units, if the fair market value of one unit is less than CAD 25). There are rules that deem a 'group' of persons holding units to be one person for

purposes of determining whether there are 150 unitholders. In addition, a class of units of the trust must be ‘qualified for distribution to the public’, which is defined to include a lawful distribution in a province to the public of units of the trust in accordance with a prospectus or similar document.

### Listing requirements

Unit trusts that are not redeemable at the demand of the holder and that qualify as unit trusts because of their real property holdings must be listed on a designated stock exchange in Canada.

In general, to qualify as a ‘unit trust’ (where the units are not redeemable on demand by the holder), the following requirements in respect of property ownership and income must be satisfied:

- At least 80% of its property consisted of any combination of:
  - a. shares;
  - b. any property that, under the terms or conditions of which or under an agreement, is convertible into, is exchangeable for or confers a right to acquire shares,
  - c. cash;
  - d. bonds, debentures, mortgages, hypothecary claims, notes and other similar obligations;
  - e. marketable securities;
  - f. real property situated in Canada and interests in real property situated in Canada (which would include leasehold interests);
  - g. rights to and interests in any rental or royalty computed by reference to the amount or value of production from a natural accumulation of petroleum or natural gas in Canada, from an oil or gas well in Canada or from a mineral resource in Canada.
- No less than 95% of its income was derived from, or from the disposition of, investments described in (a) through (g) above; and
- No more than 10% of its property consisted of bonds, securities or shares in the capital stock of any one corporation or debtor other than Her Majesty in right of Canada or a province or a Canadian municipality.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- Investing in property (other than real property or an interest in real property) is allowed
- Acquiring, holding, maintaining, improving, leasing or managing of any real property (or interest in real property) that is the capital property of the trust is allowed
- Any combination of the foregoing activities

To qualify as an MFT, the only undertaking of a trust must be:

- the investing of its funds in property (other than real property or an interest in real property or an immovable or a real right in an immovable);
- the acquiring, holding, maintaining, improving, leasing or managing of any real property (or interest in real property) or of any immovable (or real right in immovables) that is the capital property of the trust; or

- any combination of the foregoing activities.

An MFT generally may not carry on a business. Consequently, an MFT may not engage in trading in real estate and may not directly operate hotels or nursing homes, which are considered businesses.

#### e. Leverage

Leverage
No limitation on leverage specifically, but thin capitalisation rules may apply to limit tax-deductible interest

The ITA does not impose any leverage rules specifically aimed at MFTs. However, Canada's general thin capitalisation rules could technically apply to limit the deductibility of interest where, in broad terms, the percentage of debts owing by the MFT to certain specified (i.e. unitholders who hold at least 25% of the units) non-resident unitholders of the MFT exceeds a 1.5 to 1 debt to equity ratio. It is common for there to be limitations on leverage as a matter of investment policy set out in the declaration of trust establishing the MFT and disclosed in the prospectus.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
All income of the MFT for a taxation year is paid or payable to unitholders in the year so that MFT does not incur tax	All capital gains are paid out and retain their character as such in the hands of unitholders, provided a designation is made by the MFT	All income must be paid or recognised as a payable in the taxation year of the MFT. If it is payable, then the amount can be paid out later

#### Operative income

An MFT is not required by the ITA to pay out all of its income and capital gains. However, this is the invariable practice as a trust may deduct in computing its income for a taxation year all income paid or payable to unitholders in such year with any remaining income being subject to income tax at the highest marginal personal income tax rate at the trust level. An amount would be 'payable' to a unitholder in a taxation year if the unitholder was entitled in the year to enforce payment. The declaration of trust establishing an MFT normally includes provisions ensuring that the income is 'payable' so the MFT may deduct amounts of income it has not actually paid out by the end of its taxation year.

#### Capital gains

See above.

#### g. Sanctions

Penalties/loss of status rules
Loss of MFT status

If a REIT loses its MFT status, there will be several negative consequences including the following:

- a. The REIT will be subject to a special 36% tax on its ‘designated income’, which includes income from real property in Canada and taxable capital gains from dispositions of real property in Canada and any other ‘taxable Canadian property’;
- b. Units of the REIT will become ‘taxable Canadian property’, with the result that non-residents would generally be taxable in Canada on any gain from disposition of such units, and such dispositions by non-residents would become subject to reporting and withholding requirements;
- c. Units of the REIT may cease to be qualified investments for certain deferred income plans, such as ‘registered retirement savings plans’; and
- d. Transfers of REIT units may give rise to land transfer taxes if the REIT owns real property in certain provinces, such as Ontario

For these reasons, it is considered critical for a REIT to maintain its MFT status. There are special rules that may deem a REIT to retain its MFT status for the balance of the year where such status is lost midway through the year.

### 3 Tax treatment at the level of the REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
An MFT is entitled to deduct in a year all income determined for purposes of the ITA paid or payable to unitholders in the year so it may reduce its net taxable income to nil	Capital gains follow the same system for income, except only 50% of a capital gain (a ‘taxable capital gain’), is included in income, and 50% of a capital loss can be applied to offset taxable capital gains	Credit or refund of foreign withholding tax possible

#### Current income

An MFT is not exempt from income tax under the ITA. Rather, an MFT computes its income in the same manner as any other resident of Canada and is entitled to deduct in computing its income for a taxation year all income paid or payable to a unitholder in such taxation year. Consequently, distributions by an MFT are effected on a pre-tax basis. An MFT cannot flow through any losses to unitholders.

The tax treatment of distributions to unitholders of an MFT will generally depend on their characterisation for purposes of the ITA and the residency of the unitholder. As noted above, the SIFT rules may apply an entity level corporate-style tax on certain REITs that do not qualify for the REIT Exception.

#### Capital gains

Only 50% of a capital gain realised is, in principle, taxed as a taxable capital gain, unless this income is distributed to unitholders during that taxation year, in which case the value of the distribution is deducted from taxable profits (as described above). The other 50% is completely exempt from income tax, whether distributed or not. 50% of a capital loss can be applied as an allowable capital loss to reduce or eliminate taxable capital gains in any of the three years preceding the year or any year following the year in which the taxable gains were realised. The other 50% cannot be applied as an allowable capital loss.

## Withholding tax

If a REIT invests outside Canada, it may be subject to foreign income and withholding taxes. Provided the REIT makes the appropriate designation, investors in the REIT can generally claim a foreign tax credit for all or a portion of the foreign taxes when the related foreign source income is distributed by the REIT. Alternatively, the REIT may deduct such foreign taxes in computing its own income in some circumstances.

## Other taxes

All provinces eliminated capital taxes effective July 1, 2012. In any case, as legal entities that are organised as trusts, REITs were generally not subject to provincial capital taxes.

REITs or their unitholders may be subject to provincial and municipal land transfer taxes in respect of acquisitions of real property. For instance, the highest provincial rate in Ontario is 2% for commercial property calculated on the value of the consideration and payable by the purchaser. Ontario taxes both registered and unregistered conveyances of land. There is limited relief from the tax. The City of Toronto imposes a similar land transfer tax.

Canada has both a federal Good and Services Tax (GST) and provincial sales tax regime. The current federal GST rate is 5%. Canadian REITs are subject to normal Canadian rules which vary depending on the province in which the services are provided.

## Accounting rules

In Canada, accounting rules are published in the CPA Canada Handbook.

All publicly-accountable entities, as defined by the Canadian Accounting Standards Board (AcSB), are required to report financial statements in accordance with International Financial Reporting Standards (IFRS). Therefore, all publicly-traded REITs in Canada are required to report under IFRS.

Provided a REIT does not meet the broadly worded definition for a publicly-accountable entity, as defined by the AcSB, it can choose to follow the Accounting Standards for Private Enterprises (ASPE).

## b. Transition regulations

### Conversion into REIT status

N/A

Where a trust owning property commences to qualify as an MFT, there is no deemed or actual disposition of property and therefore no tax payable under the ITA. There are not any rules permitting a tax-deferred transfer of property to an MFT, except if there is a qualifying transfer of property to the MFT by another MFT or by a 'mutual fund corporation', and other conditions are satisfied. These latter provisions, in effect, provide for a tax-free merger of MFTs.

Some REITs have established Canadian subsidiaries (or indirectly held partnerships) so that transfers to it can qualify for a tax deferral. The vendor of property cannot receive non-share (or non-partnership interest) consideration (e.g. cash, debt) that exceeds the tax cost of the transferred property; otherwise, recapture and gain will be triggered. The shares or partnership interests acquired by the vendor are typically exchangeable for units of the MFT. The exercise of such exchangeable shares or partnership units would generally be a taxable event. Care must be taken to avoid the newly enacted 'character conversion

transaction’ rules in such arrangements that could convert a capital gain, only 50% of which is included in income, into a fully taxable gain.

### c. Registration duties

Registration duties
Real estate transfer tax

Some provinces impose a transfer tax on the acquisition of real estate payable by the purchaser. For instance, Ontario calculates the tax based on graduated rates applied to the value of the consideration for the land. The highest rate for commercial property is 1.5%. See the above discussion in section 3.1 under the heading ‘Other Taxes’.

## 4 Tax treatment at the unitholder level

### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
Taxable	Taxable	N/A

#### Corporate unitholder/individual unitholder

Income (including the taxable portion of capital gains and dividends) paid or payable by an MFT to unitholders will be included in the income of unitholders resident in Canada (whether individuals or corporations), and will be subject to the normal rules of taxation. The rates of taxation will depend on whether the unitholder is an individual or a corporation and the province of residency. For example, in Ontario, the generally prevailing combined federal-provincial income tax rate for 2019 is 26.5% for corporations, and the top combined rate for individuals is 53.53% on taxable income exceeding CAD 220,000.

If a REIT earns taxable dividends from Canadian corporations, provided the REIT makes the appropriate designation those amounts will retain their character as such when distributed. Unitholders that are corporations will generally be entitled to a full dividends-received deduction in respect of such dividends but may, in certain cases, be subject to a refundable Part IV tax on the dividends. Unitholders that are individuals will generally be entitled to preferential tax treatment by claiming a dividend tax credit. Distributions of income that are subject to the new entity-level SIFT tax discussed above will be considered to be dividends to unitholders.

If a REIT realises capital gains, provided the REIT makes the appropriate designation those amounts will retain their character as such when distributed. One-half of capital gains are included in income as ‘taxable capital gains’.

Distributions by an MFT in excess of income may arise because of non-cash deductions such as capital cost allowance. These distributions provide a form of tax deferral because they reduce the tax cost of the units without immediate taxation unless the tax cost becomes negative.

As noted above, capital gains, dividends and foreign source income will retain their character in the hands of unitholders if appropriate designations are filed. Otherwise, the ‘source’ of income is treated as income



from a trust.

On the disposition of a unit of an MFT, the unitholder will realise a capital gain (or a capital loss) to the extent the proceeds of disposition exceed (or are exceeded by) the aggregate of the tax cost of a unit and any disposition costs.

## Withholding tax

There is no withholding on distributions made to residents of Canada.

### b. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- To the extent the distribution is made out of the REIT's income, the withholding tax is imposed at a statutory rate of 25%</li> <li>- Tax exemption for capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- To the extent the distribution is made out of the REIT's income, the withholding tax is imposed at a statutory rate of 25%</li> <li>- Tax exemption for capital gains</li> </ul>	Tax treaty relief available

## Corporate unitholder/individual unitholder

### Distributions

A foreign unitholder (whether a corporation or an individual) will generally be subject to withholding tax on distributions from a REIT.

To the extent the distribution is made out of the REIT's income, the withholding tax is imposed at a statutory rate of 25%. However, under many treaties, the rate is reduced to 15%.

To the extent the distribution exceeds the REIT's income, the ITA provides for a 15% tax if the REIT is a 'Canadian property mutual fund investment' – which essentially means that more than 50% of the value of the REIT's units is attributable to Canadian real property or resource property.

All MFTs, including REITs, are required to keep track of their net capital gains from disposals of 'taxable Canadian property' in a 'TCP gains distributions account'. For example, if the REIT realises a gain on disposal of a Canadian real property investment, the full amount of that capital gain will be added to the TCP gains distribution account (despite the fact that only one-half of the capital gain is included in the taxable income of the REIT). When the REIT makes a distribution to a foreign investor, the distribution is treated as coming out of the balance, if any, in the TCP gains distribution account, and any portion of the distribution that would otherwise have escaped Canadian withholding tax is subject to a 15% withholding tax.

### Capital gains

Foreign unitholders (whether corporations or individuals) will generally not be subject to Canadian tax on gains from disposals of REIT units provided an ownership test is met. In particular, the unitholder must not own 25% or more of the REIT's outstanding units at any time during the 60 months preceding the disposal.

## 5 Tax treatment of the foreign REIT and its domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
Taxed on rental income and gains	Fully-taxable	Fully-taxable

### Foreign REIT

A foreign REIT generally will be subject to the normal Canadian tax rules applicable to other foreign investors in Canada, including the following:

- Rental income earned by a foreign REIT from Canadian real estate will generally be subject to a 25% withholding tax, levied on gross rentals; and
- Gains realised from disposal of Canadian real estate by a foreign REIT will be subject to Canadian tax.

In many cases, foreign REITs acquire Canadian properties through special-purpose corporations, unlimited liability companies or trusts. Through the use of leverage, both internal and external, it is normally possible to reduce or, in some cases, eliminate Canadian tax on rental income. Canada's tax treaties generally permit Canada to tax capital gains realised by foreign investors, including REITs, from disposals of real property in Canada or shares of Canadian companies whose value is derived principally from real property in Canada, although certain treaties provide an exemption in the case where the real property is used in a business of the company.

### Corporate unitholder

A corporate unitholder of a foreign REIT will generally be required to include in income any distributions received, whether or not those distributions were sourced from income generated in Canada.

### Individual unitholder

An individual unitholder of a foreign REIT will generally be required to include in income any distributions received, whether or not those distributions were sourced from income generated in Canada. ■

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AMERICAS

# Chile

FI and FIP

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
FI and FIP	2014	Law No. 20,712 on Administration of Funds and Individual Funds Portfolio (the Funds Law)	Fund type

**Public Investment Funds (FI)** and **Private Investment Funds (FIP)** are regulated in Law No. 20,712 published in the Official Gazette on January 7, 2014, and in force from May 1, 2014.

The recent Tax Reform, contained in Law No. 20,780 and Law No. 20,899, introduced modifications to the Funds Law mainly related to funds' tax treatment and in force since 1 January 2017.

In general terms, Funds are defined by law as the equity constituted by contributions made by individuals or entities, exclusively for investment in securities and property that the law allows, which management is the responsibility of an entity different from the contributors.

FIP and FI must not be confused. Indeed, FI must publicly offer their participation quotes, must have at least 50 sharers (or at least one institutional investor), and must be managed only by an Investment Fund Manager. FIP have less than 50 shares, do not make a public offer of their quotes and are managed by an 'Investment Fund Manager' or by a Closed Stock Corporation.

According to the Chilean legislation, an **FI** and **FIP** could invest in shares or quotas (interest ownerships) of an entity, which in turn has an investment on a real estate asset. The foregoing, since it is not possible for an FI or an FIP to invest directly in real estate.

Thus, in Chile, there are no funds equally structured such as REIT, but rather Investment Funds with investments in companies which in turn have an investment in real estate asset.

In this regard, FI and FIP investors are subject to tax on the dividends received by individuals from the FI or FIP and are subject according to general rules with respect to the gains/loss derived from the transfer of their quotas.

## 2 Requirements

### a. Formalities/procedure of FI and FIP

#### Key requirements

- Approval of the fund by the Chilean Securities Commission (FI)
- Management by a Chilean corporation

In case of an FI, the Chilean Securities Commission (*Comisión para el Mercado Financiero* or *CMF*) must approve the internal regulation, the agreements between the fund and its investors, including their amendments.

The FI must be managed by an entity that has to be organised as a special Chilean Stock Corporation in Chile (*sociedad anónima especial*), named 'Investment Fund Manager'. The Investment Fund Manager will be supervised by the CMF, and subject to the regulations stated in Law N° 20,712.

The existence of the ‘Investment Fund Manager’ must also be authorised by the CMF. Its business activity must be limited exclusively to the management of funds or resources from third parties, and it is required to have a minimum paid-in share capital in cash of UF 10,000 (USD 440,000 approximately).

Notwithstanding the aforementioned, these manager companies may include within their object other complementary activities authorised by the CMF.

With respect to FIP, they may be organised without the approval and audit of the CMF. Notwithstanding this, the FIP must be audited by a registered external auditor and fulfil certain corporate requirements. These types of funds may be managed by an Investment Fund Manager, as explained above, or by a Closed Stock Corporation.

## b. Legal form/minimum initial capital

Legal form	Minimum share capital
Unincorporated entities	<ul style="list-style-type: none"> <li>- No initial requirement</li> <li>- After one year, UF 10,000 in case of FI</li> </ul>

### Legal form

Funds (i.e. FI and FIP) may only be organised as unincorporated entities (i.e. do not have the status of a separate legal entity) which are formed by the contributions made by individual and corporate investors. In this sense, since funds are considered as a co-ownership without legal status, they may not be considered as a taxpayer.

### Minimum initial capital

In case of FI, there is no minimum initial capital required, although the law requires that after a year from the commencement of the fund’s operations its total equity must be at least an amount expressed in units of an indicator indexed for inflation called *Unidad de Fomento* or UF. This minimum total equity amount is UF 10,000, which is equivalent to approximately USD 400,000.

If this obligation is not met, the Investment Fund Manager must communicate it to the CMF within the next business day. From this moment, the CMF may grant the FI a period of a maximum of one year to reach the minimum equity requirement. If the situation has not been amended, the fund must be liquidated.

FIP has no minimum initial capital required by law. In relation to this, to the procedure and to the applicable penalty, the FIP must follow the rules stated in the respective internal regulation.

## c. Unit holder requirements/listing requirements for FI and FIP

Unitholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- <b>FIP:</b> less than 50 members that are not ‘members of the same family’ (those who maintain among them a certain degree of consanguinity or affinity relationship, and entities directly or indirectly controlled by each of those people)</li> <li>- <b>FI:</b> at least 50 members or one institutional investor</li> </ul>	No

## Unitholder requirements

**FIP** cannot have 50 or more members. If an FIP reaches 50 or more members, it will be treated as an FI and subject to the same rules and requirements set for FI. On the other hand, after a year from the commencement of the fund's operations, the FIP must be held by at least four unrelated Unitholders, and none of them must hold participation lower than 10%. Furthermore, the Investment Fund Manager and or its related parties can not hold more than 20% of the FIP's equity. The foregoing applies unless an institutional investor is a member of the fund with more than 50% of the quotas issued by the FIP.

The requirement for FI is that after one year from the approval by the Chilean Securities Commission of the FI's internal regulations, the FI must permanently have at least 50 members unless an institutional investor is a member of the fund. In the latter case, just a single institutional investor is required.

With regards to the FI, the Investment Fund Manager, persons or entities related to it and employees of the managing entity may not own individually or considered together more than 35% of the units of the fund that it manages. Any amount owned in excess of 35% would not have any voting rights in the fund's unitholders meetings. They would be required to dispose of their excess units, within the term set by the Chilean CMF and may be subject to administrative penalties imposed by the Chilean CMF.

FIP and FI cannot conduct operations between themselves unless managed by unrelated entities.

## Listing requirements

In the case of FI, the Fund Manager will be responsible for the custody and maintenance of a participation quotas registry, which in turns have to comply with the CMF instructions.

### d. Asset level/activity test

#### Restrictions on activities or direct investments

- Real estate
- Water Rights
- Vehicles of any kind
- Mining properties
- Directly perform productive activities

There are no specified limits concerning the investment on a corporation regarding the value of the real estate assets of the FI or FIP.

Law No. 20,712 establishes in article 57 that direct investments, among others, in real estate, are forbidden for FI and FIP. The Law also forbids the FI and FIP to directly perform productive activities.

According to article 56 of Law No. 20.712, the investment of the fund may be made in shares or rights of real estate stock corporations or companies, respectively.

FI and FIP cannot hold shares in another FI or FIP if both are managed by the same managing entity. No specific consequence has been contemplated for this.

## e. Leverage

Leverage
Liabilities may not exceed the limit set by the internal rules of the fund

Liabilities may not exceed the limit set by the internal rules of the fund.

## f. Profit distribution obligations of FI and FIP

Operative income	Capital gains	Timing
At least 30% of the fund's annual profits	At least 30% of the fund's annual profits	Annually

### Operative income

At least 30% of the FI and FIP annual profits must be distributed each year. Distributions must be paid within 180 days following the close of the commercial year. Provisional distributions in advance of final distributions are allowed.

For purposes of distributing profits, 'income' is defined as the net received benefits which comprise the sum of profits, interest, dividends and capital gains effectively received during the calendar year (cash basis) less the losses and expenses accrued during the same calendar year.

### Capital gains

No distinction is made between capital gains and operative income when calculating the fund's annual profits, at least 30% of which must be distributed each year.

## g. Sanctions

Penalties/loss of status rules
Loss of FI or FIP status and liquidation possible

If the FI or FIP invests in non-authorised assets, it will lose its status and must be dissolved and liquidated.

The Law does not provide for any specific consequence if the profit distribution obligation is not complied with.

Where membership in the FI falls below the 50 member requirement, the Investment Fund Manager must communicate this to the CMF within the next business day. From this moment, the CMF may grant the FI a period of a maximum of one year to reach the minimum member requirement. If the situation has not been amended, the fund must be liquidated.

Finally, in case the FIP does not fulfil the corporate requirements mentioned in point 2.3. above, it will be taxed as a Chilean Stock Corporation (Sociedad Anónima – S.A.).



### 3 Tax treatment at the level of FI and FIP

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt	Tax-exempt	N/A

#### Current income

Funds in Chile do not have a separate legal personality. However, a fund constitutes a separate estate, a pool of assets different to the assets of the management company and the assets of the individuals or entities that hold participation in it.

According to Chilean Tax Law, Funds (i.e. FI and FIP) are not considered as ‘taxpayers’, therefore, they are not levied with corporate tax on their received or accrued profits. Accordingly, the tax authorities may consider that they are not a resident person for treaty purposes, except in cases where the treaty specifically provides otherwise, as provided in the treaties for instance with Croatia, Poland, South Korea and UK.

Notwithstanding Funds are not considered as taxpayers, investment fund manager companies are legally obliged to act on account and on behalf of the funds they manage, being lawfully required to comply with all administrative and tax obligations on their behalf (i.e. withhold, declare and pay taxes imposed on distributions made to their non-resident shareholders).

#### Capital gains

Tax-exempt.

#### Withholding tax

FIP receipts are not subject to withholding taxes in Chile.

#### Other taxes

No other income taxes would be applicable to the fund. However, according to article 81 of Law No.20.712, a 40% tax would apply on the following disbursements or operations made by an FI or FIP:

- those not required for the development of the fund’s activities and investments not authorised by the law;
- loans made by the fund to their individual and non-resident investors;
- providing to its investors the use of one or more of the assets that compose the fund; and
- guaranteeing obligations of the Fund’s individual and non-resident investors with assets belonging to the fund.

In such cases, the Investment Fund Manager is liable for the payment of the tax.



## Accounting rules

IFRS would have to be followed.

### b. Transition regulations

#### Conversion into REIT status

No regulations

No pre-REIT structure is contemplated by Chilean law.

Chilean law does not contemplate the possibility of conversion into a REIT or vice versa.

However, under general rules, the gain derived from the sale of real estate held by individuals or non-residents is exempt up to an amount of 8,000 UF (this amount is the summation of all capital gains obtained by the individual or non-resident for real estate sales during his life)

If the seller is an entity subject to corporate tax, any gain is treated as ordinary income.

### c. Registration duties

#### Registration duties

Notary fee and register fees

Transfers of real estate located in Chile must be formalised in a public deed signed before a public notary and registered with the land register. Notary fees and land register fees apply. In addition, in order to authorise the public deed, evidence must be provided to the notary that there are no outstanding unpaid real estate taxes.

No real estate transfer tax applies in Chile.

VAT is levied on the sale of real property, whether new or used, regardless of who the property is owned by, if the sale is through someone whose ordinary business is the sale of real estate.

## 4 Tax treatment at the unitholder's level, in the case of FI and FIP

### a. Chilean unitholder

Corporate unitholder	Individual unitholder	Withholding Tax
<ul style="list-style-type: none"> <li>- Corporate tax</li> <li>- Tax credit for 65% of the corporate tax paid by such profits at the level of the fund's portfolio companies, if any</li> </ul>	<ul style="list-style-type: none"> <li>- Personal income taxes (IGC)</li> <li>- Tax credit for 65% of the corporate tax paid by such profits at the level of the fund's portfolio companies, if any</li> </ul>	<p>Entities not subject to tax</p> <p>Individuals, general income tax</p>

## Corporate unitholder

Taxable profits distribution and capital gains realised on the sale of units held in a fund are treated in the same way as gains derived from the sale of publicly traded shares of Chilean corporations subject to provisions of article 14 B of the Income Tax Law.

There is a tax credit for 65% of the corporate tax paid by such profits at the level of the fund's portfolio companies, if any.

A return of capital would be tax-free to the extent of basis recovery. Any excess would be treated as dividend income and subject to the treatment discussed above.

## Individual unitholder

Dividends are subject to personal income taxes. In case of a fund investing in corporate entities, a credit for 65% of corporate taxes paid on the underlying investments may be available.

A return of capital distribution is treated the same as for corporate domestic unitholder.

Capital gains realised on the sale of the fund shares are treated the same as for corporate domestic unitholder.

Individual unitholders are liable to self-assess and file the corresponding personal or corporate taxes that apply.

## Withholding tax

Dividends paid to Chilean residents that are legal entities organised in Chile are not subject to withholding tax. Individuals are subject to the general rules of income tax.

### b. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- <b>FI:</b> 10% WHT as sole tax</li> <li>- <b>FIP:</b> 35% WHT (with a 65% tax credit for corporate tax paid by the underlying investments; the tax credit increases up to 100% when the beneficial owner is resident in a tax treaty country)</li> </ul>	<ul style="list-style-type: none"> <li>- <b>FI:</b> 10% WHT as sole tax</li> <li>- <b>FIP:</b> 35% WHT (with a 65% tax credit for corporate tax paid by the underlying investments; the tax credit increases up to 100% when the beneficial owner is resident in a tax treaty country)</li> </ul>	<ul style="list-style-type: none"> <li>- No tax treaty relief available</li> <li>- If the holder is resident in a country with a tax treaty, the tax credit could be 100%</li> </ul>

## Corporate or Individual unitholder

From January 1, 2017, the local taxation of non-residents investors is as follows:

### a. Taxable profits distributions:

**FIP:** Non-resident holders are subject to a 35% withholding tax on the taxable profit distributions made to them by a fund, with a tax credit for 65% of the corporate tax paid by such profits at the level of the fund's portfolio companies, if any.

If the holder is resident in a country with which Chile has a valid tax treaty, the tax credit could be 100% of the corporate tax paid by the underlying investments. In order to be able to use the tax credit benefits, the holder must obtain a 'certificate of residence' from the corresponding tax authority.

The corporate tax rate is 25.5% in 2017 and 27% from 2018 onwards.

**FI:** Dividends paid by an FI are subject to a 10% withholding tax as sole tax, without credit against corporate taxes paid by the underlying investments.

b. Capital Gains:

**FIP:** Non-resident holders are subject to a 35% withholding tax on the capital gain obtained from the sale or redemption of its quotas in a fund.

**FI:** The capital gain obtained from the sale or redemption of the quotas, is subject to a 10% withholding tax as sole tax.

Capital reductions or liquidations qualify as non-taxable income. However, all cash flows must follow the imputation rules set forth in article 14B of the Chilean Income Tax Law according to which distributions shall be firstly allocated to taxable income and then to non-taxable income.

### Withholding tax

Non-residents investors of FI and FIP are non-required to file tax returns for taxable profits distributions, but they are subject to withholding taxes.

The management company of the fund should withhold, declare and pay the tax imposed on distributions made to their non-residents holders. The dividend withholding tax must be filed and paid until the twelfth day of the month immediately following the month in which the dividend was paid.

Regarding the tax rate, no major differences would exist in a case where the investor is resident in a tax treaty country because all Chilean tax treaties have a provision that Chilean dividend Income tax is not subject to the limitation of the dividends article of the treaties. However, as we mentioned before, there will be differences regarding the % of tax credit that could be used against the withholding tax, when this credit proceeds. ■

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AMERICAS

# Costa Rica

REIF

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIF	1997 and 2009, respectively	Securities Market Regulatory Act (Law 7732) and General Regulations of Fund Management Companies and Investment Funds	Fund type (showing some characteristics of a REIT)

Real Estate Investment Trusts do not exist in Costa Rica, per se. However, the Securities Market Regulatory Act establishes a type of investment fund that has similar characteristics.

In general, investment funds are treated as independent estates owned by a plurality of investors. Only authorised investment fund management companies (Sociedades Administradoras de Fondos de Inversión - SAFI) can manage an investment fund. The participation units of the investors are represented by participation certificates (participations), issued with the same characteristics and under the same conditions for each investor. Only investment funds authorised by the General Superintendence of Securities (Superintendencia General de Valores – SUGIVAL) may conduct a public offering of its participation units or quote on a local securities exchange.

Costa Rican legislation establishes two types of real estate investment funds: a) Real Estate Investment Funds (REIF) and b) Real Estate Development Investment Funds (REDIF). The principal difference between these investment funds refers to the type of assets in which each of them is allowed to invest.

REIFs should only be organised as closed-ended funds and can only assume risks related to real estate activity. These funds mainly invest in real estate for leasing and eventually, selling. The real estate must be facilities that have already been built. The assets in which the REIF invests could be located within Costa Rica or abroad. In the former case, the minimum amount an investor can invest into a REIF is USD 1,000, and when the investment is in real estate assets located abroad, the investment must be of at least of USD 5,000. The minimum number of investors into the REIF is 50. For SUGIVAL to authorise a REIF, it must have minimum net assets of USD 5 million and the diversification of assets is subject to the following rules: 80% annual average of monthly balances of the fund assets must be invested in real estate assets and 20% must be kept in cash in a current account to attend cash needs, or in publicly-traded securities. Participants or related entities or individuals cannot act as lessees of the assets of the fund. However, the SAFI or related entities could act as lessees of the fund, provided that the total monthly income they generate does not exceed 5% of the total monthly revenues of the fund. The assets must be valued on an annual basis.

REDIFs should only be organised as closed-ended funds and their public trade is restricted. These funds must invest in real estate development projects, which may be in different development stages, such as a design or construction phase. Once the construction is finished, the real estate must be sold or leased. The assets could be located within Costa Rica or abroad. The minimum amount an investor can invest in a REDIF is USD 1,000. For SUGIVAL to authorise a REDIF, it must have minimum net assets of USD 5 million. The minimum number of investors is 25. The SAFI or related entities could act as lessees of the REDIF, provided that the total monthly income they generate does not exceed 5% of the total monthly revenues of the REDIF.

The investment funds are governed by the Securities Market Regulatory Act (Law 7732 dated December 17, 1997, and published in the Official Gazette No. 18 of January 22, 1998) and the General Regulations of Fund Management Companies and Investment Funds (issued by the Financial System Oversight National Board on December 19, 2008 and published in the Official Gazette No. 10 of January 15, 2009).

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Licence from the National Securities Commission (SUGEVAL) for the investment fund management company (SAFI)
- Registration on the REIF list
- Fund must be authorised by the SUGEVAL
- Approved prospectus by the SUGEVAL

The Investment Fund Management Company (SAFI) could be a local entity or a branch of a foreign entity, but their business purpose must be to act as the investment fund management entity. However, as an ancillary business, they can buy and sell local or foreign investment funds. They must obtain authorisation to operate within the local market from the SUGEVAL. Among other requirements, the request must be filed by the person who will act as a legal representative of the company, and a draft of the articles of incorporation must be attached to the request, along with the shareholders, directors and legal representatives' résumé and a sworn statement indicating that none of them have been convicted of a crime during the previous five years.

Other requirements include: (i) capital stock must be paid and subscribed, (ii) a description of the Integrated Risk Management Unit, which should be structured to comply with the rules of the regulations, and (iii) policies and procedures manual of the SAFI. This manual should include selling and marketing rules.

The license to operate granted by the SUGEVAL to a SAFI is conditional on the filing of the original documents within a six-month period after the authorisation date. Therefore, the SAFI has a six-month period to register the original documents of incorporation before the Mercantile Section of the Public Registry. The SAFI has a one-year term to begin operations as of the date of communication that final requirements have been completed. If the SAFI fails to begin operating during that year, the licence will be cancelled. It is understood that a SAFI has begun operations if it registers at least one investment fund.

As for investment funds, the authorisation process is performed online. Once the authorisation is obtained, the original documentation should be filed within a three-month period.

After obtaining the authorisation, the investment fund will be registered before the Securities and Intermediaries National Registry.

The requirements to register an investment fund include:

- a. a request signed by the legal representative of the SAFI and filed before the SUGEVAL;
- b. a board of directors agreement in which said board agreed on the organisation of the investment fund. This agreement should comply with the requirements specified by the SUGEVAL;
- c. an investment fund prospectus;
- d. a code ISIN issued by the authorised codified entity;
- e. a procedures manual; and
- f. when the fund is to be publicly-traded, it must comply with additional requirements established in the Securities Public Trade Regulations.

The prospectus should include the relevant information of the investment fund that would allow the investors to make an informed investment decision. Therefore, the investment fund prospectus should contain the following information:

- a. the purpose of the investment fund;
- b. the main characteristics of the investment fund (i.e. the characteristics of the participation units and of the issuance and redemption of units procedures, the term of the fund, the mechanisms for estimating returns and distributions to investors, commissions payable to the SAFI, among others);
- c. the terms of investment policy;
- d. descriptions, policies and warnings in relation to the risks associated with the investment;
- e. a general description of the entity responsible for the management of the investment fund (SAFI); and
- f. legal declarations indicating that all information is reliable.

Investment funds must start operations within a nine-month period following the notification from the SUGEVAL that all requirements have been completed. This term may be extended upon request for an additional nine-month period. If they do not start operations during this time, the authorisation to operate the fund would become invalid. However, regarding REDIFs the term to start operations is extended to 18 months.

## b. Legal form/minimum initial capital

Legal form	Minimum share capital
- The SAFI must be a corporation or a branch of a foreign fund manager company	- The SAFI must have a minimum share capital of CRC 132 Million <sup>1</sup> (approx. USD 223,180.31) <sup>2</sup> , as of May 17, 2018. This amount is updated annually; from June 30, 2019, the required amount will be CRC 139 million <sup>3</sup> (approx. USD 235,015.63)

### Legal form

The fund management company can be a Costa Rican corporation or a branch of a foreign fund management entity, both of which should be incorporated before the Public Registry as established by the Commerce Code.

If a foreign management company is interested in marketing a foreign REIF in Costa Rica, the regulations allow the local trading of authorised REIF from the following countries: the United States of America, Spain, Mexico, Colombia, Chile, Canada, Brazil, the United Kingdom, France, the Netherlands, Australia, Germany, Ireland, Italy, Luxemburg, Switzerland, Portugal, Japan and Hong-Kong.

### Minimum initial capital

The SAFI must have a minimum share capital of CRC 139,000,000 (approx. USD 235,015). However, this amount is updated every year through a resolution from the SUGEVAL.

<sup>1</sup> In accordance with the General Superintendence of Financial Entities decree SGV-A-221, in effect as of March 7, 2017.

<sup>2</sup> US\$ 1 = CR\$ 591.45 on May 17 of 2019. Source: Costa Rica Central Bank, Website: [www.bccr.fi.cr](http://www.bccr.fi.cr),

<sup>3</sup> In accordance with the General Superintendence of Financial Entities decree SGV-A-221, in effect as of March 7, 2017.



For REIFs and REDIFs, the real estate investment fund must have USD 5 million in net assets.

The minimum investment value by an investor into REIFs that only invest in assets located in Costa Rica is USD 1,000, and if the REIF invests in assets located outside of Costa Rica, the minimum investment amount is USD 5,000.

### c. Unitholder requirements/listing requirements

Unitholder requirements	Listing mandatory
REIF: Minimum 50 participants REDIF: Minimum 25 participants	Yes

#### Unitholder requirements

The minimum number of participants in a REIF is 50 and REDIF is 25. However, the general rule for investment funds is 50. If the investment fund does not comply with the minimum investors' requirement for a period exceeding the six months, the fund will be deregistered.

#### Listing requirements

Closed-ended investment funds are required by law to be registered for trading on an organised local exchange market.

If the investor decides to sell his/her participation interest, the participation cannot be redeemed directly by the investment fund except in the circumstances established by law. The latter include, for example, when the investors request that their units be bought back, which can be requested when they do not agree with the amendments made to the fund's investment policies.

Therefore, when selling participation in a REIF/REDIF, the participant would have to trade the participation on a stock exchange. The participation value will be determined both by the valuation of the assets and by its fair market value according to the stock exchange.

The SAFI must be registered before the SUGEVAL. However, the SAFI is not a listed company on the Costa Rican Stock Exchange, only the investment fund is listed.

### d. Asset level/activity test

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- The main activity must be the acquisition and/or leasing of real estate</li> <li>- 80% of property in real estate assets</li> <li>- The remaining percentage could be invested in other financial investments, such as publicly-traded securities</li> <li>- No more than 25% of the REIF's income can derive from one individual or corporation that belongs to the same economic unit (does not apply to REDIFs)</li> <li>- There are some limitations regarding the sale of the REIF's asset (does not apply to REDIFs)</li> </ul>

At least 80% of the annual average remaining balance of assets must be invested in real estate. The remaining 20% must be kept in a checking account or invested in publicly traded securities. The 80/20

percentages apply to both Costa Rican investment funds investing in Costa Rican assets as well as CR funds investing in non-Costa Rican assets. However, these percentages should not apply to foreign funds registered with the SUGEVAL since foreign funds must comply with the regulations of their country of incorporation.

REIFs have three years to fulfil these investment percentage requirements.

No more than 25% of the REIF's income can be derived from one individual or corporation that belongs to the same economic unit.

Real estate assets may not be sold by the REIFs until three years after the acquisition and registration as the REIF's property.

Neither investors, individuals nor companies related to the fund may lease real estate belonging to the fund. The SAFI manager or companies integrated to its economic group may lease real estate from the fund as long as it does not represent more than 5% of the REIF's monthly income.

#### e. Leverage

##### Leverage

- Loans to SAFI are limited to 20% of their assets
- Loans to REIFs and REDIFs are limited to 60% of their real estate property and 10% of any other securities owned by the fund (this 10% cap is the same that applies to financial funds)

Loans to SAFI are limited to 25% of their assets<sup>4</sup>. Loans to financial funds are limited to 10% of their assets. In exceptional cases, the SUGEVAL may authorise a 30% limit on loans to financial funds; however, the investors' assembly must agree on this.

Non-financial investment funds may have a leverage of up to 60% of the total value of their assets. This cap applies to REIFs and REDIFs.

In general, with the exception of the specific situations described above, an investment fund may not encumber or lien its assets to obtain debt.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
No requirement	No requirement	No requirement

##### Operative income

The law does not establish a mandatory percentage to be distributed nor a specific timing. This will be established in the investment fund's prospectus. In practice, Costa Rican Funds substantially distribute all of their income to their investors.

<sup>4</sup> Amended by Article 19 of the Regulations of Risk Management issued by the Financial System Oversight National Board on February 13, 2009 and published in the Official Gazette No. 41 of February 27, 2009.

## Capital gains

The law does not establish a mandatory percentage to be distributed, or a specific timing. This will be established in the investment fund's prospectus.

### g. Sanctions

#### Penalties/loss of status rules

Determined by the SUGEVAL

If the Costa Rican investment fund fails to comply with regulatory requirements, the SUGEVAL could take control of the REIF/REDIF or liquidate it.

In the case of closed-ended funds, such as REIFs, the SUGEVAL may call for an investors' assembly to determine if the fund must be liquidated or not. Also, the investors' assembly may decide to liquidate the fund and the Superintendent from the SUGEVAL will ratify the decision.

## 3 Tax treatment at the level of REIF

### a. Corporate tax/withholding tax (current Law –in effect until June 30, 2019)

Current income	Capital gains	Withholding tax
5% on gross income	5% on an adjusted basis	N/A

To date, investment funds, including REIFs and REDIFs have enjoyed a preferential tax treatment in Costa Rica. Article 100 of the Securities Market Regulatory Act (*Ley Reguladora del Mercado de Valores – LRMV*)<sup>5</sup> establishes that investment funds are subject to taxation under a special system, pursuant to which, revenues obtained by investment funds are divided into the following three groups:

- Income derived from bonds, either subject to or exempt from withholding taxes: the general 8% withholding tax on interest income derived from financial investments is applicable in these cases. Bonds issued in local currency by the Banco Popular y de Desarrollo Comunal are exempt. Jurisprudence has stated that an additional 5% fixed rate tax is applicable to the capital gains derived from the sale of such securities, as explained below.
- Income derived from tax-exempt bonds and other types of assets not subject to withholding taxes (i.e. dividends, offshore investments, exchange currency differences, and leases received by real estate investment funds): a 5% fixed rate tax on the gross amount is applicable in these cases.
- Capital gains: a 5% fixed tax rate applies to capital gains derived from the sale of the investment fund's participation. The tax base is the difference between the sale price and the value of the asset in the accounting records on the date of the transaction.

In Costa Rica, there is no registration duty or capital duty on the fund or transfer duty on the transfer of the investor's interests in the fund.

<sup>5</sup> Securities Market Regulatory Act, Law 7732 dated December 17, 1997 and published in the Official Gazette No. 28 of January 27, 1998.

Distributions of yields from a fund are not subject to withholding taxes. Yields, dividends and capital gains derived by the investors from their participation in the investment fund are not considered taxable income. Roll-up is in fact permitted without adverse tax consequences.

Investment funds are exempt from transfer taxes applicable to the acquisition or sale of assets.

## Other taxes

No other taxes should apply.

## Accounting rules

The SUGEVAL has a series of regulations that REIFs/REDIFs must comply with for accounting purposes. Also, REIFs have special rules for the appraisal of assets. Assets must be appraised at least once a year by a registered appraiser and by a financial professional. IFRS 40 is also applicable.

### b. Income Tax Reform (new rules, in effect from July 1, 2019)

On December 2018, the Costa Rican Congress enacted a comprehensive tax reform legislation, through which it established a new Value Added Tax and introduced several amendments to the Income Tax Law, including changes in the way passive income is taxed and a new capital gains tax.

The first aspect to point out from the Tax Reform is that Article 100 of the Securities Market Regulatory Act will be repealed as of July 1, 2019. Therefore, the special taxation rules explained in the previous section will no longer apply from July 1, 2019.

Instead, the following taxation system will apply to passive income and capital gains:

Current income	Capital gains	Withholding tax
Optional tax treatment	15% on an adjusted basis	N/A

The amended Income Tax Law modifies the rules applicable to passive income obtained both from immovable and movable capital, and expressly states that investment funds are considered as taxpayers under the new provisions.

Regarding income derived from immovable capital (i.e. rental income), as a general rule, the investment fund would be subject to a 15% tax on a tax basis corresponding to 85% of the gross amount obtained monthly as rental income. Nevertheless, the same law provides those taxpayers who have hired at least one employee to generate rental income the option to inform the Tax Administration of their intention to be taxed under general income tax rules. Although a 30% tax rate would be applicable to the annual rental income, under general income tax rules the taxpayers are allowed to deduct all expenses incurred to obtain said income.

Furthermore, passive income from movable capital, such as dividends and interest, obtained by the investment fund will be taxed with a 15% tax on gross income, which will generally be withheld at source.

The same law also introduces a 15% capital gains tax imposed on the adjusted basis, which corresponds to the difference between the transfer value and the acquisition value. When an asset is disposed of other than through a sale (e.g. by donation), the market value will be used to determine the gain (or loss).

<sup>5</sup> Stock Market Regulatory Act, Num. 7732 dated December 17, 1997 and published in the Official Gazette Num. 28 of January 27, 1998.

### c. Transition regulations

Conversion into REIT status
N/A

Not applicable under Costa Rican legislation.

### d. Registration duties

Registration duties
Transfer tax exemption

A transfer tax applicable upon the transfer of real estate is levied at 1.5%. Although exempt from transfer tax pursuant to the Securities Market Regulatory Act, the sale of real estate to or from a fund will still be subject to other stamp duties and registration fees, which amount to approximately 1% of the value of the transaction.

## 4 Tax treatment at the unitholder's level

### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
Exempt or 15%	Exempt or 15%	N/A

To date, all passive income, such as dividend income, and capital gains obtained by domestic investors from their participation in an investment fund are exempt from taxation in the country.

Pursuant to the new Article 28 bis of the Income Tax Law, as of July 1, 2019, passive income and capital gains derived by the investor from its participation in the investment fund will be exempt from any tax on the part corresponding to income and capital gains for which investment funds have already paid the corresponding taxes.

### b. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding tax
Not subject to tax	Not subject to tax	15%

To date, all passive income, such as dividend income, and capital gains obtained by foreign investors from their participation in an investment fund are exempt from taxation in the country.

Effective next July 1, 2019, and as a consequence of the elimination of Article 100 of the Securities

Market Regulatory Act, a foreign unitholder that receives Costa Rican source income derived from its participation in an investment fund would be subject to a 15% withholding tax.

## 5 Treatment of foreign REITs and their domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
Taxed under normal Costa Rican income tax rules, whether as a non-resident taxpayer (subject to WHT) or as a PE subject to ordinary income tax	Not liable to tax or 15% withholding tax	15% withholding tax

### Foreign REIT

According to Articles 52 and 59 of the Income Tax Law, a foreign REIT that derives Costa Rican source income would be subject to the non-resident withholding tax, the rate of which may range from 5% to 30% depending on the characterisation of the income.

A foreign REIT that actually owns and rents or develops real estate within Costa Rica could be considered a permanent establishment (PE) in Costa Rica. According to Article 2 of the Income Tax Law, a foreign entity would have a PE in the country if it has a fixed place of business through which it conducts for-profit activities. According to that same provision, a fixed place can be any factory, building or real estate used for those purposes. A PE is considered an autonomous taxpayer for Costa Rican income tax purposes and would be subject to a 30% corporate income tax rate computed on net income. Consequently, it would be required to prove the existence of deductible expenses by complying with a number of tax obligations, including bookkeeping, filing of tax returns, issuance of invoices, etc.

If a foreign REIT wants to be registered before the SUGEVAL, it must comply with certain requirements established by the SUGEVAL, such as being authorised by a regulatory entity that is a member of IOSCO. Also, the investment fund should have at least one year of operation and must have an equity of at least USD 20 million, the fund manager should have a minimum of three years' experience in the field, and should have an independent custodian entity, among others. However, only the commercialisation of real estate investment funds duly authorised in the United States, Spain, Mexico, Colombia, Chile, Canada, Brazil, the United Kingdom, France, the Netherlands, Australia, Germany, Ireland, Italy, Luxemburg, Switzerland, Portugal, Japan and Hong-Kong are permitted.

### Domestic corporate unitholder

As of today, when the foreign REIT distributes its profits to its investors, such distribution of dividend income from the foreign REIT to its corporate unitholders in Costa Rica is not subject to taxation, provided the domestic corporate unitholders are also considered as taxpayers for income tax purposes.

However, effective next July 1, 2019, the abovementioned exemption would only be applicable if the domestic corporate unitholder obtaining dividend income from the foreign REIT performs a for-profit activity in Costa Rica and is a taxpayer for income tax purposes.

Please note that Article 27 ter (2)(iv) of the Costa Rica Income Tax Law establishes that 100% of the PE's net income credited or paid to its parent entity is considered as taxable income subject to a 15% withholding tax.

## Domestic individual unitholder

Currently, when the foreign REIT distributes its profits to its investors, such distribution of dividend income from the foreign REIT to its domestic individual unitholders is subject to a 15% withholding tax. The Tax Reform has not introduced any changes in this regard.

Distribution of dividends to foreign unitholders is subject to a 15% non-resident withholding tax, regardless of whether the beneficiary is a legal entity or an individual.

If the foreign REIT only has investments abroad, with no connection to Costa Rica other than the tax residency of the unitholders (individuals or legal entities), neither the REIT nor the unitholders income is subject to taxation in Costa Rica. ■

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GLOBAL  
REIT SURVEY

AMERICAS

# Mexico

FIBRAS

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction

	Enacted year	Citation	REIT type
FIBRAS	2004 Last amended in 2014	Mexican income tax Law	trust

‘FIBRAS’ (Fideicomisos de Inversión de Bienes Raíces) were introduced in Mexico in 2004 to encourage real-estate investment following the same model of the US REITs (Real Estate Investment trust). Basically, FIBRAS afford a special tax treatment to trusts whose purpose is to acquire or construct real properties to be leased or those whose purpose is to acquire the right to receive income from leasing such properties, as well as those whose purpose is to grant financing for such objectives.

During its first stage (2004-2006), tax incentives were not sufficient to attract investors so additional amendments were introduced in 2007 to attract small and institutional investors to a portfolio of real properties in a diversified array of real property products, such as shopping centres, industrial facilities, office buildings, apartment complexes and hotels, through the issuance of publicly traded securities or real property participation certificates. A New MITL was enacted in December 2013 and became effective on January 1, 2014, pursuant to which some minor aspects are to be considered in FIBRAS.

Recently the FIBRAS have become much more attractive as investment real estate vehicles for both Mexican and non-Mexican investors.

## Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
Mexico	14	6	EUR 12,864	0.56%

## Top REITs\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield	% of Global REIT Index
Fibra Uno Administracion S.A. de C.V.	EUR 4,520	5.54%	8.86%	0.30%
Administradora Fibra Danhos S.A. de C.V.	EUR 1,677	-27.01%	9.56%	0.02%
Prologis Property Mexico S.A. de C.V.	EUR 1,173	36.61%	5.92%	0.06%
PLA Administradora Industrial S. de R.L. de C.V.	EUR 1,086	23.35%	9.90%	0.09%
Macquarie Mexico Real Estate Management S.A. de C.V.	EUR 767	36.90%	6.53%	0.07%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Formation of FIBRAS

### a. Formalities

#### Key requirements

- Incorporation under Mexican law
- Mexican trustee
- FIBRAS: listed and private

First, the trust must be created or established in accordance with Mexican law and the trustee must be a Mexican banking institution authorised to act as such in Mexico.

The primary objective of the trust must be to acquire or construct real properties in order to lease them, to acquire the right to receive income from leasing such properties, or to grant financing for such purposes backed by a mortgage security on the leased assets.

Although in theory there could be Listed FIBRAS and Private FIBRAS, in practice only listed FIBRAS have been incorporated:

- a. listed FIBRAS whose trust certificates for the assets that make up trust property are placed in Mexico among the general investing public; and
- b. private FIBRAS are those formed with at least ten non-related investors, who individually may not own more than 20% of all of the investment certificates issued. Mexican law provides that two or more individuals are considered to be related parties when one of them participates, directly or indirectly, in the administration, control or equity of the other, or when an individual or group of persons participate, directly or indirectly, in the administration, control, or equity of said persons. Members of partnerships are considered to be related, as are the persons who in accordance with this paragraph are considered related parties of said members.

### b. Legal form/minimum initial capital

Legal form	Minimum initial capital
trust	No

#### Legal form

The legal form to establish a FIBRA is through a trust.

trusts in Mexico are governed by the Mexican General Law of Negotiable Instruments and Credit Operations and are entered into with an authorised Mexican financial institution, which acts as the trustee. The settlor in the trust is the investor who contributes real property, funds or both to the trust and the beneficiaries are the parties that are entitled to receive the benefits from the gains or income of the trust.

According to the Mexican income tax Law ('MITL'), real property trusts are considered as FIBRAS provided they meet the following requirements:

- a. The purpose of the trust must be: (i) the acquisition or the construction of real estate property intended for lease; or (ii) the acquisition of the right to receive income from the leasing of such assets; in addition to (iii) granting financing for such purposes backed by a mortgage security on the leased assets.

- b. At least 70% of the funds of the trusts are invested in real estate properties, or in the rights or credits referred to above, and the remainder is invested in Federal Government Securities registered in the National Securities Registry, or in shares of debt-instrument mutual funds.
- c. The real estate properties that are constructed or acquired must be leased and not be sold for at least four years as of the conclusion of their construction or their acquisition. Real properties that are sold before the said term has ended will not receive the preferential tax treatment at hand.
- d. The trust shall be enrolled at the Registry of trusts engaged in the acquisition and construction of real estate, pursuant to the general rules, issued by the Mexican Tax Administration Service. This requirement is deemed to be met when the relevant trust obtains a favourable ruling issued by the Mexican Tax Authorities, concerning the tax treatment applicable to such trust, among other requirements.

### Minimum initial capital

Mexican legal and tax provisions do not establish any limits relating to the initial capital of FIBRAS, but it is natural that a substantial amount of capital will be required for its operation. It is also important to note that Mexico has enacted thin capitalisation rules which will be explained hereinafter.

### c. Certificate holder requirements/listing requirement

Certificate holder requirements	Listing requirement
<ul style="list-style-type: none"> <li>- Solely for Private FIBRAS</li> <li>- At least ten investors who are unrelated parties</li> <li>- Each investor may not hold more than 20% of the certificates</li> </ul>	None

### Certificate holder requirements

The trustee in a FIBRA is required to issue certificates to the investors for the assets in the trust which must be placed in Mexico either among general investing public; or in the alternative be acquired by at least ten non-related investors, none of which may individually own more than 20% of all of the investment certificates issued.

### Listing requirement

Listed FIBRAS certificates required to be listed in the Stock Exchange in order to receive the preferential tax treatment as well as incorporated in accordance with Mexican law.

### d. Patrimony of FIBRAS

Restrictions on activities/investments
70%:30% ratio

At least 70% of the patrimony of FIBRAS must be invested in real estate property or rights to receive income from leasing or acquisition of real estate properties, and the remainder must be invested in securities issued by the Federal Government registered at the National Registry of Securities or in shares of debt-instrument mutual funds.

In general, there are no restrictions regarding real property developments. Please take into consideration that only in case of lodging properties is required by Mexican tax regulations to meet some additional requirements.

#### e. Leverage

Leverage
Thin Capitalisation Rules

Interest payments made to foreign-related parties are subject to thin capitalisation regulations, which provide that interest payments made to foreign-related parties arising from foreign-related debt exceeding three times the average equity of the company ('3-to-1 debt/equity ratio') will not be deductible. Nevertheless, in certain cases, taxpayers may seek a ruling from Mexican tax authorities in order to exceed the 3-to-1 debt/equity ratio mentioned above.

#### f. Taxable income distribution/obligations of the trustee

Taxable income distribution	Timing
95% of taxable income	Annually

#### Taxable income

At least once a year, no later than March 15, the trustee must distribute, to the holders of the investment certificates, at least 95% of the taxable income of the immediately preceding fiscal year generated by the assets that make up the trust property.

#### g. Sanctions

Penalties/loss of status rules
Tax incentives do not apply May lose status as FIBRA

In the event of non-compliance with organisational and asset rules, the trust may lose its status as a FIBRA. The sale of real property prior to the four-year holding period does not constitute 'non-compliance'. In this case, the tax benefit is lost only for the property that is sold.

## 3 Tax treatment at the Level of FIBRAS

#### a. Corporate taxes/Tax withholding

In general terms, income tax is levied at a rate of 30% on taxable income (taxable revenues minus authorised deductions) calculated on an accrual basis.

## Operating income

Mexican tax regulations provide that a trustee of a FIBRA is required to determine, on behalf of the beneficiaries, the income tax arising from the activities of the FIBRA as any corporation or company would, i.e. it will be entitled to deduct any expense that complies with Mexican tax requirements. Once the net gain or taxable income is determined, upon distribution, the trustee will be required to make a tax withholding, unless the beneficiary of the income is exempt from paying such tax (i.e. registered pension or retirement funds). Any distribution made by the trustee to the beneficiaries during the tax year will be creditable against the annual tax liability of the beneficiary.

Mexican tax residents are required to add any distribution made by FIBRAS to other income they receive during the tax year, and they will be entitled to credit the tax withholding made by the FIBRAS.

FIBRAS have no obligation to make estimated payments of income tax. This allows the trust to allocate cash to project financing rather than paying estimated taxes. However, the trust has the obligation to file and pay income tax, as applicable, on an annual basis.

Mexican tax provisions establish that the net operating losses for income tax purposes (NOL's) may be carried forward ten years and that the trust may use its losses sustained in prior taxable years to offset taxable income for the year.

## Capital gains

Upon disposition of any portion to the estate of the FIBRAS, income tax will apply. Please note that the tax must be updated for inflation from the month when the real property was contributed into the trust, and up to the month in which the transfer takes place.

## Other taxes

Local land taxes (property tax and transfer tax) will apply to the real property owned by the FIBRAS.

## Accounting rules

In Mexico, the Federal Fiscal Code (FFC) lists the requirements with which the books and records must comply among which we find the following:

- a. The accounting systems and records must comply with the requirements listed in the Regulations of the Federal Fiscal Code (RFFC) (i.e. preparing financial statements, linking the financial statements with accounts, identifying transactions, and preparing transaction vouchers as evidence of transactions);
- b. The accounting records must be analytical and must be registered within two months following the date on which the respective transactions were performed;
- c. The accounting books must be kept at the tax domicile of the taxpayer;
- d. The books and records must follow the Mexican Financial Information Norms and be kept in Mexican Pesos;
- e. Certain accounting records must be submitted to the Mexican Treasury electronically on a monthly basis;
- f. Mexican entities must also ensure that all invoices and receipts (including for withholding tax) are generated electronically (Comprobante Fiscal Digital por Internet), and must comply with various requirements.

## b. Transition regulations

### Conversion into FIBRA status

Deferred taxation of contributions to the trust

A contribution of real property is deemed a taxable event. Nevertheless, persons who, in their capacity as settlors, contribute real properties to the trust and receive investment certificates for the total or partial value of said properties may defer the payment of the income tax liability on the gain obtained on the sale of such properties until they sell each such certificate. The tax liability corresponding to each certificate sold for the period from the month of the contribution of the real properties to the trust until the month in which the certificates are sold will be updated by inflation.

The tax will be calculated by applying the 30% rate to the amount of the gain obtained in the sale of the real properties and must be paid within fifteen days following the sale of the corresponding investment certificates.

The gain will be calculated in accordance with this MITL. For this purpose, the sale price of said properties will be considered to be the value assigned to them in the indenture of the aforementioned certificates, and the resulting gain will be divided by the number of investment certificates, which is determined by dividing the aforementioned value by the par value of the individual investment certificate.

The deferral of the tax payment will end when the trustee sells the real properties. The settlor who has contributed said properties must pay this tax within fifteen days after the day on which said properties are sold.

## c. Other fees

### Other Fees

- Local property transfer tax
- Public registry fees
- Notary public fees
- trustee fees
- Other local fees

In Mexico, the transfer of real property is subject to a real property transfer tax at a State level. Generally, property transfer tax is triggered when the trustee receives the certificates, but if dealing with a FIBRA, the property transfer tax may be deferred up to the moment the certificate is sold or when the real property is sold by the trust depending on state laws. The transfer tax rate varies depending on the state where the real property is located.

With regard to the fees of the Public Registry, the Notary Public, the trustee, and any other local fees that may apply depending on local laws, please note that the amount to be paid varies depending on the state where the FIBRA is formed, but it is important to take such fees into consideration since such can amount to a considerable sum.

## 4 Tax treatment at the certificate holder level

### a. Domestic holder

Corporate certificate holder	Individual certificate holder	Tax withholding
<ul style="list-style-type: none"> <li>- 30% income tax on the taxable income resulting from the sale of the certificates</li> <li>- Sale of certificates through an authorised Stock Exchange are tax-exempt for income tax, in some cases</li> </ul>	<ul style="list-style-type: none"> <li>- 30% income tax on the taxable income resulting from the sale of the certificates</li> <li>- Sale of certificates through an authorised Stock Exchange are tax-exempt for income tax</li> </ul>	<ul style="list-style-type: none"> <li>- The trust must withhold income tax on the taxable income distributed to the holders of the investment certificates, by applying the 30% rate to the distributed amount of said taxable income, unless the holders that receive the income are exempt from paying income tax on such amounts</li> <li>- The purchaser of the investment certificates must withhold, from the seller, 10% income tax on the gross income that the seller receives for such certificates, without any deductions, unless the seller is a legal entity residing in Mexico for tax purposes or is income tax exempt for the item of income earned from the goods, rights credits or securities that compose the trust estate</li> </ul>

#### Corporate certificate holder

The distributions paid by the trust to Mexican entities are considered taxable income and are subject to income tax at a rate of 30%. The income that derives from the sale of certificates is considered to be taxable income for income tax purposes, and is taxed at a 30% tax rate. Please take into consideration that the trust will carry out a withholding tax at the rate of 30%.

#### Individual certificate holder

The distributions paid by the trust as well as income earned for the disposition of the certificates by Mexican individuals are considered taxable income and is subject to income tax at variable rates depends on the amount of the income. The top rate for individuals in Mexico pursuant to MITL is 35% rate. Please take into consideration that the trust will carry out a withholding tax at the rate of 30%.

Finally, the income from the sale of participant certificates through an authorised Stock Exchange, received by Mexican individuals' resident in Mexico, is exempt for income tax.

#### Tax withholding

The distributions paid by the trust to Mexican entities and individuals is subject to a tax withholding made by the trustee or by the financial broker who has the certificates in deposit unless such entities or individuals are exempt from such payment. Further, the tax so withheld is a tax credit for Mexican entities or individuals.

The purchaser of the investment certificates must withhold, from the seller, 10% income tax on the gross income that the seller receives for such certificates, without any deductions, unless the seller is a Mexican resident individual and the transaction is undertaken in the stock exchange.

## b. Foreign certificate holder

Corporate certificate holder	Individual certificate holder	Tax withholding
Final income tax withholding	Final income tax withholding	<ul style="list-style-type: none"> <li>- 10% tax withholding made by the purchaser of the certificates, unless the transaction is undertaken in a recognised stock exchange</li> <li>- Tax withholding of 30% on the distribution of profits</li> </ul>

### Corporate certificate holder

Amounts withheld from corporate holders of certificates who are foreign residents are deemed as a final tax payment.

If the owner of the certificate is a foreign pension and retirement fund, trust distributions and the transfer of certificates is exempt for income tax purposes. Certain requirements must be met in order to be considered a foreign pension and retirement fund for Mexican tax purposes.

### Individual certificate holder

Amounts withheld from individual holders of certificates who are foreign residents shall be deemed in Mexico as a final tax payment.

### Tax withholding

Distributions paid by the trust to foreign entities and individuals is subject to a tax withholding made by trustee or by the financial broker who has the certificates in deposit at a rate of 30%, unless such entities or individuals are exempt from such payment, and is considered a final tax payment.

The purchaser of the investment certificates must withhold, from the seller, 10% income tax on the gross income that the seller receives for such certificates, without any deductions, unless the seller is a foreign resident and the transaction is undertaken in the stock market.

Finally, it is important to point out, that the foreign shareholders may take advantage of the benefits afforded by the Tax Treaties entered by Mexico.

## 5 Treatment of foreign trust

Foreign trust
Income tax if the foreign trust is considered a resident in Mexico; otherwise -taxation depends on a tax treaty



## Foreign trusts

The benefit of the special tax regime applicable to FIBRAS will not be applicable to a foreign trust because, in order to obtain the special tax regime granted to FIBRAS, the trust must be incorporated under Mexican law. In this case, the activities of the foreign trust in Mexico will determine the applicable tax regime. It is possible that the foreign trust would be treated in Mexico as a permanent establishment. In this case, it would be subject to income tax.

It is possible that it would be treated as a foreign resident with revenues from a source of wealth located in Mexico; accordingly, the income tax treatment will depend on the type of Mexican source income obtained by the non-resident, and whether the non-resident resides in a country with which Mexico has a tax treaty.

## SIBRAS

Until 2014, investors could also incorporate Mexican entities commonly referred to as SIBRAS (Sociedades Inmobiliarias de Bienes Raíces). However, as we mentioned before, a new MITL was enacted in December 2013 and became effective on January 1, 2014, pursuant to which such possibility is now repealed.

Please take into consideration that pursuant to the New MITL commercial corporations that took the tax incentive for SIBRAS, shall abide by the following:

1. Shareholders that contributed real estate to the corporation shall include in gross income the gain from the disposition of the goods so contributed when any of the following situations takes place:
  - a. They dispose of the shares of such corporation, in the proportion that such shares represent with regard to all the shares received by the shareholder for the contribution of the real property to the corporation, provided that such gain was not included in gross income previously; and
  - b. The corporation disposes of the contributed goods, in the proportion that the part being transferred represents of such goods, provided that such gain was not included in gross income previously.

If any of the situations described in the two preceding subsections has not taken place through December 31, 2016, the shareholders of the SIBRAS shall include in gross income the full amount of the gains from the disposition of the contributed goods that were not included in gross income previously.

2. The gains that are included in gross income described shall be updated from the month in which they were earned through the month in which they are included in gross income. ■

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AMERICAS

# Puerto Rico

REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type	REIT market
REIT	<ul style="list-style-type: none"> <li>- Enacted in 1972</li> <li>- Amended in 2000, 2006, 2011, 2014 and 2018</li> </ul>	<ul style="list-style-type: none"> <li>- Internal Revenue Code for a New Puerto Rico, as amended (IRCNP)</li> <li>- IRCNP §1082.01 to §1082.03 and §1101.01(a)(8)(F) (previously PRIRC of 1994 1500 to §1502 and §1101(18))</li> </ul>	In principle, corporate type (election for tax status)	<ul style="list-style-type: none"> <li>- Significant improvements were expected from the 2006 changes in the PRIRC; however, no statistics are available which evidence such improvement</li> <li>- Amendments made during 2014 change certain requirements to increase investment in REITs and the creation of new REITs</li> <li>- In 2018, an amendment was included in §1101.01 specifying every non-profit entity must request a determination from the Secretary approving the tax exemption (applicable to foreign REITs)</li> </ul>

The law that established Real Estate Investment Trusts ('REITs') in Puerto Rico was enacted in 1972 and amended in 2000, 2006, 2011, 2014 and 2018. The REIT provisions are found in the Internal Revenue Code for a New Puerto Rico (IRCNP)<sup>1</sup>, Sections 1082.01 to 1082.03, and Section 1101.01(a)(8)(F) (previously PRIRC of 1994, Sections 1500 to 1502, and Section 1101(18)).

REIT legislation prior to the 2006 amendments was very restrictive and did not result in the expected investment and development that was contemplated when originally enacted. The 2006 amendments liberalised certain requirements to promote REIT market activity in Puerto Rico. However, the Puerto Rico Commissioner of Financial Institutions does not maintain separate statistics for REITs in Puerto Rico. Therefore, there is no public data available to assess any changes to REIT market activity as a result of the 2006 amendments.

During 2014, the REIT legislation was further amended to liberalise certain requirements and include, as an eligible activity, the income from the purchase of real property to be remodelled and rented. The intention for this amendment is to promote the purchase of redeveloped properties by the REITs and help to reduce large inventories held by local banks. In addition, during 2014 the IRCNP was amended to defer the gain realised on certain assets when the total proceeds from the sale of such assets are invested in a REIT. The purpose of this amendment is to promote the investment of local capital into REITs.

On 2018, the IRCNP was amended to require that every nonprofit entity request a determination from the Secretary approving the tax exemption granted under section 1101.01. The Secretary may request a Report of Previously Agreed Procedures or a Compliance Report issued by an Authorised Public Accountant, with a valid license in Puerto Rico in order to confirm that the entity meets the requirements to obtain the exemption requested. In these cases, the request will be deemed approved in thirty days unless the Secretary rejects the request before the said period is complete. The Secretary is empowered to establish, through regulations, administrative determinations, circular letters or bulletins of a general nature, the conditions under which the Compliance Report will apply and the procedures that the Certified Public Accountant must follow to issue said report. This requirement applies to foreign REITs described below in Section 5.

<sup>1</sup> On January 31, 2011, the Governor of the Commonwealth of Puerto Rico signed into law a new Puerto Rico internal revenue code, to be known as the 'Internal Revenue Code for a New Puerto Rico' (hereinafter referred to as the 'IRCNP' or the '2011 Code'). The 2011 Code repealed almost in its entirety the Puerto Rico Internal

The REIT regime is principally a tax regime; corporations, trusts, certain partnerships and associations can elect for REIT status. However, the entity must be created or organised in the Commonwealth of Puerto Rico. In this survey, we refer to the corporate REIT type.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Election with the income tax return
- REITs are regulated by the Puerto Rico Commissioner of Financial Institutions
- Managed by one or more trustees or directors

Once the legal structure is created, in order to operate as a REIT for tax purposes, an election is required. The election is made together with the filing of the income tax return for the year in which the tax regime is intended to be effective.

The Commissioner of Financial Institutions will oversee the operations of the REIT as a regulator. Pursuant to the Puerto Rico Uniform Securities Act, all stocks or shares in a REIT will be considered 'Securities'.

In order to comply with federal laws:

1. The investor must register the issuance of securities as part of the 'full and fair disclosure' policy stated by the Securities Act of 1933;
2. Sales could be regulated by the Securities Exchange Act of 1934;
3. The REIT must also comply with the Uniform Securities Act of Puerto Rico<sup>2</sup>.

The guidelines established by the North American Securities Administration Association (NASAA) will apply until otherwise modified by the Commissioner of Financial Institutions of Puerto Rico via regulations.

REITs shall present audited financial statements together with the corporate income tax return if their gross income for the year is in excess of USD 3,000,000.

The REIT must be managed by one or more trustees or directors.

### b. Legal form/minimum share capital

Legal form	Minimum share capital
Corporation, partnership, trust or association	No minimum capital

<sup>2</sup> Act 20 of 2014 clarifies that REITs must comply with the provisions established by the Uniform Securities Act of Puerto Rico.

Revenue Code of 1994, as amended. However, the new code incorporates many of the provisions of the 1994 PR Code, including the REITs provisions. There are no substantive changes to such provisions in the 2011 PR Code. The 2011 Code also provides further guidance to US REITs that may qualify for tax exemption.

## Legal form

REITs may be organised as corporations, certain types of partnerships, trusts, or associations. These entities must be domestic entities, organised or created under the laws of the Commonwealth of Puerto Rico. The entity must be one that would be taxable as a domestic corporation if it were not for the tax exemption provided for by the Puerto Rican REIT legislation. As a grandfathering provision, any partnerships in existence as of January 1, 2011, the effective date of the 2011 Code, remained in the REIT regime to the extent they have filed an election to be treated as a corporation. Partnerships created on or after January 1, 2011 cannot be REITs.

The REIT cannot be a financial institution as defined under Section 1033.17(f) of the IRCNPR (previously Section 1024(f) of the 1994 PRIRC) or an insurance company subject to taxation under Subchapter A of Chapter 11 of the IRCNPR.

## Minimum share capital

There are no minimum capital requirements in Puerto Rico. Transferable capital must be represented by stocks or participation certificates.

All of its stocks, shares or interests must be transferable and issued exclusively in exchange for cash.

### c. Shareholders requirements/listing requirements

Shareholder requirements	Listing mandatory
At least 20 <sup>3</sup> (50 shareholders prior to January 24, 2014) shareholders or partners	No

## Shareholder requirements

A REIT has to be composed of at least 20<sup>3</sup> shareholders or partners (50 shareholders prior to January 24, 2014). For this purposes, the shareholder of an exempt investment trust<sup>4</sup> shall be classed as shareholders of the REIT.

At no time during the last half of its taxable year should more than 50% of the total value of outstanding shares be owned by less than six individuals, based on the attribution rules of Section 1033.17(b)(2) of the IRCNPR (previously Section 1024(b)(2) of the 1994 PRIRC). In order to comply with these provisions, the REIT must maintain records that demonstrate the actual ownership of its outstanding shares or interests.

At present, there are no distinctions between resident and non-resident shareholders.

## Listing requirements

Listing of a REIT is not mandatory.

<sup>3</sup> Act 20 of 2014 reduced the amount of shareholders from 50 to 20 effective after January 24, 2014.

<sup>4</sup> An exempt investment trust is an entity that avails to the tax treatment under Section 1112.02 of the IRCNPR.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- At least 95% of gross income must be qualifying investment income
- At least 75% of gross income must be qualifying real estate investment income
- At least 75% of the value of total assets must be represented by real estate assets, cash or equivalents, and securities and obligations of Puerto Rico
- Not more than 25% of the value of total assets is represented by securities other than those mentioned above

At least 95% of gross income must be derived from dividends, interest, rents from real property, gain from the sale of stocks, securities, real property and rights to real property, net gain from the sale of certain real estate assets and payments received or accrued for entering into agreements to execute loans guaranteed with mortgages on real property, or acquire or lease real property.

At least 75% of gross income must be derived from:

- (i) rents derived from real property located in Puerto Rico;
- (ii) interest on obligations secured by a mortgage on real property or rights to real property located in Puerto Rico;
- (iii) gain from the sale or other disposition of real property that is not of the type of property that qualifies as inventory; (iv) dividends or other distributions and gains derived from the sale or other disposition of shares of transferable stock, certificates, or participation in another REIT;
- (iv) income from the purchase of real property to be redeveloped and rented; and
- (v) amounts received or accrued as consideration for entering into agreements to make loans secured by mortgages on real property and/or rights to real property located in Puerto Rico, and/or to buy or lease real property and/or rights to real property located in Puerto Rico.

At the end of each quarter of each taxable year, at least 75% of the value of total assets must be represented by real estate assets, cash or equivalents, and securities and obligations of Puerto Rico and/or of the US (and whichever instrumentality or political subdivision thereof); and not more than 25% of the value of total assets must be represented by securities other than those mentioned above. For the purpose of these sections, real property means land located in Puerto Rico or improvements thereon used as: hospitals, schools, universities, public or private housing, transportation facilities and/or public or private roads, office buildings, governmental facilities, facilities of the manufacturing industry, recreational centers, parking facilities, residential properties, shopping centers, hotels and buildings or structures acquired from the government of Puerto Rico, its agencies and instrumentalities.

Subsidiaries of a REIT will not be treated as a separate entity, and all its assets, liabilities, income items, deductions and credits will be considered as belonging to the REIT. Subsidiary means a corporation, company, or partnership wholly owned, directly or indirectly, by a REIT.

Starting January 1, 2007, the acquisition of real property must be made through the purchase of assets, stocks or participations in a transaction that generates Puerto Rican source income subject to tax in Puerto Rico, except for assets bought from the government of Puerto Rico. This acquisition of real property can be either directly or through related companies.

#### e. Leverage

##### Leverage

No restrictions



There are no leverage restrictions. Only for purposes of determining the compliance with the 95% qualifying gross income requirement, the IRCNPR provides a special rule for the income (interest and gain) generated by the REIT with respect to certain hedging instruments.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of net taxable income must be distributed as taxable dividend, and 90% of its exempt income must be distributed as an exempt dividend	Included in net income	Annually

#### Operative income

At least 90% of the net taxable income and exempt net income of a REIT must be distributed annually as taxable and exempt dividends, respectively. If the REIT does not distribute such net income, it will be taxable as a regular corporation at a maximum tax rate of 39%<sup>5</sup>.

#### Capital gains

Gains from the sale of capital assets are part of a REITs gross income computation and therefore part of its net income determination. Also, certain net gains from the sale or disposition of real property that does not constitute a prohibited transaction are part of the net income determination of the REIT.

#### g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Loss of REIT tax exemption</li> <li>- Loss of REIT status</li> </ul>

The election to operate as a REIT could be terminated if the provisions and requirements under the IRCNPR are not satisfied for the taxable year for which the election is made or for any succeeding taxable year. The loss of REIT status requires a five-year waiting period to re-elect unless waived by the Puerto Rico Secretary of Treasury for reasonable cause.

A REIT that fails the gross income tests above, one or both, may be treated as satisfying those tests to maintain its election if: (1) certain disclosures are made with the income tax return for such taxable year, (2) the inclusion of any incorrect information on those disclosures is not due to fraud with the intent to evade taxes, and (3) the failure to meet the test or tests is due to reasonable cause and not to gross negligence<sup>6</sup>.

However, if a REIT fails to comply with the gross income tests above to operate as such during the taxable year but its election is not deemed terminated, the imposition of taxes will be applicable. The penalty is calculated as a tax charge of 100% on the greater of:

- i. the excess of:
  - a. 95% of the gross income (excluding gross income from prohibited transactions) of the REIT, less

<sup>5</sup> Act 40 of 2013 increased the maximum corporate tax rate from 30% to 39%, effective for taxable years commencing after December 31, 2012.

<sup>6</sup> Act 20 of 2014 substituted the term 'willful neglect' for 'gross negligence' effective January 24, 2014.

- b. the amount of such gross income derived from the dividends, interest, rents from rental property and other qualified income; or
- ii. the excess of:
  - a. 75% of the gross income (excluding the gross income from prohibited transactions) of the REIT, less
  - b. the amount of such gross income derived from qualified domestic income; multiplied by a fraction the numerator of which is the taxable income of the REIT for the taxable year (without taking into account any deduction for net operating loss) and the denominator of which is the gross income for the taxable year (excluding gross income from prohibited transactions).

In addition, the REIT is subject to a 100% tax on prohibited transactions, as discussed below.

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Eligible income is tax-exempt	Eligible capital gains are tax-exempt	Eligible income received by the REIT is not subject to withholding tax

#### Current income

The eligible income is not taxed at the level of the REIT to the extent that the distribution requirements are met.

Income from prohibited transactions is subject to tax at a rate of 100%. This tax is levied upon the net income from prohibited transactions, excluding prohibited transactions for which there was a loss. A prohibited transaction is the sale or disposition of property primarily held for sale to customers in the ordinary course of a trade or business (inventory). The sale of certain real property shall not be treated as a prohibited transaction if certain requirements are met and the property is held for one year or more.

In the case that the REIT is not in compliance with distribution requirements, it will be taxable as a regular corporation.

#### Capital gains

Eligible capital gains are not taxed at the level of the REIT.

#### Withholding tax

No withholding tax is levied on eligible income received by the REIT. As an otherwise taxable corporation, it would be subject to any other income tax withholding rules on income from prohibited transactions and other related income.

#### Other taxes

The REIT is subject to other taxes like municipal license taxes (similar to a gross receipt tax) and real and personal property taxes. For property tax purposes, the REIT may avail to other tax exemptions that might



be available under the Municipal Property Tax Act depending on the type of activity or industry in which the property is used.

### Accounting rules

There are no special accounting rules existing for a REIT. Generally, the REIT will follow US GAAP.

#### b. Transition regulations

Conversion into REIT status
No regulations

#### c. Registration duties

Registration duties
Stamp duties and register fees

The acquisition of real estate by the REIT will be subject to various kinds of stamp duties and registration and notary fees. These stamp duties and notary fees depend on the value of the property and vary from transaction to transaction.

## 4 Tax treatment at the shareholder's level

#### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Final withholding tax on distributions</li> <li>- Capital gains taxable</li> </ul>	<ul style="list-style-type: none"> <li>- Final withholding tax on distributions</li> <li>- Capital gains taxable</li> </ul>	Withholding tax of 10% on distributions

#### Corporate shareholder

Dividends are subject to a final withholding tax of 10%.

If the shareholder is a resident entity, gain from the sale of the shares in a REIT would be taxable at special rates if considered long-term capital gains (corporations will be taxed at 15% or 20% for transactions after June 30, 2014<sup>7</sup>, rather than at a maximum tax rate of 39% or 37.5% for taxable years beginning after December 31, 2018<sup>8</sup>).

#### Individual shareholder

<sup>7</sup> Act 77 of 2014 increased the special tax rate on long term capital gains applicable to corporations from 15% to 20% for transactions executed after June 30, 2014.

<sup>8</sup> On December 10, 2018 Act 257 of 2018 was enacted in which various amendments were introduced to the IRCNPR, including changes in the tax rate for taxable years commencing after December 31, 2018.

Dividends are subject to a final withholding tax of 10%.

Residents of Puerto Rico would be subject to taxation on capital gains from the sale of the shares in a REIT. The special rate is available if the gain is considered a long-term capital gain (individuals and trusts will be taxed at 10%, or 15% for transactions after June 30, 2014<sup>9</sup>, rather than at a maximum tax rate of 33%).

## Withholding tax

Taxable distributions are subject to withholding tax at the rate of 10%, as defined in Section 1082.02 of the IRCNPR (previously Section 1501 of the 1994 PRIRC). The trustees or directors to whom the management of the REIT has been delegated are responsible for deducting and withholding the required tax rate on the taxable distributions.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Withholding tax on distributions</li> <li>- Potentially withholding tax on capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- Withholding tax on distributions</li> <li>- Potentially withholding tax on capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- Withholding tax of 10% on distributions</li> <li>- Puerto Rico has not entered into any Tax Treaties</li> </ul>

### Corporate shareholder

Dividends will be subject to a 10% withholding tax.

Taxation of capital gain income in the case of a foreign shareholder will depend on the source of the gain and the residency status of the shareholder. If the shareholder is a non-resident entity, income tax withholding at source would be applicable only if the gain is considered from sources within Puerto Rico. Generally, the rule to determine the source of the gain in the case of personal property (shares) is the residence of the seller, with the exception of property that constitutes inventories, depreciable property, and intangible property, each of which is subject to specific rules.

### Individual shareholder

The foreign individual shareholder is subject to a 10% withholding tax.

Taxation of capital gain income in the case of a foreign shareholder will depend on the source of the gain and the residency status of the shareholder. The rules to determine the source are the same that we indicated above under corporate shareholder.

## Withholding tax

Taxable dividends, as defined in Section 1082.02 of the IRCNPR (previously Section 1501 of the 1994 PRIRC), are subject to withholding tax at the rate of 10% as provided by Sections 1062.08 and 1062.11 of the IRCNPR (previously Sections 1147 and 1150 of the 1994 PRIRC) related to income tax withholding at source on payments to non-resident persons. Treaty relief is not available.

<sup>9</sup> Act 77 of 2014 increased the special tax rate on long term capital gains applicable to individuals from 10% to 15% for transactions executed after June 30, 2014.

## 5 Treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Foreign REIT cannot qualify for REIT status. US REIT may qualify as a tax-exempt organisation	No specific tax privilege for corporate shareholders of foreign REIT	No specific tax privilege for individual shareholders of foreign REIT

### Foreign REIT

A foreign REIT will not qualify as a REIT in Puerto Rico since the entity must be created or organised under the laws of Puerto Rico. However, an entity organised or created under the laws of any state of the United States of America qualifying during the taxable year as a real estate investment trust under the United States Internal Revenue Code of 1986, as amended, may qualify as a tax-exempt organisation in Puerto Rico to the extent that certain investment requirements are met. This exemption may be extended to related persons of the US REIT. As a tax-exempt organisation, the foreign REIT must request a determination with the Secretary to approve the exemption <sup>10</sup>.

### Corporate shareholder

No specific tax privilege. Distributions from a foreign REIT to a Puerto Rican corporate shareholder will be subject to tax as any other income at the regular rates.

### Individual shareholder

No specific tax privilege. Distributions from a foreign REIT to a Puerto Rican individual shareholder will generally be subject to tax as any other income at the regular rates. ■

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major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
US-REIT	1960	Internal Revenue Code	Corporate type

The US Congress created the Real Estate Investment Trust (US-REIT) in 1960 to make large-scale, income-producing real estate investments accessible to smaller investors. Congress reasoned that the average investor should be able to invest in large-scale commercial properties just as if it were any other kind of investment, that is, through the purchase of equity. Similar to shareholders benefiting from the ownership of stocks in other corporations, the stockholders of a REIT also receive economic benefits from the production of income through commercial real estate ownership. REITs offer distinct advantages for investors. Firstly, greater diversification is achieved by investing in a portfolio of properties rather than just in a single property. Second, the managerial activities are performed by experienced real estate professionals. Also, in order not to be subject to a corporate-level tax REITs are required to distribute all of their taxable income to shareholders, who benefit from this stream of cash distributions.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
United States	192	124	EUR 1,040,060	64.98%

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Prologis	EUR 44,368	28.99%	2.65%	3.85%
Simon Property Group	EUR 43,347	0.90%	5.07%	3.76%
Public Storage	EUR 36,500	11.89%	3.36%	2.70%
Welltower Inc.	EUR 28,991	40.37%	4.27%	2.53%
Avalonbay Communities	EUR 24,872	25.40%	2.99%	2.16%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

The US REIT regime, which is governed by tax laws, has been modified on several occasions since its inception, most recently in the tax reform legislation known as the Tax Cuts and Jobs Act as signed into law on December 22, 2017. The essential rules for the US REIT can be found in section 856 and 857 of the Internal Revenue Code.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

Entities must file Form 1120-REIT with the Internal Revenue Service

To elect REIT status in the US, a company must file a special tax return (Form 1120-REIT) for the year in which the company wishes to become a REIT. There is no requirement to request prior approval or to submit a prior notification of regime election. Furthermore, the REIT must annually send letters of record to its shareholders requesting the details of the beneficial share ownership. Modest monetary penalties may be imposed on a REIT that fails to send these letters unless it is shown that failure is due to reasonable cause and not willful neglect.

### b. Legal form/minimum share capital

Legal form	Minimum share capital
Any legal US entity taxable as a domestic corporation	No

#### Legal form

A US REIT can have the form of any legal US entity (corporation, partnership, business trust, limited liability company, etc.), which is taxable as a domestic corporation. This status can be achieved by a 'check the box' election with the IRS. As a result, the entity would be treated as a corporation for tax purposes. However, the company cannot qualify for this option if it is a financial institution such as a bank or an insurance company.

Further requirements are that the REIT has to be managed by one or more trustees or directors and that the shares of a US REIT must be transferable.

A taxable REIT subsidiary is permitted to be located or organised abroad.

#### Minimum share capital

There is no minimum share capital requirement for a REIT.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- At least 100 shareholders</li> <li>- Five or fewer individuals or foundations may not hold more than 50% of the shares</li> <li>- No restriction on foreign shareholders</li> </ul>	No

## Shareholder requirements

Firstly, REIT shares must be transferable. Beginning with the REIT's second taxable year, the REIT is required to have a minimum of 100 shareholders. Also, no more than 50% of its shares may be held by five or fewer individuals or private foundations during the last half of the taxable year. A number of 'look through' rules can determine whether the latter criterion is met.

Various stock classifications (i.e. different classes of shares such as common stock and preferred stock) are allowed. However, all shareholders within the same class of stock must be treated equally. Otherwise, dividends from such classes of stock would no longer be considered eligible for the dividends paid deduction. Effective January 1, 2015, these so-called 'preferential dividend' rules for all 'publicly offered' REITs (REITs whose securities are registered with the SEC) have been repealed.

There is no restriction on foreign shareholders other than possible 'FIRPTA' consequences, under which foreign shareholders are treated as doing business in the US unless certain exceptions apply.

## Listing requirements

Listing is not mandatory to obtain REIT status. A private REIT is allowed.

### d. Asset level/activity test

#### Restrictions on activities/investments

- At least 75% of its assets must be real estate, government securities or cash
- 75% asset test and 75% and 95% income tests
- Cannot own more than 10% of another corporation's stock, other than in another REIT or a taxable REIT subsidiary (ownership of a 100% owned 'qualified REIT' subsidiary is ignored)
- No more than 5% of the value of its assets can be represented by securities of any one issuer, other than another REIT or a taxable REIT subsidiary (ownership of a 100% owned 'qualified REIT' subsidiary is ignored)
- Cannot own more than 20% of its assets in securities of one or more taxable REIT subsidiaries

75% of a REIT's assets must be comprised of real estate (including mortgages), government securities or cash items (including money market funds). In 2016, the IRS issued final regulations concerning the definition of real estate. In general, these regulations provide that land, inherently permanent structures and structural components are real estate for purposes of this 75% asset test rule. In addition, they provide a set of per se examples of assets that are considered real estate and they set forth a facts and circumstances test as well as a set of examples for assets that are not per se real property.

In particular, parking facilities; bridges; tunnels; roadbeds; railroad tracks; transmission lines; pipelines; and fences are considered inherently permanent structures that are real estate and wiring; plumbing systems; central heating and air conditioning systems; elevators or escalators; walls; floors; ceilings; permanent coverings of walls, floors and ceilings; windows; doors; insulation; chimneys; fire suppression systems, such as sprinkler systems and fire alarms; fire escapes; central refrigeration systems; integrated security systems; and humidity control systems would be considered structural components that are real property.

At least 75% of the gross income must be derived from real estate property rental or from interest on mortgages on real estate property. Furthermore, at least 95% of the gross income must come from a combination of real estate-related sources and passive sources, such as dividends and interest. No more than 5% of a REIT's income may come from non-qualifying sources.

At the end of each quarter, the REIT may not have securities of taxable REIT subsidiaries that represent more than 20% of the REIT's total asset value. Further restrictions apply. As part of renting real estate, a REIT may provide all kinds of tenant services customarily expected in the real estate rental business. Services are broad and extensive, e.g. providing utilities (sub-metering), security services, cleaning services in common areas, internet and cable TV, etc.

A US REIT may own, operate, manage and develop real estate for its own portfolio. If it develops real estate for third parties, the resulting income is disqualified and must fit under the 5% 'bad income' allowance. US REITs may develop real estate for third parties or trade real estate through their taxable REIT subsidiaries (TRS).

A REIT is allowed to invest in non-US real estate assets, which are considered real estate under the 75% asset test.

A REIT's ownership interests in a partnership are ignored. Instead, the REIT is considered an owner of the partnership's assets to the extent of the REIT's capital interest in the partnership. Also, the ownership of one REIT by another REIT is considered ownership of the real estate, i.e. a good asset. If the REIT is a shareholder of a company other than another REIT or a TRS, then the REIT cannot own more than 10% of the shares. Further, the REIT may have no more than 5% of its total assets represented by securities of any one issuer other than another REIT or a TRS.

#### e. Leverage

Leverage
No legal restrictions

There are no statutory or regulatory leverage limits for US REITs. However, the tax reform bill passed in December 2017 limits the deductibility of business interest to 30% of a taxpayer's tax version of EBITDA (EBIT starting in 2022). A taxpayer conducting a real estate trade or business may elect out of these limits, but then it must use longer cost recovery periods for its depreciable real estate assets.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
At least 90% of its taxable ordinary income	Not required to distribute	Annually

##### Operative income

US law requires the REIT to annually distribute at least 90% of its ordinary taxable income in the form of dividends. If a REIT declares a dividend in the last quarter of the year but pays it by the end of January, the dividend distribution is treated as if it had occurred the previous December. These 'relationship back-rules' apply if the REIT makes the actual distribution the following year. However, a 4% excise tax is imposed if the REIT fails to distribute at least 85% of its income within the year the income is generated.

##### Capital gains

US REITs are not required to distribute capital gains. Capital gains not distributed are subject to corporate income tax (lowered to 21% after 2017), but then the shareholders get an increased tax basis for their pro-rata share of the tax as well as a tax credit for the taxes paid by the REIT.



## g. Sanctions

### Penalties/loss of status rules

- Various penalties
- Possible loss of REIT status

Various penalties may occur. If insufficient income was distributed, the REIT might compensate with taxable deficiency dividends. If the REIT fails a de minimus amount of the asset test, it must fix the failure within six months of discovery. If the REIT fails the asset test by more than a de minimus amount, the REIT must pay corporate taxes on all income from non-qualified assets. In this case, it must also show reasonable cause for the failure. A USD 50,000 penalty is imposed for failures other than the asset test failures. A reasonable cause must also be proven in such cases. If there is no reasonable cause, then the REIT may technically lose its REIT status. Usually, however, the IRS will consider a closing agreement for some lesser amount.

If the REIT fails either the 75% or 95% gross income tests, it is subject to a penalty essentially equal to 100% of the amount by which it failed the respective tests, less allocable deductions.

After the loss of REIT status, the entity must observe a five-year waiting period before it can re-apply. The government may waive this penalty, depending on the reasonable cause.

A USD 50,000 penalty is imposed if the REIT shareholder limitations are disregarded.

## 3 Tax treatment at the level of the REIT

### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt to extent distributed	Tax-exempt to extent distributed	<ul style="list-style-type: none"> <li>- No refund of foreign withholding tax</li> <li>- It can use a foreign tax as a deduction</li> </ul>

### Current income

Distributed dividends are deducted in calculating a REIT's taxable income. Retained income is subject to ordinary corporate income tax, but tax depreciation deductions are made in calculating taxable income. Dividends from ordinary income are generally taxed as ordinary dividends less a 20% deduction under section 199A. The profits of a taxable subsidiary are subject to corporate income tax.

A REIT that acts as a dealer, as contrasted with an investor, is subject to a 100% excise tax on the profit from dealer sales. There is a safe harbour under which a REIT can be certain it will not be subject to the 100% excise tax if it complies with multiple objective tests.

Non-arm's length transactions conducted with a taxable REIT subsidiary (as well as non-arm's length transactions between a TRS and a REIT's tenants) are 100% taxable.

## Capital gains

Retained capital gains are subject to corporate income tax.

## Withholding tax

A US REIT is not entitled to obtain a refund for its foreign withholding tax credit. The credit applies to its foreign source income. However, it can use a foreign tax as a deduction.

## Other taxes

State income tax regimes virtually always follow the federal income tax rules.

## Accounting rules

US GAAP rules apply. A US REIT and its subsidiaries must file a consolidated financial statement.

### b. Transition regulations

#### Conversion into REIT status

- 'Built-in gains' are taxable
- Exemption is possible if assets are held for five years

By the end of the REIT's first taxable year, the REIT must distribute all the earnings and profits for years before it became a REIT. Also, the REIT must pay a corporate tax on 'built-in gains' (the value of its assets at the time of REIT conversion minus the assets' tax basis). The taxes may be excused only if the REIT does not sell or exchange those assets in a taxable transaction for five years. 'Like-kind' exchanges in which no built-in gain is recognized are permitted.

Many REITs use an UPREIT structure, which means 'Umbrella Partnership'. Under this structure, the REIT's sole asset is its interest in a partnership called the 'Operating Partnership' (OP). The REIT almost always has the general partner interest and typically owns more than half of the partnership interests. Property owners transfer either their assets or partnership interests to the OP in exchange for limited partnership interests (LP units). As with any other transfer to a partnership, the contribution of these assets or other partnership interests, is a tax-deferred transaction in which gain is not realised until the transferor's debt obligations shift or the transferor disposes of the partnership interest in a taxable transaction.

Usually after a year, the OP limited partners may exchange their OP units either to the REIT or the OP (depending on the particular transaction) and then the REIT or the OP, as the case may be, has the option of either transferring to the LP unitholder REIT stock on a one-for-one basis with each unit the LP unit owner exchanges or cash equal to the fair market value of such stock. The exchange of the LP units for REIT stock or cash is a taxable transaction.

### c. Registration duties

Registration duties
Transfer tax

Real estate acquisition is usually subject to transfer taxes in most states.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Income, capital gains and return of capital distributions are taxed at a rate of 21%	<ul style="list-style-type: none"> <li>- Capital gain dividends are taxed at the maximum 23.8% rate</li> <li>- Return of capital is tax-deferred</li> <li>- Individual shareholders receive a 20% deduction on ordinary REIT dividends</li> </ul>	N/A

#### Corporate shareholder

US corporations pay the same 21% rate on REIT capital gains and REIT ordinary income distributions. Corporate shareholders do not receive typical dividends received deduction with respect to REIT dividends. The return of capital distribution reduces the shareholder's tax basis in its shares of the REIT.

#### Individual shareholder

An individual US shareholder is subject to an income tax of up to 37%. An additional 3.8% surtax on investment income for taxpayers with adjusted gross income in excess of USD 200,000 (USD 250,000 for taxpayers who file a tax return as a married couple) also is applicable.

REIT ordinary dividends qualify for the lower 20% rate on 'qualified dividend income' (plus the 3.8% surtax, if applicable) only if they are paid out of income that has already been subject to corporate taxes, e.g. dividends attributable to distributions from a taxable REIT subsidiary. REIT dividends that are neither 'qualified dividend income' nor capital gain dividends are termed 'qualified REIT dividends' and also receive a 20% deduction. Therefore, the top marginal rate on dividends other than 'qualified dividends' is 33.4%.

Shareholders are taxed on capital gain distributions from assets the REIT held for at least one year at a 23.8% rate (including the 3.8% surtax). However, if the gain is attributable to the recapture of depreciation, the tax burden is 28.8%, including the surtax.

Return of capital distributions reduce the shareholder's tax basis and are therefore tax-deferred. To the extent a return of capital distribution exceeds tax basis, it is treated as a sale of the stock and the gain is taxable at the 23.8% maximum rate (including the 3.8% surtax). (The return of capital rules for a REIT are the same as for non-REIT corporations).

## Withholding tax

No withholding tax is levied on distributions to US shareholders.

### b. Foreign shareholders

Corporate shareholders	Individual shareholders	Withholding tax
<ul style="list-style-type: none"> <li>- 30% on income dividends</li> <li>- 21% on capital gain dividends</li> <li>- 10% on return of capital</li> </ul>	<ul style="list-style-type: none"> <li>- 30% on income dividends</li> <li>- 21% on capital gain dividends</li> <li>- 10% on return of capital</li> </ul>	Tax treaty relief available

### Corporate shareholders

Final withholding tax.

### Individual shareholders

Final withholding tax.

## Withholding tax

A withholding tax of 30% is levied on ordinary income dividends. This rate may be reduced by a double tax treaty. The US usually imposes a 15% tax on dividends paid by REITs in countries with which the US has a valid double tax treaty. The amount of the repayment of capital that is not subject to a withholding tax is taxed at a rate of 10%. The rate returns to 30% in most treaties for foreign shareholders who own more than 10% of a REIT. Non-US pension funds and certain governmental entities such as sovereign wealth funds might benefit from a tax exemption.

Capital gain dividends attributable to the sale of US real property are subject to the Foreign Investment in Real Property Tax Act (FIRPTA). According to FIRPTA, foreign shareholders are treated as if they were US taxpayers. Unless the shareholder owns 10% or less of a listed REIT, the capital gain dividends are subject to a 21% (plus branch profits tax) withholding tax. If the shareholder does own 10% or less of the REIT shares, then the treatment of capital gain dividends is similar to the treatment of ordinary dividends. Legislation enacted on December 18, 2015, exempts non-US pension plans from FIRPTA.

A return of capital distribution is subject to a 10% withholding tax. If a withholding certificate is obtained, 0%.

The sale of stock of a listed US real estate company (if the non-US shareholder owns 10% or less of the REIT) or of any domestically controlled REIT is not subject to FIRPTA or any US tax.

## 5 Treatment of foreign REITs and their domestic shareholders

Foreign REIT	Corporate shareholder	Individual shareholder
Generally, 30% withholding tax	<ul style="list-style-type: none"> <li>- Dividend distributions are taxed at a rate of 21%</li> <li>- Return of capital is tax-deferred</li> </ul>	<ul style="list-style-type: none"> <li>- Dividends are generally taxed at a maximum 23.8% rate if a foreign REIT is not a 'PFIC'</li> <li>- Return of capital is tax-deferred</li> </ul>

## Foreign REIT

Unless the foreign REIT elects to be taxed on a net basis or is actively operating rental property so that it is considered doing business in the US, there is a 30% withholding tax on gross rental income. Most non-US investors filing as a US business heavily leverage to reduce US taxable income.

## Corporate shareholder

US corporate shareholders generally are taxable at a 21% rate on distributions from foreign REITs. The return of capital distribution reduces the shareholder's tax basis in its shares of the REIT. Furthermore, there is no credit available to US corporate shareholders for US withholding taxes paid by the foreign REIT with respect to US source income. Generally, these dividends are not eligible for the dividends received deduction applicable to dividends from US corporations.

Finally, if the foreign REIT is considered a 'passive foreign investment company' (PFIC), which may be the case if the rental income of the foreign REIT is not attributable to the activities of its own employees, a US shareholder either is subject to tax and substantial interest charges upon receipt of a distribution from the PFIC (or disposition of the PFIC stock) or may elect instead to be taxed on the PFIC investment on a current basis using an earnings flow-through approach or a mark-to-market approach.

## Individual shareholder

An individual US shareholder is generally subject to an income tax at the maximum rate of 23.8% (including the 3.8% surtax noted above) on dividends distributed by a foreign REIT if the foreign REIT is both eligible for treaty benefits under a US tax treaty and is not a PFIC, as described above (although the maximum withholding tax rate with respect to REIT dividends under most treaties is 15%). Return of capital distributions reduce the shareholder's tax basis and are therefore tax-deferred. To the extent a return of capital distribution exceeds tax basis, it is treated as a sale of the stock and the gain is taxable at the 23.8% maximum rate (including the 3.8% surtax). The return of capital rules for a REIT are the same as for non-REIT corporations. Furthermore, there is no credit available to a US individual shareholder for US withholding taxes paid by the foreign REIT with respect to US source income.

If the foreign REIT is considered a PFIC, which may be the case if the rental income of the foreign REIT is not attributable to the activities of its own employees, an individual US shareholder either is subject to tax at rates of up to 40.8% (including the 3.8% surtax noted above) and substantial interest charges upon receipt of a distribution from the PFIC (or disposition of the PFIC stock) or may elect instead to be taxed on the PFIC investment on a current basis using an earnings flow-through approach or a mark-to-market approach. ■

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## ASIA - PACIFIC

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ASIA - PACIFIC

# Australia

UNIT TRUST

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction

	Enacted year	Citation	REIT type
<ul style="list-style-type: none"> <li>- Unit Trust</li> <li>- (esp. listed Property Trust)</li> <li>- Public Trading Trust</li> </ul>	1985	<ul style="list-style-type: none"> <li>- (Public) Unit Trust and Equity law</li> <li>- 'Trust Income', Division 6, ITAA 1936</li> <li>- 'Public Trading Trusts' Regime, Division 6C, ITAA 1936</li> <li>- 'Managed investment trust', Subdivision 12-H of Schedule 1 of the Tax Administration Act 1953</li> </ul>	Trust type

Fixed trusts have traditionally been the preferred vehicle for holding real estate investments in Australia. They are typically set up as a listed (public) or unlisted fixed unit trust (i.e. investors subscribe for units). Unit trusts are generally treated as transparent for Australian tax purposes. One of the key tax benefits arising for the investor from a trust structure is that distributions from the trust retain their tax attributes ('flow-through' entity), making an investment via a fixed trust generally comparable in most respects to a direct interest in the real estate. Unit trusts stapled to company structures are common in Australia.

Unit trusts are legally established under a Trust Deed pursuant to the general principles of the law of equity. Certain public unit trusts may also qualify as Managed Investment Schemes regulated under Corporations Law. Division 6 of the ITAA 1936 (Trust Income rules) regulates the taxation of income derived by a trust (but not an 'attribution managed investment trust' ('AMIT')), whilst Division 6C of the ITAA 1936 (Public Trading Trust Regime) assesses some trusts effectively as companies (depending on the type of activity undertaken by the trust) and Division 276 of the Income Tax Assessment Act 1997 ('ITAA 1997') regulates the taxation of AMITs. Distributions to non-Australian investors from a unit trust that is classified as 'managed investment trust' ('MIT') including the new AMIT are also taxed under the withholding tax rules contained in Subdivision 12-H of Schedule 1 of the Tax Administration Act 1953.

The application of certain tax law provisions for trusts (such as loss rules, scrip-for-scrip CGT rollover) varies depending upon whether a trust is classified as a 'fixed trust' or 'discretionary trust'. Subsequent to the Full Federal Court judgment in *Colonial First State Investments Ltd v Commissioner of Taxation*, there is uncertainty around the ability of a trust (and a unit trust in particular) that is not an AMIT to qualify as a fixed trust for Australian tax purposes without seeking confirmation from the Australian Taxation Office ('ATO'). Under current Australian tax law, where a trust does not meet the legislative definition of 'fixed trust', the Commissioner can exercise his own discretion to treat that trust as a fixed trust. Given the large number of tax provisions that rely on the concept of 'fixed trust' and the wide-ranging impacts for business, it has been long-standing industry practice (that applied before this decision) for most unit trusts (including property trusts) to be treated as if they qualify as a fixed trust (without seeking written confirmation from the ATO). This judgment highlights the weaknesses in the existing law that have been inherent since the concept of 'fixed trust' was first introduced and the need for trust law reform.

There have been two key developments in this area. Firstly, on September 13, 2017, the Commissioner of Taxation released Practical Compliance Guideline PCG 2016/16. PCG 2016/16 broadly seeks to provide clarity and outlines the factors the Commissioner will consider when deciding whether to exercise the discretion to treat an interest in the income or capital of a trust as being a fixed entitlement. The PCG includes a proposed safe harbour compliance approach that also allows certain trusts to allow themselves to be treated as though the Commissioner had exercised the discretion to treat a trust as a fixed trust. Secondly, on May 5, 2016, the Federal Government enacted the Tax Laws Amendment (New Tax System for Managed Investment Trusts) Act 2016 ('AMIT Amendment') which introduced the long-anticipated AMIT regime and other key changes to the taxation of trusts (discussed below), including but not limited to providing fixed trust treatment subject to certain conditions being satisfied.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Australia	44	11	EUR 86,776	5.91%

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Goodman Group	EUR 16,800	55.20%	2.00%	1.44%
Scentre Group	EUR 12,582	-10.50%	5.77%	1.05%
Dexus Property Group	EUR 8,731	36.04%	3.87%	0.76%
Mirvac Group	EUR 7,544	46.66%	3.71%	0.66%
GPT Group	EUR 7,340	26.24%	4.22%	0.64%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

- No special legal or regulatory requirements
- Certain requirements to benefit from withholding tax concessions and capital account election measures under the MIT rules

A trust is established pursuant to a trust deed, which sets out the terms of the trust.

No special legal or regulatory requirements need to be satisfied in order for a property trust to be established. Property trusts whose units are offered to the public may be subject to regulatory requirements such as the Managed Investment Scheme rules under the Australian Corporations Law, which includes that the trust must be managed by a corporate trustee/responsible entity/fund manager. However, these requirements do not impact on the tax treatment of the trust as a 'flow-through' entity.

## MIT requirement

Certain withholding tax concessions apply to distributions to non-Australian investors in an MIT (refer 4.2).

Under the MIT definition (applicable from July 1, 2010), the broad requirements to be satisfied for a trust to qualify as an MIT, include:

- It must have a relevant connection to Australia (i.e. Australian managed and controlled or have an Australian resident trustee).
- It must be a Managed Investment Scheme ('MIS') within the meaning of the Corporations Act 2001 that is either:
  - a registered MIS under the Corporations Act 2001 ('registered MIS'); or
  - an unregistered MIS that satisfies a wholesale test ('wholesale trust') as well as certain licensing requirements.
- It carries out a substantial proportion of its investment management activities in Australia in respect of its Australian assets (refer below).
- It is not a 'trading trust' (i.e. the trust must not carry on, or control, a trading business).
- It satisfies the relevant 'widely-held' requirement (refer below).
- It is not closely held (that is, a 75% or greater interest is not held by 20 or fewer persons (retail trust) and ten or fewer person (wholesale trust), excluding interests held by specified 'eligible widely-held investors'. Also, a foreign individual cannot hold an interest of 10% or more).

At present, there is little guidance on what 'substantial proportion' of investment activities in Australia means, however at a minimum, we would expect an Australian investment manager to be actively engaged in the management of the Australian assets such as identification and review of investments, due diligence as well as responsibility for undertaking the analysis for investment decisions being considered.

The widely-held requirement test is complex. The test will be easier to satisfy where ownership interests (even up to 100%) are held by 'eligible widely-held investors', which include:

- domestic and foreign life insurance companies;
- complying superannuation funds with at least 50 members;
- foreign superannuation funds (indefinitely continuing provident, benefit, retirement, or superannuation funds that are established outside Australia, managed and controlled outside Australia and have a majority of non-Australian resident members) with at least 50 members;
- pooled superannuation trusts that have at least one member which is a complying super fund that has at least 50 members;
- other managed investment trusts;
- foreign collective investment vehicles which have at least 50 members and are recognised under a foreign law as being used for collective investment where member contributions are pooled together and members do not have the day-to-day control over the operation of the entity
- certain tax-exempt foreign government pension funds (or their wholly-owned subsidiaries);
- certain sovereign wealth funds;
- entity wholly-owned by an Australian government agency;
- an entity of a kind listed in specified regulations.

The structure by which otherwise eligible investors hold an interest in an Australian trust will influence whether these widely held requirements can be satisfied.

As part of the AMIT Amendments, the Government has widened the list of ‘widely-held’ investors for the MIT regime to make it easier to satisfy the widely-held requirement test by including an ability to look through:

- wholly-owned companies in a broad range of circumstances; and
- allow tracing through a Collective Investment Vehicle and a limited partnership in which at least 95% of the interests are held by other qualifying investors and the remaining interests are held by a general partner habitually exercising management powers.

Furthermore, the AMIT regime has also formally separated MITs into one of three classes. Each of these classes is required to fulfil the MIT requirements above noting the following exceptions:

- Capital election MIT – will be able to satisfy each the above requirements with the exception of not meeting the ‘substantial proportion of investment management activities carried out in Australia with respect to the trust’s Australian assets’ requirement. Accordingly, a capital election MIT will be unable to access the MIT withholding tax regime or attribution rules. A Capital election MIT will be able to make an election to treat certain assets as being held on capital account.
- Withholding MIT – The same as a capital election MIT however, this MIT will also meet the requirements to have a substantial proportion of investment management activities carried out in Australia for the trust’s Australian assets and can access the concessionary MIT withholding tax rates. Further, a withholding MIT will only be subject to the attribution rules where it meets the AMIT requirements and makes an election to apply the rules.
- AMIT – In addition to the above, AMITs member must have a ‘clearly defined interests’ and make an irrevocable election to be an AMIT. Should these provisions be satisfied, an AMIT will be able to access the attribution regime as discussed below.

The ‘Treasury Laws Amendment (Making Sure Foreign Investors Pay Their Fair Share of Tax in Australia and Other Measures) Act 2019 (Act No.34 2019)’ (‘the Act’) was enacted on 5 April 2019 which introduces legislation to limit the availability of the MIT 15% withholding tax concession. Broadly, under the new legislation, the 15% withholding tax rate will not apply to ‘non-concessional MIT income’. Non-concessional MIT income is income from certain cross staple arrangements, income from underlying trading activities, income from agricultural land or income from certain residential housing investments. Under the new measures, non-concessional MIT income would be subject to withholding at the top corporate tax rate (currently 30%). However, there is transitional relief that is available for certain existing arrangements. This is discussed in more detail below.

## b. Legal form/minimum initial capital

Legal form	Minimum initial capital
Unit trust	USD 1

### Legal form

A unit trust generally qualifies for the ‘flow-through’ tax treatment and the ‘flow-through’ treatment is not limited to resident trusts.

A non-resident entity will be treated as transparent for tax purposes provided it can be properly characterised as a trust for Australian tax purposes.

However, a trust which is treated as a public unit trust (e.g. listed or at least 50 investors or 20%-owned by Australian superannuation funds<sup>1</sup> and certain exempt entities) does not qualify for ‘flow-through’ treatment if it is carrying on ineligible trading activities.

The term ‘property trust’ used with respect to Australia in the remainder of this report is a reference to such a fixed unit trust unless otherwise specified.

### Minimum initial capital

Apart from the requirement that there must be at least nominal corpus of the trust estate, there is no minimum initial capital required.

### c. Unit holder requirements/listing requirements

Unit holder requirements	Listing mandatory
No requirements	No

#### Unit holder requirements

No requirements exist with respect to the profile of the investor.

#### Listing requirements

Listing is not mandatory in Australia to obtain ‘flow-through’ status. However, large property trusts (known as ‘listed managed investment trusts’ or ‘A-REITs’) are typically listed in Australia for commercial purposes. It is also easier to qualify as a MIT if the trust is listed on Australian Stock Exchange.

A number of requirements must be met in order to be listed on the Australian stock exchange, including among others minimum net tangible assets or profit requirements and minimum unit-holders numbers and parcel value requirements.

### d. Asset levels/activity test

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- Public unit trusts and MITs investing in land must do so for the purpose, or primarily for the purpose, of deriving rent (eligible investment business)</li> <li>- Public unit trusts that carry on a trading business (i.e. a business that does not wholly consist of eligible investment business) are not accorded ‘flow-through’ treatment and unit trusts that carry on a trading business will not qualify as a MIT</li> <li>- May invest in a single property</li> </ul>

There are no restrictions on the type of activities that can be undertaken by a property trust, unless the trust qualifies as a public unit trust (broadly, unit trusts that are listed, have at least 50 unitholders or 20% of the units are held by and certain exempt entities) or wishes to qualify as an MIT. Unit trusts, other

<sup>1</sup> The Government has proposed to amend the public trading trust rules such that 20% or more ownership of a unit trust by Australian superannuation funds should not result in it being treated as a public unit trust.

than public unit trusts and MITs, can engage in trading activities, for example managing and developing real estate, without losing the benefits of ‘flow-through’ treatment.

Public unit trusts and MITs must only carry on an ‘eligible investment business’ in order to be eligible for ‘flow-through’ treatment. ‘Eligible investment business’ covers investing in ‘land’ for the purpose (or primarily for the purpose) of deriving rent (except for profit-based rentals derived from land), and/or investing or trading in various financial instruments including units in unit trusts, shares in companies (including foreign hybrid companies), loans and derivatives. The definition of ‘land’ has included fixtures on the land and certain moveable property (e.g., chattels) customarily supplied, being a property that is incidental and relevant to the renting of the land and ancillary to the ownership and utilisation of the land. Ineligible activities are regarded as trading activities.

A safe-harbour rule operates to broadly allow a trust to derive up to 25% of its income from investments in land (excluding capital gains from asset realisation) in the form of trading income (i.e. not rent) so long as it is incidental and relevant to the ‘eligible investment business’ being the leasing of land. Further, none of the rental income should be excluded rent, i.e. rent intended to transfer all or substantially all of the profits of another person to the lessor.

Where a trust does not meet this safe-harbour test, it can assess whether it is investing in land for the purpose, or primarily for the purpose of deriving rent under the existing law. Furthermore, a 2% safe-harbour allowance for non-eligible investment business’ income (at the whole of trust level) reduces the scope for inadvertent minor breaches of the ‘eligible investment business’. The trustee of a unit trust is taken not to carry on a trading business in a year if no more than 2% of the gross revenue of the unit trust is income other than from ‘eligible investment business’.

In summary, provided the public unit trust, MIT or AMIT carries on primarily (i.e. predominantly) eligible passive land investment activities, and non-eligible activities are incidental and relatively insignificant, the public unit trust should retain the ‘flow-through’ treatment for that income year and/or the trust will retain MIT status.

If the public unit trust carries on a trading business, it will be taxable as if it was a company (at the company rate of 30%) and its unitholders were shareholders. Alternatively, the trust will lose MIT status.

A public unit trust may not control or have the ability to control directly or indirectly, an entity that carries out ineligible trading activities. As a consequence, it is common for Australian property trusts to form part of a stapled security with a passive trust undertaking a range of activities relating to passive property holdings (i.e. management, redevelopment, funds management etc.) and a stapled company or trading trust actively participating in property development activities. This effectively allows the management function to be ‘internalised’.

A property trust may invest in a single real property asset.

A property trust can hold property investments offshore. Property trusts can hold investment properties indirectly through SPVs. However, the key benefits arising for an investor from a trust structure (i.e. where the benefits of direct ownership are replicated) may be lost where the interposed SPV does not qualify for look-through tax treatment.

## e. Leverage

### Leverage

Unlimited, but the extent to which interest is deductible is limited by the general thin capitalisation rules

There are no specific gearing limits for unit trust structures under Australian tax law. The general thin capitalisation rules may apply, however, to effectively impose a gearing limit where the property trust is controlled by non-resident unitholders and/or if the property trust controls a foreign entity. Exemptions from the thin capitalisation rules apply where total debt deductions (including associates' deductions) are AUD 2 million or less, or where an Australian outbound investor that is not foreign controlled has average Australian assets (including its associates' assets) that represent 90% or more of its average total assets (including its associates' assets).

Under the thin capitalisation rules, the safe harbour test broadly provides for a maximum gearing (both related and third party) of 60% of the gross assets based on the accounting balance sheet. The thin capitalisation rules also contain an arm's length debt test. This essentially looks at the amount that an independent commercial lending institution would reasonably be expected to lend as well as the amount of debt that the entity would reasonably be expected to have attributable to Australian business.

Subject to the thin capitalisation rules, a tax deduction should be available for interest expense incurred in connection with loans used to acquire the income yielding property. Breaches of thin capitalisation rules will result in a proportion of interest deductions being denied.

The Act also introduced new legislation to prevent foreign investors from using multiple layers of flow-through entities (i.e. trusts and partnerships) each issuing debt against the same underlying asset. The new legislation means that investors with an ownership of 10% or more will need to consider the debt funding in downstream entities in considering the investors' thin capitalisation position. These thin capitalisation measures apply to income years commencing on or after July 1, 2018, and a transitional period is not available.

Australia has also implemented a version of the anti-hybrid rules developed by the OECD under Action Item 2 of the Base Erosion and Profit Shifting Action Plan, which goes further than the OECD's proposal.

The purpose of the anti-hybrid rules is to prevent multinational companies from gaining an unfair competitive advantage by avoiding income tax or obtaining double tax benefits through hybrid mismatch arrangements. Broadly, hybrid mismatch arrangements arise where an entity enters into a scheme to exploit differences in the tax treatment of an entity or instrument under the laws of at least two tax jurisdictions to defer or reduce income tax. Australia's version of the OECD hybrid mismatch rules received royal assent on August 24, 2018, and applies to income years beginning on or after January 1, 2019 with the exception of imported mismatch rules which only apply in respect of 'structured arrangement' for income years commencing on or after January 1, 2019 and the complete imported mismatch rules applying from January 1, 2020.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
Typical distribution of 100% of trust's income as defined in the trust's constitution	To the extent included in the trust's income, any capital gains realised on disposal of property, including interests held in other sub-trusts or other entities	Annually or semi-annually

There are no prescribed minimum distribution rules. However, in order to ensure that the trustee is not subject to tax on the property trust's taxable income at the top marginal tax rate (currently 45% + 2% Medicare levy (if applicable)), the unitholders must be 'presently entitled' to all of the trust's trust law income at year-end. Property trusts therefore typically distribute their trust income (including tax-deferred amounts) on at least an annual basis, and listed trusts distribute generally on a quarterly or six-monthly basis.

Under the new AMIT regime, the ‘present entitlement’ system of trust taxation is replaced by an ‘attribution’ system under which the trustee allocates all of the taxable income of the trust to the unitholders on a ‘fair and reasonable basis’. The trustee will not be subject to tax on the trust’s taxable income (rather, the unitholders will be assessed on the taxable income of the trust that is allocated by the trustee) and clearly defined rules to carry forward prior year under/over amounts. This attribution regime is only available for eligible MITs which have made an irrevocable election to apply the attribution rules.

#### g. Sanctions/integrity provisions

##### Penalties/loss of status rules

- As outlined above, Public unit trusts that carry on a trading business (i.e. a business that does not wholly consist of eligible investment business) are taxed as if they are a company and are not accorded ‘flow-through’ treatment
- In addition, MITs need to satisfy an arm’s length income rule; to the extent to which the income derived exceeds an arm’s length amount, the trustee will be subject to 30% on the income derived in excess of an arm’s length amount

A ‘non-arm’s length income rule’ has been introduced which will apply to all MITs (i.e. MITs and AMITs). Where an MIT is determined by the Commissioner to be in receipt of ‘non-arm’s length income’ (e.g. interest), the trustee will be liable to taxation at 30% on the excess income above the arm’s length amount. That is, the analysis is only of the income received by an MIT rather than expenses incurred. These rules apply to any arrangements entered on or after July 1, 2016 and in respect of existing arrangements from July 1, 2018.

Certain exceptions and a safe-harbour exist to protect against this rule.

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Not taxable in the hands of the trustee provided the unitholders are presently entitled to the trust’s income at the end of the income year, otherwise trustee taxed at the highest marginal rate	<ul style="list-style-type: none"> <li>- Tax treatment of capital gains similar to that of ordinary income</li> <li>- 50% CGT discount may be available for Australian resident unit holder; however, the 50% discount will not apply to non-resident unitholders on capital gains accrued after May 08, 2012</li> </ul>	N/A

#### Current income and capital gains

Provided the unitholders are presently entitled to the property trust’s trust income (as calculated under the trust deed) at year-end, the trustee is not liable to tax on the trust’s taxable income, including capital gains. Income derived by the property trust will generally retain its character in the hands of the unitholders as it is the unitholders themselves that are subject to tax according to their own specific circumstances



If there is a portion of property trust's trust income to which unitholders are not presently entitled at year-end, then the trustee is subject to tax on the same proportion of the trust's taxable income at the top marginal tax rate (currently 47% + 2% Medicare levy (if applicable)). Where the taxable income includes capital gains, a resident trustee may be able to apply the 50% CGT (capital gains tax) discount. The 50% CGT discount is not available for non-residents

As outlined above, under the new 'attribution' system the taxable income of the AMIT will not be taxable in the hands of the trustee provided that the trustee has allocated all of the taxable income of the trust to the unitholders on a 'fair and reasonable basis'. More detailed comments on the tax treatment of an AMIT have been provided below.

## Tax losses

Tax losses are quarantined in the trust and cannot be distributed to unitholders. They can be carried forward to offset against future income and capital gains subject to satisfying the trust loss recoupment tests, the most important of which is a greater than 50% continuity of ownership test. A trust that does not satisfy the requisite trust loss tests cannot offset those income losses in future years. There is no loss carry-back. There is a same business test, but this is only available to trusts that have been listed at all times from the beginning of the loss year until the end of the year of recoupment.

Capital losses can only be offset against capital gains derived by the trust. The capital losses of trusts are not subject to the tax loss rules and can be utilised post an acquisition, in most cases.

## Withholding tax

An Australian resident property trust is generally not subject to any domestic withholding tax on income earned in Australia.

Tax offsets for foreign withholding tax deducted from foreign income derived by the property trust will attach to distributions of foreign income made by the trust to unitholders. The relevant portion of the foreign tax offsets will be available for offset against tax on foreign income of the property trust if the trustee is subject to tax on that amount as discussed above.

The property trust may have certain withholding tax and other tax obligations in respect of the net income distributed to unitholders. These are discussed in section 4 below.

## Accounting

Australian LPTs are required to prepare accounts under IFRS.

## Tax treatment of an AMIT

As noted above, the attribution regime replaces the existing Division 6 'present entitlement' provisions, and each member is allocated a 'determined member component' of assessable, exempt and, non-assessable, non-exempt characters. The trustee will attribute those amounts to members on a fair and reasonable basis, consistent with the trust documents, as if the members had derived, received or made the amounts in their own right.

Other features of the tax treatment of an AMIT include:

- **A formal introduction of an 'unders and overs' system**  
This system allows a trustee to carry forward errors in calculations of taxable income to the year that the errors are discovered. Discovered unders and overs are included in the trust's income components in the discovery year.

- **Fixed review periods**  
Income tax calculations for AMITs are subject to a four-year discovery period after which they are no longer subject to ATO review. No time limits are applicable to other trusts
- **Cost base adjustments**  
Members of AMITs are now able to make an upward as well as downward cost base adjustment in the units they hold (for both capital and revenue account holders).
- **Tax-deferred amounts not assessable**  
Under the previous law, uncertainty existed in connection to whether distributions of 'tax-deferred' income to certain investors could be considered to be ordinary income and taxable in the hands of the beneficiary. For AMITs, an amount of 'tax-deferred' income received by a member of an AMIT will be treated as non-assessable.
- **Fixed trust treatment**  
As noted above, AMITs are now deemed to be fixed trusts for tax purposes.
- **Units capable of being treated as debt interests**  
Certain debt-like interest in an AMIT is capable of being treated as a debt interest and distributions in relation to these instruments will be deductible to the AMIT and assessable to the members as interest for the purpose of interest withholding tax.
- **Multiple classes of units**  
Where an AMIT has multiple classes of members, it will be able to make an irrevocable election to treat each class of units as separate AMIT classes. These AMITs would then be able to issue different classes of units to investors seeking exposure to different categories of assets.

## Transition regulations

### Conversion into REIT status

N/A

## b. Registration duties

### Registration duties

No duty on capital contributions

There is no duty on capital contributions.

## 4 Tax treatment at the unit holder's level

### a. Domestic unit holder

Corporate unit holder	Individual unit holder	Withholding tax
<ul style="list-style-type: none"> <li>- 30% tax on the share of the trust's worldwide taxable income, including capital gains</li> <li>- Capital gains on disposal of units taxed at 30% with no CGT discount available</li> </ul>	<ul style="list-style-type: none"> <li>- Tax at rates of up to 47% (including Medicare levy) on the share of the trust's worldwide taxable income</li> <li>- 50% CGT discount may be available to resident individuals on capital gains distributed and on disposal of units</li> </ul>	<ul style="list-style-type: none"> <li>- There is no final withholding tax imposed</li> <li>- The trustee pays tax on behalf of a foreign resident beneficiary in certain circumstances</li> <li>- Withholding at 47% (inclusive of the Medicare levy) is required where an Australian tax file or business number is not quoted</li> </ul>

#### Corporate unit holder

A resident corporate unit-holder is subject to tax on its share of the property trust's worldwide taxable income, including capital gains, at the current corporate tax rate of 30%.

'Tax-deferred' distributions, being distributions in excess of the property trust's taxable income (e.g. an amount representing plant and equipment depreciation), are generally only taxable to the extent that the amount exceeds the cost base of the unit holder's investment. The unit holder's CGT cost base is otherwise reduced by the tax-deferred amount, which effectively defers taxation until such time as the units are disposed of. For certain investors, such as those that hold their investment on revenue account, these tax-deferred distributions may be assessable on receipt.

Capital/revenue gains realised on the disposal of units in the property trust are subject to tax at the current corporate tax rate of 30%.

#### Individual unit holder

An individual unit holder is subject to tax at the prevailing tax rate of up to 47% (inclusive of the medicare levy) on its share of the property trust's worldwide taxable income. However, to the extent that the trust's taxable income is made up of capital gains, the domestic unitholder may be entitled to a 50% CGT discount.

'Tax-deferred' distributions, being distributions in excess of the property trust's taxable income (e.g. an amount representing plant and equipment depreciation), are generally only taxable to the extent that the amount exceeds the cost base of the unit holder's investment. The unit holder's CGT cost base is otherwise reduced by the tax-deferred amount, which effectively defers taxation (in the form of a higher capital gain) until such time as the units are disposed of.

Capital gains realised on the disposal of units in the property trust may also be eligible for the 50% CGT discount in the hands of the domestic unit holder. No discount is available for revenue gains. The trustee may pay tax on behalf of a beneficiary in certain limited circumstances.

#### Withholding tax

Withholding from property trust distributions or from a present entitlement to trust income is required at

the rate of 47% (inclusive of the medicare levy) where an Australian tax file number (TFN) or Australian business number (ABN) or other exception is not quoted to the property trust. Unitholders are entitled to a tax credit for the amount withheld.

## b. Foreign unit holder

	Corporate unit holder	Individual unit holder	Withholding tax
Trust is not an MIT	<ul style="list-style-type: none"> <li>- Non-resident unitholders are subject to Australian tax at corporate tax rate of currently 30% on their share of the trust's taxable income that is attributable to sources within Australia</li> <li>- Capital gains on non real property are tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- Non-resident individual unitholders are subject to Australian tax on a progressive scale, starting at 32.5% on their share of the trust's taxable income that is attributable to sources within Australia</li> <li>- Capital gains on non-real property are tax-exempt and taxable capital gains may be eligible for a 50% discount to the extent that the capital gain is accrued before May 8, 2012</li> </ul>	Dividend and interest paid to non-resident unitholders are subject to a final withholding tax in accordance with domestic rules/treaty rules, on dividends or interest

Trust is an MIT (including AMIT)	<ul style="list-style-type: none"> <li>- Capital gains on non-real property are tax-exempt</li> <li>- Dividend and interest distributed to non-resident unitholders are subject to a final withholding tax in accordance with domestic rules/treaty rules, on dividends or interest</li> <li>- For other types of Australian source income, the rate of withholding tax depends on the country of residence of the foreign investor</li> <li>- For foreign investors resident in a country with which Australia has an effective exchange of information (EOI) on tax matters<sup>2</sup> the income is subject to a final withholding tax for distributions of 15% and a 10% withholding for distributions from Green Building MITs (Withholding MITs and AMITs only)</li> <li>- For foreign investors in a country with which Australia does not have an effective EOI, the income is subject to a final withholding tax at the rate of 30%</li> </ul>
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## General position<sup>2</sup>

In general, for non-resident beneficiaries that are presently entitled to the property trust's trust income (or have been allocated a direct member component by an AMIT), the trustee will be required to deduct tax on Australian-sourced income distributed other than income that is subject to a final withholding tax

<sup>2</sup> The countries with which Australia has an effective EOI on tax matters that qualify for the lower MIT withholding rate are: Anguilla, Antigua and Barbuda, Aruba, Argentina, Bahamas, Belgium, Belize, Bermuda, British Virgin Islands, Canada, Cayman Islands, China, Cook Islands, Czech Republic, Denmark, Fiji, Finland, France, Germany, Gibraltar, Guernsey, Hungary, India, Indonesia, Ireland, Isle of Man, Italy, Japan, Jersey, Kiribati, Republic of Korea, Macau, Malaysia, Malta, Mauritius, Mexico, Monaco, Netherlands, Netherlands Antilles, New Zealand, Norway, Papua New Guinea, Poland, Romania, Russia, San Marino, Singapore, Slovakia, South Africa, Spain, Sri Lanka, St Kitts & Nevis, St Vincent & the Grenadines, Sweden, Taipei, Thailand, Turks and Caicos Islands, United Kingdom, United States of America, Vietnam, Albania, Andorra, Austria, Azerbaijan, Bahrain, Barbados, Brazil, Bulgaria, Brunei, Cameroon, Chile, Colombia, Costa Rica, Croatia, Cyprus, Dominica, Estonia, Faroe Islands, Georgia, Ghana, Greece, Greenland, Grenada, Guatemala, Iceland, Israel, Kazakhstan, Kenya, Latvia, Liberia, Liechtenstein, Lithuania, Luxembourg, Marshall Islands, Moldova, Montserrat, Nigeria, Niue, Philippines, Portugal, Samoa, Saudi Arabia, Senegal, Seychelles, Sint Maarten, Slovenia, St Lucia, Switzerland, Tunisia, Turkey, Uganda, Ukraine, Uruguay and Vanuatu. This list is current as at 1 January 2019.

(e.g. interest/dividend and MIT withholding tax, as withholding tax is a final tax). This tax deducted is not a final tax.

## Non-MITs

Tax is deducted in accordance with the type of unitholder – companies at 30%, individuals on a progressive scale starting at 32.5%, and non-resident trustee beneficiaries at 45%. The unit holder is required to lodge a tax return in respect of these trust distributions (for corporate and individual unitholders but not non-resident beneficiaries that are trusts) and can claim a deduction for certain costs incurred in deriving this income. The tax deducted by the trustee may be claimed as a tax credit with any excess tax deducted by the trustee refunded to the unitholder.

## Managed Investment Trusts

A concessional withholding tax regime applies to distributions made by withholding MITs and AMITs of taxable income attributable to Australian sources to all types of non-residents including trustees. The new regime replaces the non-final 30% withholding regime that formerly applied.

For Australian source income, the rate of withholding tax on distributions by a withholding MIT and AMIT depends on the country in which the foreign investor is resident:

- For foreign investors residing in a country with which Australia has an effective exchange of information (EOI) on tax matters, the concessional MIT income is subject to a final withholding tax of 15% for distributions from July 1, 2012 and 10% for distributions from Green Building MITs. Distributions of non-concessional MIT income is subject to a final withholding tax of 30%.
- For foreign investors in a country with which Australia does not have an effective EOI, the income is subject to a final withholding tax at the rate of 30%.
- Where a foreign investor is a trust that is resident in a country with which Australia has an effective EOI and has a beneficiary resident in a country with which Australia does not have an effective EOI, except in the case where the foreign investor is a beneficiary in an AMIT, the beneficiary is required to top up the 15% withholding tax deducted on the distribution to the Trust to reflect the 30% withholding tax rate applicable for distributions to beneficiaries resident in a non-EOI country.

For capital account MITs, no concessional MIT withholding rates will apply but rather distributions to non-residents will be subject to the same withholding rates as if it were a non-MIT.

In addition, different rates of withholding apply to distributions by a withholding MIT and AMIT that qualifies as a Clean Building MIT. This is an MIT that only holds 'clean buildings' that commenced construction on or after July 1, 2012. For such Clean Building MITs, the rate of withholding on distributions to foreign investors that are resident in countries with which Australia has an effective EOI is 10% rather than 15%.

Non-concessional MIT income includes income from underlying trading businesses, income from cross-staple arrangements in certain circumstances as well as income from certain residential land investments and investments in agricultural land. There is transitional relief that is available for certain existing arrangements. Refer below for our more detailed comments in relation to the proposed changes.

For foreign investors that are trusts (other than non-Australian Pension Funds that are constituted by way of a trust), higher rates of tax may be applicable if MIT distributions derived by such trusts are not subsequently distributed to their beneficiaries.

Dividend, interest and royalty income will generally continue to be excluded from MIT withholding tax and are subject to the specific withholding tax rules. Capital gains on assets other than 'taxable Australian

property’ will also continue to be generally excluded (discussed below).

Dividend, interest and royalty income will generally continue to be excluded from MIT withholding tax and are subject to the specific withholding tax rules. Capital gains on assets other than ‘taxable Australian property’ will also continue to be generally excluded (discussed below).

### Tax-deferred distribution

‘Tax-deferred’ distributions, being distributions in excess of the property trust’s taxable income (e.g. an amount representing plant and equipment depreciation), are generally only taxable to the extent that the amount exceeds the cost base of the unit holder’s investment. The unit holder’s CGT cost base is otherwise reduced by the tax-deferred amount, which effectively defers any taxation (in the form of a higher capital gain) until such time as the units are disposed of. For certain investors, such as those that hold their investment on revenue account, these tax-deferred distributions may be assessable on receipt.

As noted above, an AMIT has additional flexibility with the ability to adjust its cost base upwards. This situation is likely to arise where a member has been attributed and taxed on a ‘direct member component’ that is in excess of the amount actually being paid.

### Distributions of capital gains

Trustees of property trusts that distribute capital gains on assets that are not ‘taxable Australian property’ are not required to withhold tax from that amount as foreign resident beneficiaries will not be taxable on the gains distributed. Gains from investments held by the trust in other trusts are eligible for the exemption provided at least 50% of the market value of CGT assets of the other trust (or trusts in which the other trust has an interest), are not ‘taxable Australian property’ at the relevant CGT event time. Taxable Australian property includes real property held directly or indirectly that is situated in Australia; therefore it usually follows that capital gains distributions from Australian property trusts remain taxable.

Non-residents will only be taxable on capital gains realised on the disposal of units in an Australian resident property trust if the unitholder held at least 10% of the units in the trust, and more than 50% of the market value of the assets of the trust comprises Australian real property or interests in other entities whose assets are principally Australian real property.

### Capital election requirement

Certain MITs can elect for capital account treatment for certain of its investments. Broadly, under the new deemed capital rules, Australian MITs (this definition is broadly the same as the MIT definition for MIT withholding tax purposes with a few exceptions) will be entitled to make an irrevocable election to apply the CGT treatment to eligible assets disposals. If the trust makes a valid election, certain assets (broadly, land, shares in companies and units in unit trusts) are deemed to be held on capital account and therefore disposal of these assets may be eligible for the capital gains tax discount and exemption for non-residents (where assets are ‘non-taxable Australian property’). If no election is made, the assets will be deemed to be held on revenue account (with the exception of real estate which will be taxed according to the ordinary capital/revenue distinction). The new concessions will also apply to unit trusts 100% owned and controlled by MITs if the trust is eligible for ‘flow-through’ treatment (i.e. carry on only an ‘eligible investment business’).

### Other Withholding Taxes

Dividend and interest income paid to non-resident unitholders is subject to a final withholding tax in accordance with domestic rules/treaty rules. To the extent that the income has been subject to final Australian withholding tax or would have been subject to withholding tax had an exemption not applied, no further tax is levied.

Withholding from other property trust distributions (or from a present entitlement to other trust income) is required at the rate of 47% where an Australian tax file number (TFN) or Australian business number (ABN) or other exception is not quoted to the fund. Unitholders are entitled to a tax credit for the amount withheld. Amounts that have tax withheld under the ‘managed investment trust’ withholding tax provisions discussed above are exempted from this requirement.

Additionally, a foreign resident capital gains withholding (FRCGW) of 12.5% will apply to vendors disposing of certain taxable property (including units in trusts) under contracts entered into from July 1, 2016, that have a contract price of AUS 750,000 or more. For contracts that are entered into from July 1, 2016 and before July 1, 2017, even if they are not due to settle until after July 1, 2017, the FRCGW withholding tax rate is 10% and applies to real property disposals where the contract price is AUS 2 million and above. There are exceptions from the obligation to withhold, for example, if the vendor provides a declaration to the purchaser that the vendor is an Australian resident. Additionally, a vendor may apply to the Commissioner for a reduction in the withholding tax rate, for example, if the vendor is not expecting a gain on disposal. The withholding is a non-final withholding tax and is creditable against the vendor’s income tax liability on lodgment of a tax return.

### c. Australian Stamp Duty

#### Landholder duty

All states and territories impose landholder duty on certain acquisitions of interests in trusts with interests in land (held directly or indirectly) valued above a landholdings threshold at rates of up to 5.95%. The quantum of duty is based on the value of all landholdings (defined more broadly than common law interests in land) and in New South Wales and Western Australia also on the value of goods.

Significantly higher rates can apply where the land is residential land and the acquiring unitholder is a foreign person. Residential land and foreign person are defined in each state and territory. Currently, the maximum rate of the additional duty where the land is residential and the acquirer is foreign is 8%. This is in addition to the regular rate of duty.

All states and territories (with the exception of the Australian Capital Territory) impose landholder duty on acquisitions of 90% or more in a listed trust, although concessional rates apply in most cases. For unlisted trusts, landholder duty is imposed in all states and territories (except Queensland) on acquisitions of 50% or more (and 20% or more in Victoria). In South Australia, both landholder duty and trust acquisition duty may apply.

#### Trust acquisition duty

Queensland and South Australia separately impose a duty on changes of interests in certain private trusts. In Queensland, trust acquisition duty is imposed where the trust has a direct or indirect interest in ‘dutiable property’, including land. In South Australia, trust acquisition duty is imposed where the trust (not being a registered managed investment scheme) has a direct interest in land. The duty is imposed, at rates of up to 5.75% of the greater of the unencumbered market value and the consideration paid. Unlike landholder duty, there is no requirement that the interest acquired in the trust be above a certain percentage interest.

## 5 New legislation in relation to MITs

### a. Integrity measures – an overview

The use of ‘stapled structures’ has been subject to uncertainty since the Australian Taxation Office (‘ATO’) issued a Taxpayer Alert (TR 2017/1) on perceived abuses of the structures on 31 January 2017.

The perceived abuse related to concerns that taxpayers were establishing stapled structures to convert active business income (which would generally be subject to a 30% corporate tax rate) to passive income through the leasing of non-traditional real estate assets to an MIT (with lease rentals subject to a concessional 15% MIT withholding tax rate).

On March 27, 2018, Treasury released details of new integrity measures, which will impact stapled structures and the broader tax concessions available to foreign investors under the managed investment trust (MIT) regime. This resulted in the release on July 26, 2018, of the second stage of exposure draft (‘ED’) legislation and explanatory material (‘EM’) which passed the House of Representatives on April 3, 2019 and was subsequently enacted on 5 April 2019. The new measures have been implemented to limit the availability of the concessional 15% to only certain income derived by an MIT.

The new measures treat income derived from stapled arrangements as subject to a 30% rather than 15% tax rate (subject to limited exceptions) and also prevent income from residential housing investments from accessing the 15% tax rate (amongst other measures, as noted below). The decision to limit the 15% withholding tax rate to investments in real estate other than residential housing reflects a view that the concessional withholding tax rate was intended by the legislature only to apply to investments in traditional commercial real estate investments and that MITs were increasingly being used to invest in residential housing investments.

Specifically, the new measures apply the corporate tax rate of 30% to distributions of income that are derived from:

- MIT cross staple arrangement income;
- MIT trading trust income;
- MIT agricultural income; or
- MIT residential housing income (other than affordable housing).

Cross staple arrangement income is broadly income that is derived by the MIT (or is referable to income derived by the MIT) from economically or legally stapled entities that carry on a trading business (i.e. a stapled operating entity). Where the operating entity is itself deriving rental income from third parties, the rental income derived by the MIT would not be subject to the 30% withholding tax. There are also certain exceptions from the 30% withholding for cross staple rent, for example, where the cross staple rent is de minimis. As stapled arrangements are a common feature in the student accommodation and hotel sectors, it is expected that many investments in these sectors will be impacted.

MIT trading trust income is income that is derived from an underlying trading business in which the MIT has a direct or indirect interest.

MIT residential housing income is income that is from residential premises but not commercial residential premises, including capital gains from disposals of entities with residential housing assets in certain circumstances. The definition of residential premises and the application of a non-concessional 30% withholding tax rate to income from residential premises will potentially impact a range of sectors including the retirement villages, aged care and serviced apartment investment assets. As noted above, there is an exception to the 30% withholding in relation to affordable housing and student accommodation assets.



## b. Transitional measures

Transitional rules will apply to certain existing investments that meet pre-defined qualifying criteria and will apply to certain pre-existing arrangements.

If the transitional rules apply, the existing MIT withholding tax rate of 15% should continue to apply until, broadly:

- For MIT cross staple arrangement income relating to a facility that is not an economic infrastructure facility (i.e. typical real estate investments) – July 1, 2026;
- For MIT trading trust income – July 1, 2026;
- For MIT agricultural income – July 1, 2026; and
- For MIT residential housing income (other than affordable housing) – October 1, 2027.

The application of the transitional provisions, in particular, are complex and will depend on the particular factual circumstances.

It is important to note that the above measures are in exposure draft legislation which has not been enacted and therefore the proposals could be subject to change prior to becoming law in Australia.

## 6 Tax treatment of foreign REIT and its domestic unit holder

Foreign REIT	Corporate unit holder	Individual unit holder
Similar to an Australian Trust, however with modifications	Like corporate unitholder of an Australian trust	Like individual unitholder of an Australian trust

### Foreign REIT

Foreign REITs are taxed on Australian sourced income and capital gains on taxable Australian property. The taxation of a foreign REIT will depend on the type of entity the REIT is for Australian tax purposes and the investments structure adapted. If the foreign REIT is a trust, the tax implications will broadly be in accordance with 3.1 and 4.2 above. Such foreign REITs may qualify as an eligible widely held investor for MIT purposes (depending upon the structure used to invest into Australia).

### Corporate unit holder

Corporate unitholders of a foreign trust are taxed on income broadly as above with a tax offset for foreign tax paid (subject to an offset cap amount).

### Individual unit holder

Individual unitholders of a foreign trust are taxed on income broadly as above with a tax offset for foreign tax paid (subject to an offset cap amount). ■

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GLOBAL  
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ASIA - PACIFIC

# Hong Kong

HK REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
HK – REIT	2003	Code on Real Estate Investment Trusts	Trust type

The Code on Real Estate Investment Trusts (Code on REITs) was first introduced in July 2003 and revised on June 2005, June 2010, April 2013 and July 2014. REITs in Hong Kong are structured as trusts. They have to comply with the Code on REITs issued by the Securities and Futures Commission (SFC) for authorisation.

There are currently ten REITs with a total market capitalisation of approximately EUR 17.697 billion as at July 10, 2014 (to be supplied by Consilla Capital).

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index**	Sector Mkt Cap (EUR m)	% of Global REIT Index
Hong Kong	9	3	EUR 33,878	2.25%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Link Real Estate Investment Trust	EUR 22,760	42.80%	2.82%	1.98%
Champion REIT	EUR 4,287	34.62%	4.02%	0.13%
Fortune Real Estate Investment Trust	EUR 2,327	23.80%	4.77%	0.14%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

\*\* The number considers only those REITs covered by the REIT regime in Hong Kong and owning properties mainly in the same country.

# 2 Requirements

## a. Formalities/procedure

Key requirements
<ul style="list-style-type: none"> <li>- To be authorised by the SFC of Hong Kong</li> <li>- Appointment of a trustee</li> <li>- Appointment of a management company</li> </ul>

REITs have to be in the legal form of a trust and governed by the Code on REITs. They also need to be authorised by the SFC of Hong Kong.

One trustee that is functionally independent of the management company of the REIT must be appointed, but may be part of the same corporate group if certain requirements are met. The REITs listed in Hong Kong have all appointed independent trustees.

Furthermore, a management company that is acceptable to the SFC has to be appointed. An independent property appraiser has to also be appointed. Annual valuation of the REIT's assets must take place. In the case of a transaction (not defined in the Code on REITs, but generally understood to refer to significant transactions such as an acquisition or disposal of property etc), the management company shall, where necessary or required by the Code, engage a financial adviser.

The management company may choose to itself perform all the functions required of it under the Code on REITs or delegate or contract out to one or more outside entities one or more of these functions.

Certain transactions with connected parties, such as the management company, the trustee, a significant unitholder of 10% or more, the property-valuer or transactions between trusts which are managed by the same management company, are subject to approval by the unitholders.

## b. Legal form /minimum initial capital

Legal form	Minimum share capital
Unit trust	No

### Legal form

REITs have to be in the legal form of a trust. A REIT may hold real estate directly or indirectly through special purpose vehicles that are legally and beneficially owned by the REIT.

### Minimum initial capital

No formal minimum capital requirements exist in the Code on REITs.

## c. Unit holder requirements/listing requirements

Unit holder requirements	Listing mandatory
No requirements	Yes

### Unitholder requirements

All REITs in Hong Kong are in the form of a trust, and investors are the unitholders of the trust. There are no specific unitholder conditions that have to be fulfilled for REITs to be authorised in Hong Kong. Also, there are no restrictions on foreign unitholders.

### Listing requirements

All REITs in Hong Kong have to be listed on the Stock Exchange of Hong Kong Limited ('SEHK') within a period acceptable to the SFC. The REITs in Hong Kong are subject to the listing rules of SEHK.

#### d. Asset levels/activity test

##### Restrictions on activities/investments

- Must primarily invest in real estate
- Must hold the real estate for at least two years
- Prohibited from investing in vacant land with exception, or engaging in property development activities with exception
- Must not acquire any asset that involves the assumption of any unlimited liability
- May invest in real estate located in Hong Kong or overseas

REITs must invest primarily in real estate that generates recurring rental income. The REIT may not acquire non-income generating real estate in excess of 10% of the total net asset value of the REIT at the time of acquisition.

A REIT must hold its real estate for a period of at least two years unless consent is obtained from its unitholders by way of a special resolution at a general meeting.

A REIT is permitted to establish and own special purpose vehicle companies (SPVs) to hold its real estate investments. Under the Code on REITs, SPVs must be legally and beneficially owned by the REIT, and the REIT must have majority ownership and control of the SPVs. Generally, no more than two layers of SPVs are allowed unless specifically approved by the SFC. Where the REIT invests in hotels, recreation parks or serviced apartments, such investments shall be held by SPVs.

REITs are prohibited from investing in vacant land unless the management company has demonstrated that such investment is part-and-parcel of permitted property development (see below).

In engaging or participating in property development activities (refurbishment, retro-fittings and renovation excepted), the aggregate investments in all property developments undertaken, together with the aggregate contract value of the uncompleted units of real estate acquired, shall not exceed 10% of the gross asset value of the REIT.

A REIT must not acquire any asset that involves the assumption of any liability that is unlimited.

If a REIT indicates a particular type of real estate in its name, it must invest at least 70% of its non-cash assets in such type of real estate.

There is no limitation to the holding of units in a REIT in Hong Kong.

REITs may invest in foreign assets.

#### e. Leverage

##### Leverage

Limitation to 45% of total gross asset value

The gearing ratio limit is 45% of the total gross asset value of the REIT.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of the audited annual net income after tax	Specified in the trust deed	Annually

### Operative income

A REIT shall distribute not less than 90% of its audited annual net income after tax in the form of dividends to its unitholders each year.

### Capital gains

Whether any capital gains on disposal of real estate could be distributed is generally specified in the trust deed when a REIT is launched for sale to the public.

## g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- De-listing</li> <li>- Loss of authorisation by the SFC</li> </ul>

# 3 Tax treatment at the level of REIT

## a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- REIT is exempt from profits tax</li> <li>- REIT may be subject to property tax</li> <li>- SPV is subject to profits tax.</li> <li>- Dividends from SPV are tax-exempt</li> <li>- Foreign sourced income is tax-exempt</li> </ul>	N/A	N/A

### Current income

A REIT is exempt from Hong Kong profits tax under the Inland Revenue Ordinance of Hong Kong. However, where the REIT holds real estate in Hong Kong directly and derives rental income thereon, such rental income will be subject to Hong Kong property tax at the prevailing rate of 15%.

Where the REIT holds real estate in Hong Kong indirectly via SPVs, such SPVs will be subject to profits tax at the prevailing rate of 16.5% in respect of the profits derived from the real estate. Such SPVs would

generally be exempt from property tax.

Under the two-tier profits tax system which is effective from the year of assessment 2018/19, the first HKD 2 million of assessable profits of REIT will be taxed at 8.25% (i.e. half of the normal tax rates), regardless of the REIT's size or industry. The remaining assessable profits will be subject to the original rate of 16.5%.

Income derived from real estate situated outside Hong Kong and capital gains is generally exempt from property tax and profits tax.

Dividends paid by an SPV to another SPV are generally exempt from profits tax.

## Capital gains

There is no capital gains tax in Hong Kong.

## Withholding tax

There is no withholding tax on interest, dividends or distributions from a REIT in Hong Kong.

Hong Kong has a territorial tax system and does not tax foreign-sourced income. There is, therefore, no question of any entitlement to a refund of a tax credit for foreign taxes withheld on the foreign-sourced income of a REIT.

## Transfer pricing

The Inland Revenue (Amendment) (No. 6) Ordinance 2018 ("the Amendment Ordinance") was gazetted on July 13, 2018. The main objectives are to codify the transfer pricing principles, implement certain measures under the Base Erosion and Profit Shifting (BEPS) package and align the provisions in the Inland Revenue Ordinance (Cap. 112) with international tax requirements.

The key elements of the Amendment Ordinance are enhancements to double taxation relief provisions, transfer pricing rules and related provisions, TP documentation requirements relating to the master file, local file and country-by-country report, amendments to preferential regimes, including an extension of tax concession to domestic transactions and prescription of thresholds for substantial activities requirements.

## Other taxes

There is no special tax treatment applicable to REITs in Hong Kong.

## Accounting rules

REITs in Hong Kong are required to comply with the local GAAP, which is in line with IFRS.

### b. Transition regulations

#### Conversion into REIT status

N/A



There are no specific tax privileges and concessions when converting into REIT status.

### c. Registration duties

#### Registration duties

##### Stamp duties

The transfer of Hong Kong real estate or shares of Hong Kong incorporated SPVs would be subject to stamp duty in Hong Kong. Stamp duty on sale of immovable property in Hong Kong is charged at rates which vary with the amount or value of the consideration. For non-residential property, the maximum rate of 8.5% applies where the transfer consideration or value of real estate is above HKD 21,739,130. For residential property, unless specifically exempted or provided otherwise, a flat rate at 15% applies to the consideration or value of the residential property, whichever is the higher.

Where shares in a Hong Kong company are transferred, Hong Kong Stamp Duty at the rate of 0.2% applies to the higher of the transfer consideration or the value of the shares.

Hong Kong Stamp Duty also applies to a lease of real estate in Hong Kong, generally at a rate of 0.25% to 1% of the average yearly rent, depending on the term of the lease.

Hong Kong introduced a Special Stamp Duty (SDD) with effect from November 20, 2010. Unless specifically exempted, any residential property acquired on or after November 20, 2010, either by an individual or a company (regardless of where it is incorporated) and resold or transferred within a specified period of time after the acquisition, would be subject to SDD. The SDD payable is calculated by reference to the stated consideration or the market value, whichever is higher, at the following regressive rates for the different holding periods by the vendor or transferor before the disposal. The SDD rates were revised for any residential property acquired on or after October 27, 2012. All parties to a contract are liable to the SSD.

Period within which the residential property is resold or transferred after its acquisition	SSD Rates
(for residential property acquired on or after	20%
October 27, 2012)	15%
More than 12 months but for 36 months or less	10%

Hong Kong introduced a Buyer's Stamp Duty (BSD) with effect from October 27, 2012. Unless specially exempted, a purchaser (any individual without Hong Kong permanent residence or any corporation irrespective of its place of incorporation) would be liable to BSD for transfer of residential property on or after October 27, 2012. BSD is charged at 15% on the higher of sales consideration or market value.

## 4 Tax treatment at the unit holder's level

### a. Domestic unit holder

Corporate unitholder	Individual unitholder	Withholding tax
Tax-exempt	Tax-exempt	N/A

#### Corporate unitholder

While distributions from REITs are not specifically tax-exempt, the Inland Revenue Department's practice so far is not to tax a REIT's distributions, whether they are received by individual or non-individual unitholders.

Gains on the disposal of REIT units are not subject to profit tax in Hong Kong if such gains are capital gains. A unitholder carrying on a trade, profession or business in Hong Kong consisting of the acquisition and disposal of units in a REIT is subject to Hong Kong profits tax in respect of any gains derived from the disposal of the units in Hong Kong.

#### Individual unitholder

While distributions from REITs are not specifically tax-exempt, the Inland Revenue Department's practice so far is not to tax a REIT's distributions, whether they are received by individual or non-individual unitholders.

Gains on the disposal of REIT units are not subject to profit tax in Hong Kong if such gains are capital gains. A unitholder carrying on a trade, profession or business in Hong Kong consisting of the acquisition and disposal of units in a REIT is subject to Hong Kong profits tax in respect of any gains derived from the disposal of units in Hong Kong.

#### Withholding tax

There is no withholding tax in Hong Kong on the distribution of profits.

#### Stamp duty

Hong Kong stamp duty is chargeable in respect of the transfer of the REIT units at 0.2% of the transfer consideration (payable by the transferor and transferee at 0.1% each). In addition, a fixed duty of HKD 5 is currently payable on any instrument of transfer of units.

### b. Foreign unit holder

Corporate unitholder	Individual unitholder	Withholding tax
Tax-exempt	Tax-exempt	N/A

## Corporate unitholder

While distributions from REITs are not specifically tax-exempt, the Inland Revenue Department's practice so far is not to tax a REIT's distributions, whether they are received by individual or non-individual unitholders.

Gains on the disposal of REIT units are not subject to profit tax in Hong Kong if the foreign unitholder is not carrying on any trade, profession or business in Hong Kong or such gains are capital gains. A unitholder carrying on a trade, profession or business in Hong Kong consisting of the acquisition and disposal of units in a REIT is subject to Hong Kong profits tax in respect of any gains derived from the disposal of units in Hong Kong.

In addition, certain transactions undertaken by genuine foreign funds are exempt from Hong Kong tax.

## Individual unitholder

While distributions from REITs are not specifically tax-exempt, the Inland Revenue Department's practice so far is not to tax a REIT's distributions, whether they are received by individual or non-individual unitholders.

Gains on the disposal of REIT units are not subject to profit tax in Hong Kong if the foreign unitholder is not carrying on any trade, profession or business in Hong Kong or such gains are capital gains. A unitholder carrying on a trade, profession or business in Hong Kong consisting of the acquisition and disposal of units in a REIT is subject to Hong Kong profits tax in respect of any gains derived from the disposal of units in Hong Kong.

In addition, certain transactions undertaken by genuine foreign funds are exempt from Hong Kong tax.

## Withholding tax

There is no withholding tax in Hong Kong on the distribution of profits.

## Stamp duty

Hong Kong stamp duty is chargeable in respect of the transfer of the REIT units at 0.2% of the transfer consideration (payable by the transferor and transferee at 0.1% each). In addition, a fixed duty of HKD 5 is currently payable on any instrument of transfer of units.

# 5 Tax treatment of foreign REITs and its domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
Local tax rules apply	No taxation	No taxation

## Foreign REIT

Local tax rules apply. Rental income derived from properties in Hong Kong is subject to either Hong Kong profits tax or property tax.

## Corporate unitholder

No Hong Kong tax if no business consisting of the acquisition and disposal of investment in REITs is carried on in Hong Kong.

## Individual unitholder

No Hong Kong tax if no business consisting of the acquisition and disposal of investment in REITs is carried on in Hong Kong. ■

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REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

Year	Citation	REIT type	REIT market
September 26, 2014	Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2014 ('REIT Regulations') – certain modifications/amendments are made from time-to-time via press release and notifications	Trust	<p>India had its first REIT listing with the units of Embassy Office Parks REIT on April 1, 2019, on the Indian Stock exchange</p> <p>India's maiden REIT offering closed on April 1, 2019, at INR 314.10 per unit on the stock exchange, up by 4.7% from its issue price of INR 300 per unit</p> <p>The Embassy Office Parks REIT is a platform jointly owned by Blackstone Group LP and Bengaluru-based developer Embassy Property Developments Private Limited</p> <p>The initial public offer of the Embassy REIT raised INR 4,750 crores</p>

Post enactment of the REIT Regulations, the regulators partnered with relevant stakeholders in the country including government bodies, investors and real estate developers and have brought about many changes in the Indian REIT Regulations to bring them in line with globally recognised norms, especially with respect to distribution policies, capital requirements, etc. The Reserve Bank of India through a series of amendments in its regulatory policy enabled foreign investments under the automatic route in REITs. The pass-through status for REITs was provided under the taxation regime for REITs right from the beginning. However, to make the pass-through status effective keeping in mind the practical considerations put forward by the stakeholders, further amendments were made into tax law. Such consistent impetus by Government to bring REITs to life has resulted in the launch of first successful REIT listing in India.

Although several foreign REITs have been investing in Indian assets over the last few years, encouraging response and a good listing of Embassy REIT opens doors for many real estate enterprises with a substantially large portfolio of rent-yielding properties to set up their own Indian REIT. Ability to raise resources through monetisation of rent-yielding properties at relatively attractive cost is a re-rating trigger for not only the REIT-issuing real estate companies but also boosts investor sentiment towards the entire sector.

## Sector summary\*

Listing Country	Number of Listed REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
India	1	0	EUR 3,609	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

A REIT should be registered with SEBI and be constituted as a trust with its trust deed having the main objective of undertaking activity of REIT in accordance with the REIT Regulations. REIT should have a sponsor, manager and trustee

#### a.1 Sponsor to REIT

Conditions for eligibility of **Sponsor** are as under:

- No maximum limit on the number of sponsors; the concept of ‘sponsor group’ incorporated to leverage on the capabilities of other group entities in terms of eligibility criteria for being a sponsor;
- A consolidated net worth of at least INR 1000 million, with each sponsors’ net worth being at least INR 200 million;
- The sponsor or its associates to have not less than five years of real estate development or real estate fund management experience; and
- Track record of at least two completed projects for a developer sponsor.

Key rights and responsibilities – **Sponsor(s) and sponsor groups:**

- Setting up a REIT and appointing a trustee.
- Transferring or undertaking to transfer assets, rights and interest in the holding company (‘Holding company’)/Special Purpose Vehicle (‘SPV’) to the REIT before allotment of units to applicants
- Minimum post-initial public offer (‘IPO’) holding of sponsor and sponsor group to be at least 25%:
  - three-year lock-in period for 25% of post-IPO holding;
  - one-year lock-in period for balance post-IPO holding;
- Sponsors and sponsor group shall collectively hold:
  - a minimum of 25% of the total units of a REIT on a post-issue basis for a period of three years from the initial offer; and
  - a minimum of 15% of the outstanding units of a listed REIT at all times.
- Each sponsor shall hold a minimum of 5% of the outstanding units of a REIT at all times.
- Divestment of 15% continued holding subject to the following:
  - the completion of a three-year lock-in period from the listing date; and
  - another sponsor acquiring the minimum holding with the prior approval of the unitholders.

#### a.2 Manager to REIT

Conditions for eligibility of a manager of a REIT (being a company, limited liability partnership (‘LLP’) or a body corporate) are as under:

- A minimum net worth of INR 100 million;
- A manager or its associates should have not less than five years of experience in fund management/ advisory services/property management in the real estate industry or in the development of real estate; and
- A manager to have at least two key personnel having not less than five years of experience in fund management advisory or property management in the real estate sector or real estate development.

#### Key rights and responsibilities – **Manager:**

- Ensuring that a REIT's, Holding company's and SPV's assets have proper legal, binding and marketable titles and agreements.
- Identifying and recommending investment opportunities.
- Complying with the conditions and strategy mandated for the investment.
- Appointing other service providers in consultation with a trustee.
- Undertaking lease and property management (directly or through agents).
- Ensuring that a REIT's assets are adequately insured.
- Addressing unitholders' grievances and distribution-related issues.
- Ensuring annual audit of a REIT's accounts by an auditor.
- Overseeing developmental activities.
- Providing activity and performance reports on a REIT every three months to its board or governing board.
- Ensuring adequate disclosure and timely submission of documents to the concerned stock exchange.
- Maintaining records pertaining to activities of a REIT for a minimum period of seven years.

### a.3 Trustee to REIT

#### Conditions for Eligibility of **Trustee:**

Registered with SEBI, and not an associate of the sponsor(s) or manager.

- Key rights and responsibilities – Trustee:
- Appointing a manager and executing his or her agreement.
- Overseeing the manager's activities and operations and obtaining compliance certificates on a quarterly basis.
- Reviewing related party transactions.
- Obtaining unitholders' approval on specified matters.

### b. Legal form and minimum initial capital

Legal form	Minimum asset size
Trust	INR 5,000 million



### c. Unitholder requirements and listing requirements

Mandatory listing of units of REIT within 3 years from the date of registration with SEBI

Slabs for minimum public float have been prescribed as under:

If post-issue capital is:	Minimum public float required
< INR 16,000 million	25% of the post-issue capital or INR 2,500 million, whichever is higher
INR 16,000 million < INR 40,000 million	Minimum INR 4,000 million
> INR 40,000 million	Minimum 10% of the post-issue capital

However, the public float shall be increased to a minimum of 25% of the post-issue capital (where lower pursuant to the above slabs) within a period of three years from the date of listing.

A minimum trading lot of INR 0.1 million and minimum subscription of INR 0.2 million.

The minimum number of subscribers to the initial public offer should be 200.

Units held by sponsors/promoters for a period of one year or more; may be offered to the public for sale:

- Holding period of equity shares, compulsorily convertible securities (from the date fully paid up), interest in Holding company/SPV (against which units of Trust were received) to be considered in the calculation of above one year.
- Above convertibles to be converted to equity shares prior to filing offer doc.

Units held by persons other than sponsor prior to listing to be held for a period of a minimum one year post listing.

Foreign investments in REIT regulated by SEBI is permissible under the automatic route per the exchange control regulations.

Concept of a strategic investor was recently defined in December 2017.:

- A strategic investor means an Infrastructure Finance Company registered as an NBFC, Scheduled Commercial Bank, International Multilateral Financial Institution, systemically important NBFC, FPIs who can invest jointly or severally minimum 5% or maximum 25% of total offer size by REIT.
- The lock-in period means 180 days from date of listing of public issue.
- Draft Offer Document is to mention the details of the strategic investor.
- The unit price for a strategic investor should be greater than or equal to the public issue price. If the strategic investor price is less than the public issue price, the strategic investor is to make an additional investment. If the strategic investor price is higher than the public issue price, no refund would be issued to the strategic investor.
- If a public issue fails due to a minimum subscription, the strategic subscription agreement will be terminated.

#### d. Asset levels/activity test

##### Restrictions on activities/investments

- Investment permitted in:
  - (1) Real estate assets in India (other than vacant land, agricultural land, etc.)
  - (2) Securities of SPVs holding permissible real estate assets in India
- Investment through a Hold Co is also permitted, subject to conditions

##### Asset-related conditions:

At least 80% of the value of a REIT to be in completed and rent/income-generating real estate, with a lock-in period of three years from the purchase date.

A maximum of 20% of the total value of REITs can be from:

- under-construction properties with a lock-in period of three years after completion and completed but non-rent generating properties with a lock-in period of three years from the date of purchase;
- unlisted equity shares of companies deriving at least 75% of their operating income from real estate activities (subject to lock-in as mentioned above being satisfied where investment in under-construction property or completed but non-rent generating property is made through unlisted equity shares);
- the listed or unlisted debt of real estate companies (other than investment in debt of Holding company/SPV);
- mortgage-backed securities;
- equity shares of listed companies in India, generating at least 75% of their income from real estate activities;
- government securities;
- unutilised floor space index ('FSI') and transferable development rights ('TDR') with respect to existing investments; or
- cash or money market instruments.

##### Additional conditions:

- a direct holding of real estate assets in India or through an SPV or a two-level structure through a holding company.

Investment through a holding company should be subject to the following requirements:

- an ultimate holding interest of the REIT in SPVs to be at least 26%;
- other shareholders/partners of the Holding company/SPV should not restrict the REIT, holding company or SPV from complying with the REIT regulations, and an agreement has been entered into with such shareholders/partners to that effect;
- the manager, in consultation with the trustee, shall appoint at least such number of nominees on the board of a holding company and/or SPV which are in proportion to the holding interest of the REIT/holding company in the Holding company/SPV; and
- in every meeting of a holding company and/or SPV, the voting of the REIT shall be exercised.

Investment not permitted in vacant land, mortgages or agricultural land (with certain exceptions).

At least 51% of the consolidated revenue of the REIT, holding company and SPV to be from rental, leasing and letting out of assets, or incidental revenue.

Investment in other REIT or lending (except lending to Holding company/SPV) not permitted.

Unitholder's approval required for disposal of a REIT's assets or interest in the SPV if it exceeds 10% of the value of the assets in a financial year.

Co-investment permitted subject to conditions.

#### e. Leverage

Leverage
<ul style="list-style-type: none"> <li>- Up to 25% of the asset size, no specific conditions</li> <li>- From 25% up to 49%, credit rating and unitholders approval required</li> </ul>

Aggregate consolidated net borrowings (i.e. net of cash and cash equivalents) and deferred payments not to exceed 49% of the value of the REIT assets. If such borrowings exceed 25% of the value of the REIT assets:

- Credit rating to be obtained from a credit rating agency registered with SEBI
- Approval of the unitholders (where the number of votes cast in favour is more than the number of votes cast against)

#### f. Profit distribution obligations

Dividend	Timing
Not less than 90% of net distributable cash flows	At least once every six months

- Minimum of 90% of the net distributable cash flow of a REIT.
- Minimum net distributable cash flows to be distributed by a holding company to a REIT (subject to provisions of the Companies Act, 2013, and Limited Liability Partnership Act, 2008):
  - 100% of cash flows received from SPVs; and
  - 90% of the balance.
- An SPV to distribute a minimum of 90% of its net distributable cash flows to a REIT/Holding company.
- A REIT is to distribute at least 90% of the sale proceeds arising from the sale of property or equity shares/interest in a Holding company/SPV unless reinvestment is proposed within a period of one year.
- Distribution to be undertaken at least once every six months.

#### g. Sanctions

### Penalties/loss of status rules

In the case of any default by REIT or parties to the REIT or any other person involved in the activity of the REIT, the same is dealt with in the manner provided in SEBI (Intermediaries) Regulations, 2008

## h. Related party transactions

Permission granted subject to the following:

- The arm's-length requirement being met;
- specified disclosures being made to unitholders and the stock exchange;
- valuation reports or fairness opinions obtained from independent valuer(s) in the case of specified transactions (for instance, buying and selling of assets);
- unitholder's approval required for the following transactions:
  - The acquisition or sale of investments from or to related parties (whether directly or through the holding company or SPV) exceeding 10% of the total value of the REIT; and;
  - borrowings from related parties in a financial year exceeding 10% of total consolidated borrowings of the REIT, holding company and SPV(s).

## i. Valuation

- Complete valuation of a REIT (in the prescribed format) to be undertaken at least once every financial year.
- The valuer to have minimum experience of five years.
- The valuer not to be an associate of the sponsor, manager/trustee.
- Half-yearly valuation of REIT assets to be conducted for the half-year ending September 30.
- Complete valuation to be undertaken for purchase or sale of property; unitholders' approval needed if:
  - The acquisition price is more than 110% of the valuation; and
  - The sale price is less than 90% of such valuation.
- A two-year cooling-off period for the valuer after every four consecutive years of valuation being done of the same property.
- The valuer's remuneration not to be linked to the value of the asset.

## j. Governance aspects

- Unitholders' meetings to be convened at least once every year within 120 days from the end of the financial year, with the gap between two meetings not exceeding 15 months. Generally, a resolution is considered as passed if unitholders casting votes in favour are more than those casting votes against it.
- For resolutions pertaining to certain specified matters (for instance, a change in the manager or sponsor, or delisting), the resolution is considered as passed if votes cast in favour are at least 1.5 times the votes cast against. An annual report to be provided to unitholders within three months from the end of the financial year; half-yearly report to be given within 45 days from September 30.
- Price-sensitive information as well as that having a bearing on operations or the performance of a REIT

to be disclosed to the stock exchange.

#### k. Other aspects

- Multiple classes of REIT units not permitted.
- However, subordinate units carrying inferior rights may be issued to sponsor(s) and their associates.
- Parity to be maintained between unitholders (no preferential voting or other rights among unitholders).

## 3 Tax treatment at the REIT level

#### a. Income tax<sup>1</sup>

Capital gains from the sale of securities of SPV	Dividend income from SPV	Interest income from SPV	Rental income from property held directly by REIT	Any other income
The income of REIT is taxable at the applicable rates	The income of REIT should be exempt	The income of REIT is not taxable	The income of REIT is not taxable	30%

#### Capital gains from the sale of securities of SPVs:

- Listed equity shares<sup>2</sup>
  - Long-term capital gains above INR 0.1 million are taxable at 10%.
  - Short-term capital gains are taxable at 15%.
- Others
  - Long-term capital gains are<sup>3</sup> taxable at 20% (with indexation<sup>4</sup>).
  - Short-term capital gains are<sup>5</sup> taxable at 30%.

#### Dividend income from an SPV:

Dividend income received by the REIT from the SPV should be exempt in the hands of the REIT. In order to further rationalise the taxation regime for REITs, Finance Act, 2016 provides an exemption from the levy of dividend distribution tax ('DDT') in respect of dividend declared, distributed or paid by the SPV to the REIT, subject to the REIT holding 100% stake in the SPV and the dividend being distributed out of the

<sup>1</sup> All the tax rates mentioned herein would have to be increased by applicable surcharge i.e. for financial year 2018-19, 7% for Indian Companies with taxable income below INR 100 Million and 12% for exceeding INR 100 Million and 2% for foreign companies with income below INR 100 Million and 5% for those exceeding INR 100 Million. Such tax liability to be further increased by education cess of 4%.

<sup>2</sup> Subject to payment of Securities Transaction Tax ('STT') on the transaction of acquisition (unless specifically excluded) as well as on sale of the shares of the SPV

<sup>3</sup> If held for more than 24 months

<sup>4</sup> Indexation is not applicable on sale of debt securities

<sup>5</sup> If held for up to 24 months

profits of SPV post-acquisition by the REIT. Such a conditionality creates leakage on account of the DDT in the case of investment by a REIT in an SPV through a holding company wherein the holding by the holding company is not 100%.

### Interest income from SPV:

Interest income received by the REIT from the SPV should be exempt in the hands of the REIT. However, the REIT is required to withhold tax at the rate of 5% on the distribution of such income to a foreign unitholder and at the rate of 10% on the distribution of such income to a domestic unitholder.

### Rental income from property held directly by REIT:

Rental income received by the REIT should be exempt in the hands of the REIT. Tenants are not liable to withhold taxes on rental income paid to REIT on the property held directly by the REIT. However, the REIT would be required to withhold tax at the rate of 10% on the distribution of such income to a domestic unitholder and in the case of the distribution of such income to a non-resident unitholder, the withholding shall be at the rates in force.

Other income of the REIT:

Any other income, including income from the assets held directly by the REIT, should be taxable at 30%.

## b. Registration duties

### Registration duties

- Stamp duty and registration costs on real estate range between 5% and 15%
- Stamp duty on transfer of shares is up to 0.25

There are no specific exemptions available to REITs.

Stamp duty is levied at the time of registration of the purchase transaction. Rates for stamp duty varies between 5% and 15% on real estate transactions, depending upon the state in which the instrument for transfer is executed. Stamp duty is levied on the sale price or value of the asset as per circle rates, whichever is higher.

Registration of documents recording the transfer of real estate asset in the name of purchaser attracts registration fee. Registration fee is a state levy and varies across states in India.

The following fee structure is applicable to the REIT under the REIT Regulations:

Fees	REIT
Application fees	INR 0.1 million
Registration fees	INR 1 million
Issue filing fees	0.1% in the case of the initial and follow-on offer and 0.05% in the case of the rights issue

## 4 Tax treatment at the unitholder's level<sup>6</sup>

### Income-tax on units received in exchange of shares of the SPV

- Units received in exchange of shares of the SPV should not be taxable in the hands of the unitholder at the time of such exchange. However, at the time of disposal of such units by the unitholder, the unitholder would be liable to pay the applicable capital gains tax (the preferential capital gains regime, explained below under the heading 'Income-tax on sale of units by the unitholder', would be applicable for such units held by the unitholder).
- The cost of acquisition of the shares of the SPV should be considered to be the cost of acquisition for the purposes of computing the capital gains in the hands of the unitholder. The period of holding of the units should be computed from the date of acquisition of the shares of the SPV.

### Income-tax on units received in exchange of assets (other than shares of the SPV)

- Units received in exchange of assets (other than shares of the SPV) shall be taxable at the time of swap. Long-term capital gains<sup>7</sup> on the swap of assets shall be taxable at the rate of 20%, and short-term capital gains shall be taxable at the rate of 30%.

### Income-tax on sale of units by the unitholder

- Long term capital gains<sup>8</sup> more than INR 0.1 million on sale of units of a REIT by the unitholder should be taxable at the rate of 10% in the hands of the unitholder, subject to payment of STT.
- Short-term capital gains<sup>9</sup> on the sale of units of a REIT by the unitholder should be chargeable to tax at the rate of 15%.
- Securities transaction tax, at the rate of 0.1%, should be leviable on the transaction value of the sale. Separately, STT at 0.2% should be leviable in the case of sale of unlisted units of REIT by a unitholder which was acquired by way of swapping of shares of an SPV.
- Minimum Alternative tax ('MAT') at the rate of 18.5% shall be payable on profits arising (as per books of account) from the sale of units. In the case of Sponsors, a separate computation mechanism is prescribed for calculation of MAT.

### Income-tax on distributions received from the REIT

Income received by the investors as distributions from the REIT is exempt in the hands of the investors. However, such distributions received from the REIT, which are attributable to the interest income accrued to/received by the REIT and rental income received from the tenants with respect to the property held directly by the REIT are as follows:

- Interest income should be chargeable to income tax in the hands of the unit holder being resident at the applicable rates. Interest income received by a non-resident unit holder should be taxable at

<sup>6</sup> All the tax rates mentioned herein would have to be increased by applicable surcharge i.e. for financial year 2018-19, 7% for Indian Companies with taxable income below INR 100 Million and 12% for exceeding INR 100 Million and 2% for foreign companies with income below INR 100 Million and 5% for those exceeding INR 100 Million. Such tax liability to be further increased by education cess of 4%.

<sup>7</sup> If held for more than 36 months (other than immovable property)/ 24 months in case of immovable property

<sup>8</sup> If held for more than 36 months

<sup>9</sup> If held for up to 36 months

the rate of 5%. Taxes withheld by the REIT as discussed above should be available as credit.

- Rental income should be chargeable to income tax in the hands of the unit holder at the rates applicable to such unit holder (a non-resident unit holder may be allowed to take treaty benefits if available on such income). Taxes withheld by the REIT as discussed above should be available as credit.

## 5 Exchange Control Regulations

### Foreign investment permitted in REIT

- Persons resident outside India, including Registered Foreign Portfolio Investor ('RFPI') and Non-resident Indian (NRI), have now been permitted to invest in units of REIT.

### Sale/transfer/pledge of units in REIT

- Such investments can be transferred or sold in any manner or redeemed as per SEBI regulations/RBI directions.
- Further, these units could be pledged by the non-resident unitholder to secure credit facilities.

### Are investments by REIT treated as foreign investment?

- Investments by a REIT shall be regarded as a foreign investment only if either the sponsor or the manager<sup>10</sup> is not Indian 'owned and controlled'. If such sponsor or the manager is foreign owned, they would need to comply with the applicable sectoral caps and other restrictions. For this purpose, ownership and control of companies and LLP are to be determined in accordance with the regulations prescribed.

### Procedural conditions

- The payment for the units of REIT is to be made by inward remittance through normal banking channels, including by debit to a Non-Resident Rupee ('NRE') or a Foreign Currency Non-Resident ('FCNR') account. REIT will have to report foreign investment in the REIT to RBI in the recently introduced Single Master Form.

### Definition of 'real estate business'

- In the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000, 'real estate business' has been regarded as a prohibited sector for foreign investment.
- These regulations have now been amended to exclude REITs registered and regulated under the extant SEBI regulations, from the ambit of 'real estate business'. This potentially enables the REITs to directly buy (and sell) real estate. ■

*Note: All tax rates quoted in this document are exclusive of a surcharge as may be applicable and health and education cess.*

<sup>10</sup> Sponsor or Manager can be organised in the form of a LLP



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EUROPEAN PUBLIC  
REAL ESTATE ASSOCIATION

GLOBAL  
REIT SURVEY

ASIA - PACIFIC

# Indonesia

DIRE

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

Enacted year	Citation	REIT type	REIT market
2007	Regulation of Bapepam-LK (Capital Market and Financial Institution Supervisory Agency) Number IX.M.1 No: Kep-425/BL/2007 dated 18 December 2007	Collective Investment Contract – Real Estate Investment Fund (Dana Investasi Real Estat – DIRE)	One DIRE is established as of May 2018

A DIRE is a Real Estate Investment Fund as mentioned in Regulation of Bapepam-LK (Capital Market and Financial Institution Supervisory Agency, currently Otoritas Jasa Keuangan – “OJK” (Financial Services Authority)) Number IX.M.1 concerning Guidelines for Investment Managers and Custodian Banks in Conducting Management of Real Estate Investment Funds in the form of Collective Investment Contracts (CIC)<sup>1</sup>.

There are two types of DIRE, a Sharia DIRE and a ‘conventional’ DIRE. A Sharia DIRE is a collective investment scheme in real estate, according to Sharia Law. Specific Sharia DIRE guidelines were issued in 2016 which state that a Sharia DIRE must have 90% of its income derived from Sharia-compliant activities. If a DIRE does not comply with these guidelines, then it is a conventional DIRE.

Currently, two DIRE is established as of May 2018 in Indonesia.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Indonesia	2	0	EUR 983	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

Registration with the OJK or BAPEPAM, LK and Indonesia Stock Exchange

All of the following requirements apply to both conventional and Sharia DIREs.

A DIRE may make a public offering on its participation units to public investors. If a DIRE does not list its participation units on the Indonesia Stock Exchange, its investment manager shall buy back participation units that are redeemed by unitholders.

<sup>1</sup> CIC is a Collective Investment Contract as mentioned in the guidance relating to Article 18 paragraph (1) letter b of Law Number 8 of 1995 concerning the Capital Market.

A registration statement for a public offering by a DIRE shall be submitted to OJK by its investment manager (based on Decision of the Chairman of Capital Market and Financial Institutions Supervisory Agency Number: Kep-423/BL/2007 dated December 18, 2007).

In cases where a DIRE does not make a public offering, its investment manager shall submit the Collective Investment Contract of the DIRE to OJK no later than ten days following the signing of such Collective Investment Contract by attaching the following documents:

- a. any document used in the offering; and
- b. any other contract related to the DIRE in the form of a Collective Investment Contract.

The requirements for listing of participation units of a DIRE on the Indonesia Stock Exchange are as follows:

1. the registration statement for the purpose of the public offering of the DIRE that was submitted to OJK has become effective;
2. the value of assets that will comprise the initial portfolio of the DIRE is at least IDR 50,000,000,000 (IDR 50 billion) (approx. USD 3,473,200)<sup>2</sup>;
3. the number of participation units owned by the largest unitholder is not more than 75% of the total participation units of the DIRE that are in issuance at that time. This requirement also applies while the participation units of the DIRE are listed on the Indonesia Stock Exchange; and
4. there are at least 100 holders of participation units in the DIRE after the public offering.

#### b. Legal form/minimum share capital

Legal form	Minimum share capital
Collective Investment Contract	IDR 50 billion (approx. USD 3,473,200)

Value of assets that will comprise the initial portfolio of the REIT in the form of CIC is at least IDR 50 billion.

The real estate owned by a DIRE must be at least 60% occupied.

A DIRE is a vehicle that is used to pool funds from public investors that is then invested in real estate assets, assets related to real estate, and/or cash or cash equivalent.

‘Assets related to real estate’ are securities or shares of both listed and non-listed real estate companies.

A Special Purpose Company (SPC) is a Limited Company which has paid-up capital that is at least 99.9% owned by the DIRE. A DIRE can be set up with or without an SPC. However, it is usual that a DIRE does set up an SPC and typically holds its real estate investments via an SPC. The contract should be established in accordance with the rules and regulations promulgated by OJK.

A DIRE is established by an investment manager and a custodian bank. The investment manager and custodian bank of the DIRE shall fulfil their duties in good faith and in the interest of the DIRE.

<sup>2</sup> US\$ 1 = IDR 14,273 on 31 May 2019.

An investment manager that manages a DIRE shall make sure that:

- a. The DIRE invests:
  1. no less than 50% of its net asset value in real estate;
  2. no less than 80% of its net asset value in real estate and assets related to real estate; and/or
  3. cash and cash equivalents equate to no more than 20% of its net asset value; and
- b. Assets that are included in the portfolio of the DIRE have a strong legal foundation, are legitimate and liquid.

#### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
At least 100 shareholders	No

The number of participation units owned by the largest unitholder must not be more than 75% of the total participation units of the DIRE.

In the case where the name of the DIRE is derived from certain real estate or certain assets related to real estate, the DIRE shall invest no less than 70% of its net asset value in that real estate or assets related to real estate after which it is named.

There must be at least 100 holders of participation units in the DIRE after a public offering.

#### d. Asset level/activity test

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- Prohibition on engaging in short selling of real estate to realise a profit margin</li> <li>- Prohibition on investing in vacant land or in a property that is still under development; the activity of development shall exclude redecoration, repairs and maintenance, and renovation</li> <li>- Prohibition on lending and/or pledging real estate under its control for the interest of other persons</li> <li>- Prohibition on investing in real estate and or asset related to real estate outside of Indonesia</li> <li>- Prohibition on issuing debt securities</li> <li>- Prohibition on engaging in a short sale (less than two years)</li> <li>- Assets of the DIRE cannot form part of assets owned by the investment manager or custodian bank</li> </ul>

DIREs shall only invest in real estate, assets related to real estate in Indonesia, and or cash or cash equivalent.

DIREs are prohibited from investing in vacant land or in a property that is still under development. Development activities shall exclude redecoration, repair and maintenance, and renovation.

DIREs are prohibited from lending and/or pledging real estate under its control for the interest of other persons.

The investment manager and custodian bank of the DIRE are prohibited from acting for and on behalf of themselves in buying and selling real estate, assets related to real estate and other assets of the DIRE for which they act.

DIREs are only permitted to borrow funds by way of other than issuing debt securities for the purpose of acquiring real estate. The value of such borrowing must not exceed 45% of the value of the real estate to be acquired.

In the case where an investment manager or custodian bank of a DIRE quits or transfers its duties to other investment manager or custodian bank, the former investment manager or custodian bank is to continue managing the DIRE before a replacement is appointed.

DIREs are prohibited from engaging in a short sale of real estate to realise a profit margin.

DIREs are prohibited from transferring real estate assets that have been owned for less than two years, unless:

- a. It was clearly stated to the unitholders of the DIRE at the time of making the investment that the intention was to sell the investment within two years; or
- b. more than one-half of all existing participation unitholders of the DIRE have given their approval to make the sale in a general meeting of unitholders of the DIRE.

DIREs are prohibited from transferring real estate assets for a price that is 90% or lower than the price assessed by an appraiser, and the date of the valuation shall not be more than 6 months from the date of the asset transfer.

#### e. Leverage

Leverage
Shall not exceed 45% of the market value of the real estate

A DIRE is only permitted to borrow funds other than by way of issuing debt securities for the purpose of acquiring Real Estate. The value of such borrowing must not exceed 45% of the value of the real estate to be acquired.

#### f. Profit distribution obligations

Operative income	Timing
90% of its distributable income	Annually

A DIRE shall distribute no less than 90% of its net after-tax profit to all unitholders every year.

In the case where a DIRE uses an SPC to hold its investments, the SPC shall distribute all returns from the investment to the DIRE each year.

#### g. Sanctions

Penalties/loss of status rules
Administrative sanction

With no prejudice to criminal provisions in the Capital Market Field, OJK may impose sanctions on any violation of authorities' rule, as well as on any person that causes the violations to occur. With no prejudice to criminal provisions in the Capital Market field, OJK has the authorisation to impose administrative sanctions, such as:

- a. a written warning;
- b. a fine that is the obligation to pay a certain amount of money;
- c. restrictions on business activities;
- d. suspension of business;
- e. revocation of business license;
- f. cancellation of approval; and
- g. cancellation of registration.

### 3 Tax treatment at the level of REIT

#### Corporate tax/withholding tax/value added tax/duty on the acquisition of land and buildings

##### Acquisition

Generally, DIREs set up SPCs to acquire real estate assets. As such, the seller of the land and/or buildings will transfer its assets to the SPC.

##### *Transfer tax on land and building*

The transfer of the land and buildings will be subject to a 0.5% final tax imposed on the purchase price. This tax will be treated as a tax cost for the seller and cannot be recovered as a tax credit and is not tax-deductible by the seller.

Final tax means that the tax will be imposed on the transfer value once only, at the time of the transaction. Thus, any capital gain or capital loss from the transfer should be excluded from the corporate income tax calculation of the seller.

##### *Transfer of shares*

Where there is a transfer of shares in a company with underlying property to a DIRE, the seller will be subject to tax at a rate of 25% on the capital gain (potentially reduced by any tax losses of the seller), but no final transfer tax should arise.

##### *Value Added Tax (VAT) on the transfer of land/building*

The transfer of land and buildings from a seller to a DIRE is subject to VAT at a rate of 10%. The 10% VAT can be treated as an input VAT by the SPC. In order to be reclaimed as an input VAT, the SPC must be registered as a VAT-able entrepreneur (PKP). Once the real estate asset is leased, the SPC should impose 10% VAT on the rental of the land and building to its customers.

It is highly likely that the input VAT arising on the acquisition of the land and buildings by the SPC will be much higher than any output VAT on the rental activity, resulting in a VAT overpayment. In this case, the SPC can file a refund request to the Indonesian Tax Office (ITO) or carry forward the overpayment to the

following months. A refund request will trigger a tax audit on the SPC, which will take a 12-month period to conclude. However, under the existing tax regulation, the VAT overpayment can be refunded in advance within one month. This is because SPC can be qualified as a low-risk taxpayer.

Please note that under current VAT legislation, registration as a VAT-able company is required if there is a delivery of taxable goods and/or taxable services exceeding IDR 4.8 billion (approx. USD 333,427.20)<sup>3</sup> within a fiscal year. While there is no requirement for a DIRE to provide this level of taxable supplies (i.e. rent), we would expect that this would be the case.

#### *Duty on the acquisition of land and buildings*

Acquisition of land and buildings is subject to a duty on the acquisition of land and buildings (BPHTB) at a maximum of 5%. The BPHTB is charged to the party receiving or obtaining the title to the land and buildings (i.e. the buyer); in this case, the SPC. This duty is applied to the acquisition value or the 'tax value' attributed to the land and buildings, whichever is higher.

#### *Holding period*

Rental income received by the SPC from tenants is subject to a 10%, final income tax under Article 4(2), meaning that the rental income should be excluded from the ordinary income of the SPC. As the rental income is excluded from the ordinary income in the corporate income tax calculation, the expenses incurred (maintenance, service charge, investment manager fee etc.) attributable to the income related to the rental of land and buildings shall be treated as non-deductible expenses in the corporate income tax calculation. The non-deductible expense includes the depreciation of land and buildings, amortisation of the duty on the acquisition of land and buildings and any other relevant costs, such as investment management fees, etc.

The VAT on rents at a rate of 10% will be charged by the SPC to the tenants, which, when received, should be paid to the ITO.

Any payment of management fees to a property manager, investment manager or custodian bank by the SPC or DIRE is subject to 2% Article 23 WHT.

Any dividend payment from the SPC to the DIRE is tax-exempt, thus the dividend income received by the DIRE from the SPC is not subject to corporate income tax at the level of the DIRE.

## Exit taxation

In the event that the DIRE divests of its real estate, this transaction would trigger a transfer of land and building that would be subject to 10% VAT, which would be payable by the purchaser to the DIRE, which would then need to be paid to the ITO, and 2.5% income tax on the gross proceeds (based on Government Regulation No. 34 Year 2016) in the hands of the SPC or DIRE. BPHTB at a rate of 5% will be imposed at the level of the buyer.

Based on the OJK Regulation, the DIRE is required to distribute 90% of its net income after tax to unitholders. There is no more tax on the income distribution received by the unitholder from the DIRE as the income received from the DIRE is exempt from tax under Indonesian income tax law.

### a. Transition regulations

#### Conversion into REIT status

Not applicable

<sup>3</sup> US\$ 1 = IDR 14,393 on 31 May 2019.



## b. Registration duties

Registration duties
Not applicable

# 4 Tax treatment at the shareholder's level

## a. Domestic or Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Distributions tax-exempt	Not subject to taxation	Not applicable

### Corporate shareholder

The distribution of income paid by a DIRE to a domestic corporation or a foreign tax resident is typically tax-exempt.

In practice, any transfer of units of the DIRE between unitholders under closed-ended funds is subject to 0.1% income tax on gross sale proceeds in the hands of the selling unitholders. Under an open-ended DIRE, unitholders are required to sell their units to the asset manager, and the gain is exempt from income tax in the hands of the unitholders. The ITO has not yet issued a specific regulation on this particular transfer of units.

### Individual shareholder

The distribution of income paid by a DIRE to a domestic individual or foreign individual is tax-exempt.

In practice, any transfer of units between unitholders in closed-ended funds is subject to 0.1% final income tax in the hands of the selling unitholders. The ITO has not yet issued a specific regulation on this transfer of units.

### Withholding tax

Not applicable.

## 5 Tax treatment of foreign REIT and its domestic shareholder

Foreign REIT	Corporate unit holder	Individual unit holder
Taxed in Indonesia if income is accrued or derived from Indonesia	25% corporation tax	Up to 30% income tax

### Foreign REIT

Income arising within a foreign REIT will only be taxed in Indonesia if it is accrued in or derived from Indonesia, subject to the provisions of the relevant double tax treaties between Indonesia and the jurisdictions in which the foreign REIT is established.

### Corporate unit holder

Typically, income received by Indonesian tax resident companies is subject to 25% corporate tax. Foreign tax credits can typically be considered in the corporate tax calculation. This analysis may vary depending on the double tax treaty between Indonesia and the jurisdiction of the foreign REIT.

### Individual unit holder

Typically, income received by Indonesian tax resident individuals is subject to up to 30% individual tax. Foreign tax credits can typically be considered in individual tax calculations. This analysis may vary depending on the double tax treaty between Indonesia and the jurisdiction of the foreign REIT. ■

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J-REIT

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A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
J-REIT	2000	Investment Trusts and Investment Corporations Law	Trust or corporate type entities (in practice, only corporate type exist)

## History

Japan's REIT is known as the Japanese Real Estate Investment Trust ('J-REIT'). It was introduced with the amendment to the Investment Trusts and Investment Corporations Law in November 2000 (Investment Trust Law or 'ITL'). The ITL provides for two different types of investment vehicle: 'Investment Trusts' and 'Investment Corporations (toshi hojin)'. All J-REITs have been formed so far as Investment Corporations, and therefore, only this type of structure will be discussed below. The ITL adopts an external management structure for J-REITs, whereby the relevant Investment Corporation is prohibited from having employees and must outsource management by entering into contracts with a registered Asset Management Company, Asset Custodian and General Administrator.

Under the applicable tax law, an Investment Corporation J-REIT is subject to Japanese corporate tax at an effective tax rate of around 35%. However, a J-REIT can deduct dividends distributed to its shareholders from its taxable income if the J-REIT complies with certain requirements under the Japanese Special Taxation Measures Law ('Special Taxation Measures Law') as discussed further below.

The first two J-REITs were listed on the Tokyo Stock Exchange ('TSE') in September 2001, sponsored by two of the largest real estate companies in Japan. The number of listed J-REITs increased, and the J-REIT market expanded significantly until the 2007 global financial crisis. The Tokyo Stock Exchange REIT INDEX ('TSE REIT INDEX') peaked at 2,612.98 on May 1, 2007, and fell to its lowest level at 704.46 on October 1, 2008. The market recovered thereafter, and as of July 1, 2019, the TSE REIT INDEX was at 1951.82 points.

In 2018, two new REITs were listed on the TSE. CRE Logistics Fund J-REIT, Inc., Xymax REIT Investment Corporation, Takara Leben Real Estate Investment Corporation and Itochu Advance Logistics Investment Corporation were listed. During the first quarter of 2019, two new REITs, Escon Japan REIT Investment Corporation and were listed on the TSE.

As a result, 63 J-REITs were listed on the TSE, and the total market capitalisation of J-REITs was around JPY 14.3 trillion as of May 31, 2019.

In 2018, the total amount of assets acquired by all listed J-REITs amounted to JPY 1,778 billion.

Furthermore, the total amount of new J-REIT unit offerings in 2018 was JPY 709 billion.

## Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
Japan	66	36	EUR 118,827	8.23%

## Top five REITs\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield %	% of Global REIT Index
Nippon Building Fund Inc	EUR 8,493	25.31%	2.81%	0.66%
Japan Real Estate Investment Corporation	EUR 7,406	21.68%	2.93%	0.61%
Nomura Real Estate Master Fund	EUR 6,141	16.51%	3.75%	0.51%
Nippon Prologis REIT	EUR 4,750	18.75%	3.55%	0.36%
Japan Retail Fund Investment	EUR 4,652	19.99%	4.06%	0.41%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Building Lots and Building Transactions Agent Licence
- Discretionary Transactions Agent Licence
- Registration of the Asset Management Company with the Financial Services Agency
- Registration of the J-REIT with the Local Finance Bureau

As stated above, J-REITs are typically Investment Corporations that must be managed by an external registered Asset Management Company. As of September 2007, new comprehensive regulations in the form of the Financial Instruments and Exchange Law ('FIEL') came into effect to regulate financial services. Although the regulations under the ITL continue to apply to J-REITs, the FIEL supersedes a part of the ITL with respect to regulating the Asset Management Company of an Investment Corporation.

Under the FIEL, an Asset Management Company must be registered as an Investment Manager. As such, the FIEL replaced the previous approval process with a new registration process. However, this process is relatively similar to the former approval procedures.

The first step for a sponsor of the J-REIT is establishing an asset management company and acquiring a 'Building Lots and Building Transactions Agent Licence' and a 'Discretionary Transaction Agent Licence' from the Local Municipal Government and the Ministry of Land, Infrastructure, Transport and Tourism ('MLIT'), respectively. After these licences are obtained (or at least the application is formally accepted by the MLIT), the Asset Management Company may apply for registration as an Investment Manager with the FSA. The requirements for the Investment Manager registration include a minimum paid-in-capital/net assets of JPY 50 million and having sufficiently experienced personnel, most notably including a compliance officer and a chief investment officer. Once the registration is completed, the registered Asset Management Company can incorporate a J-REIT as a promoter of the Investment Corporation.

After the J-REIT is set up, it must be registered with the Local Finance Bureau in order to commence its business as a J-REIT. The J-REIT will be subject to the reporting and inspection requirements of the FSA, Securities and Exchange Surveillance Commission and the Local Finance Bureau.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Corporation (in practice)	JPY 100 million

### Legal form

A J-REIT must be established as a domestic Investment Corporation in compliance with the ITL. As previously stated, a J-REIT can either be a 'trust type' or a 'corporate type' under the ITL. When the first J-REITs were formed, the trust type was administratively cumbersome and more expensive to establish. In addition, the corporate governance rules applicable to the corporate type J-REIT were considered to be more attractive to investors. As a result, as of June 1, 2019, all current publicly listed J-REITs are Investment Corporations.

### Minimum share capital

J-REIT shares have only one class with voting rights called investment units. The minimum share capital for a J-REIT required under the ITL is JPY 100 million.

## c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- No requirements under the Investment Trust Law (ITL)</li> <li>- Special shareholder conditions in order to deduct dividend distribution under the Special Taxation Measures Law</li> </ul>	No

### Shareholder requirements

There are no shareholder (unit holder) requirements under the ITL. However, for the J-REIT to deduct distributed dividends under the Special Taxation Measures Law, certain specific shareholder (sometimes referred to as common shareholder) conditions must be met.

### Listing requirements

There is no requirement for a J-REIT to be listed on a stock exchange under the ITL or the Special Taxation Measures Law. A number of J-REITs are unlisted.

After J-REITs were introduced under the ITL in 2000, the TSE established the infrastructure for J-REITs to be listed on the TSE in March 2001. The listing requirements for J-REITs include the following:

1. The J-REIT under the ITL must be a close-ended fund;

2. At least 70% of the J-REIT's investment assets must be invested in, or expected to be invested in, real estate assets, including (1) real estate, (2) leasehold rights in real estate, (3) surface rights, (4) easement, and (5) trust beneficiary interests of trusts owning real estate assets; provided that the J-REIT submits prior to approval to its listing certain documents such as copies of the sale and purchase agreements under which the J-REIT would acquire real estate assets;
3. At least 95% of the J-REIT's total assets must be invested, or expected to be invested, in real estate assets, assets relating to real estate assets (e.g. an interest in tokumei kumiai (TK) partnership or shares in an Investment Corporation, which owns more than 50% of its assets in real estate assets), cash and cash equivalents;
4. Net assets and total assets must exceed JPY 1 billion and JPY 5 billion, respectively; and
5. Minimum free-float requirements (at the time of the initial listing):
  - (1). The number of outstanding shares should be 4,000 shares or more;
  - (2). The total number of shares held by the '10 largest J-REIT shareholders' should be 75% or less of the total outstanding shares; and
  - (3). The number of shareholders other than the '10 largest J-REIT shareholders' should be 1,000 or more.

\*The TSE listing rules previously required the real estate assets described in item 2 above to be located in Japan. However, such restriction was removed in the amendments to the TSE listing rules as of May 2008. Accordingly, J-REITs are allowed to invest in foreign real estate, either directly or indirectly through certain special-purpose foreign companies. Regarding 2013-2014 ITL amendment on investments through special-purpose foreign companies, please refer to paragraph 2.4 below.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- Merely an asset holding vehicle
- Investment primarily in 'Qualified Assets'

Under the ITL, a J-REIT is established for investments 'primarily' in 'Qualified Assets'. In principle, a J-REIT is merely an asset holding vehicle; and is not permitted to have employees and is required to outsource asset management, asset custody and general administrative functions to external professionals.

'Qualified Assets' include (1) securities (including typical securities and trust beneficiary interests), (2) derivatives rights, (3) real estate, (4) leasehold rights in real estate, (5) surface rights, (6) promissory notes, (7) monetary claims, (8) interests in a tokumei kumiai (TK) partnership which are not securities, (9) commodities, (10) certain commodities derivatives, (11) renewable energy generating plants, and (12) public facility operation rights. 'Primarily' is interpreted to mean more than 50% of the total assets.

Renewable energy generating facilities and rights to operate public facilities were included in 'Qualified Assets' in 2014 in order to facilitate investments in infrastructure assets. In this connection, the TSE created a new market for listed infrastructure funds in April 2015, and four infrastructure funds were listed on the new market as of June 1, 2019, all of which are focusing on solar renewable energy generating facilities. Please note that listed infrastructure funds have listing, tax and other regimes different from J-REITs in certain material respects.



Under the ITL, a J-REIT cannot own more than 50% of the voting shares of another company. However, an amendment to the ITL was enacted in 2013 which became effective in 2014, making this restriction inapplicable where a J-REIT acquires more than 50% of the voting shares in a company located in a foreign jurisdiction whose sole purpose is to acquire, lease and dispose of real estate in that jurisdiction as long as such company pays the J-REIT certain dividends which are distributable to the J-REIT within six months of the end of each fiscal year of the company under the applicable laws or customs of the jurisdiction. This is provided that the laws of the jurisdiction or customs where the real estate is located or other unavoidable circumstances prohibit the J-REIT from conducting such transactions itself. FSA lists the United States, India, Indonesia, the PRC, Vietnam and Malaysia as examples of such jurisdictions. The TSE and the Investment Trust Association also similarly amended their own rules.

Furthermore, in order to deduct distributed dividends for tax purposes under the Special Taxation Measures Law (see paragraph 3.1B, points f and g below) there is a restriction (i) on owning an interest in 50% or more of another company, and (ii) on owning certain assets, such as renewable energy generating facilities and concessions to operate public facilities, in an amount of 50% or more of the total book value of assets on the J-REIT's balance sheet as of the end of the fiscal period. However, as a result of the amendment to the ITL enacted in 2013, certain foreign companies held by a J-REIT for the limited purposes of acquiring, leasing and disposing of foreign real estate are now excluded from this restriction.

As discussed under paragraph 2.3 above, the listing rules of the TSE also have asset holding requirements (See paragraph 2.3, points 2 and 3).

## e. Financing

### Financing

J-REITs can issue shares and bonds and obtain loans

Under the ITL, there are three methods for J-REITs to procure funding: (1) issuing shares, (2) issuing bonds (Investment Corporation Bonds), which are permitted only by closed-end type J-REITs, and (3) loans from financial institutions. As the framework of J-REITs is primarily intended to enable equity investors to invest in real estate through them, issuing shares is the fundamental funding method, and issuing bonds and loans supplement that, in particular by improving the capital efficiency through leverage.

In order to diversify the funding methods and capital policy of J-REITs, the ITL amendment in 2013 introduced frameworks such as 'Rights offering' and 'Repurchase of its own shares'.

The rights offering is a capital funding method whereby (i) a J-REIT issues share acquisition rights to existing shareholders for no consideration, and (ii) the shareholders subscribe to and purchase such shares in the J-REIT by exercising their rights. The advantages of a rights offering include:

- J-REIT being able to raise capital without diluting existing shareholders' ownership; and
- it can be a relatively feasible funding option under severe economic conditions  
(e.g., unavailability of sufficient credit from financial institutions).

Repurchase by a J-REIT of its own shares was generally prohibited under the original ITL, the amendment to the ITL removed such restriction on the repurchase from shareholders of publicly traded shares of J-REITs which primarily invest in real estate and certain other assets subject to the J-REIT's Articles of Incorporation permitting such repurchase:

- Share repurchasing is thought to be an effective measure for enhancing J-REIT's financial base by improving capital efficiency, among other things.



- In 2017, Invesco Office J-REIT, Inc. was the first J-REIT to conduct such share repurchase. In 2017, Invesco Office J-REIT, Inc. was the first J-REIT to conduct such share repurchase.

## f. Leverage

Leverage
<ul style="list-style-type: none"> <li>- No gearing (LTV) limit under applicable law</li> <li>- May only obtain loans from Qualified Institutional Investors</li> </ul>

Under the ITL, there is no restriction concerning borrowings or gearing ratio. Typically, the J-REIT provides in its financial policy disclosed in the annual securities report a limitation on the gearing ratio (LTV ratio) of approximately 55% to 60% of the ratio of the total assets.

In order to qualify to deduct distributed dividends under the Special Taxation Measures Law, J-REITs may not obtain loans from lenders that are not Institutional Investors. The Institutional Investors for this purpose generally include securities companies, banks, insurance companies, pension funds, etc. However, the scope of such 'Institutional Investors' under the Special Taxation Measures Law is narrower than as provided under the FIEL.

### Profit distribution obligations

Ordinary income	Capital gains	Timing
Greater than 90% of 'distributable profits' under the Special Taxation Measures Law	Same as ordinary income	In relation to the same taxable period

Under the Special Taxation Measures Law, in order for a J-REIT to be permitted to deduct distributed dividends, a number of conditions must be satisfied. One such condition is that a J-REIT is required to make a distribution to its investors of more than 90% of its distributable profits during the same applicable tax period, which is an amount based on accounting profits with certain adjustments. Capital gains are not distinguished from ordinary income for the purpose of satisfying this requirement. Although there is no minimum distribution requirement under the ITL, the ITL requires that a distribution only be made based on the approval of its audited financial statements for the relevant fiscal period approved at a Directors' meeting. The fiscal period of a J-REIT is generally six months (or sometimes one year) and the taxable period of a J-REIT is usually its fiscal period. The shorter fiscal year allows the J-REIT to make distributions more often than once a year.

## g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Regulatory actions</li> <li>- Prohibition on deduction of dividend distributions</li> </ul>

In principle, a J-REIT is created under the ITL and is required to register with the Local Finance Bureau in order to operate its business as a J-REIT. If a J-REIT does not comply with the ITL, a J-REIT may ultimately be required to terminate its J-REIT activities. All activities of a J-REIT are subject to regulatory scrutiny, and any deviation may result in regulatory actions including an order to improve its conduct or the

withdrawal of its registration.

Even if the listing requirements or the dividend deduction requirements are not met, the

J-REIT registration may not be revoked. However, a J-REIT properly operating under the ITL should comply with all listing requirements of the TSE (see paragraph 2.3) in order to continue being listed, and comply with all dividend deduction requirements under the Special Taxation Measures Law in order to deduct its distributed dividends for each relevant taxable period.

### 3 Tax treatment at the REIT level

#### a. Company tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Corporate tax at an effective rate of approximately 35%</li> <li>- Dividends are deductible from taxable income under certain conditions</li> </ul>	Not distinguished from ordinary income	Varies depending on the specific circumstances of the shareholder

#### Ordinary income

Japanese companies are subject to corporate income taxes at an effective rate of approximately 35%. Rental income, business income and capital gains are not distinguished from ordinary income for Japanese corporate tax purposes and are taxed aggregately at the effective tax rates discussed above.

Under the Special Taxation Measures Law, however, a J-REIT is allowed to deduct distributed dividends from its taxable income if all of the following requirements are met. Any remaining taxable income after the deduction of distributed dividends will be subject to regular Japan corporate taxes.

The requirements for deducting dividend distributions are as follows<sup>1</sup>:

##### A. Requirements for an eligible J-REIT:

- a. The J-REIT must be registered under Article 187 of the ITL;
- b. Either of the following conditions must be met:
  - i. There must be a public offering of the J-REIT shares with a total issue price of JPY 100 million or more at the time the J-REIT is established; or
  - ii. The outstanding shares must be owned by at least 50 shareholders or exclusively by Qualified Institutional Investors at the end of the relevant fiscal period.
- c. The Articles of Incorporation provide that more than 50% of the shares must be offered domestically (this requirement is calculated on an aggregated basis for all issuances, including past issuances); and
- d. The J-REIT must have a fiscal period of one year or less.

##### B. Requirements relating to the applicable fiscal year:

- a. The J-REIT must not engage in any business other than asset management, open any place of business other than its head office, or hire any employees;

<sup>1</sup> Article 67-15, the Special Taxation Measurement Law

- b. The asset management function must be outsourced to a qualified asset manager as defined in Article 198 of the ITL;
- c. The custody function for the assets owned by the J-REIT must be outsourced to a qualified custodian as defined in Article 208 of the ITL;
- d. None of the shareholders or its affiliates must collectively hold more than 50% of the outstanding shares or voting rights at the end of the relevant fiscal period;
- e. More than 90% of its ‘distributable profits’ as defined in the Special Taxation Measures Law must be distributed in the same fiscal period (in determining whether this requirement is met certain distributions in excess of retained earnings may be treated as dividends. Further, adjustments to the calculation basis can be made in the changes (increases or decreases) to the reserve for temporary differences arising between tax and accounting treatments as well as for the reserve for negative net asset item adjustments (e.g. deferred hedging losses); these adjustments should help meet this distribution requirement due to differences between the tax and accounting treatments of income or expenses);
- f. The J-REIT must not hold 50% or more of the equity of another company (including another J-REIT), except for certain foreign companies held for the limited purpose of acquiring, leasing and disposing of foreign real estate;
- g. As of the end of the fiscal period, the amount of certain assets as specified under the Enforcement Order of the ITA, such as real estate and related trust certificates except certain renewable energy generating facilities and concessions to operate public facilities, is in excess of 50% of the book value of total assets on the J-REIT’s balance sheet; and
- h. The J-REIT must not have loans from parties other than ‘Institutional Investors’, as defined in the Special Taxation Measures Law.

### Accounting rules

A J-REIT must comply with Japanese accounting rules (J-GAAP) and, as a general principle, can only make dividend distributions from profits calculated based on J-GAAP, although in certain circumstances a J-REIT may be permitted to make a distribution in excess of profits in accordance with special provisions of the ITL.

Neither US-GAAP nor IFRS is allowed for a J-REIT. A J-REIT’s financial statements are prepared on a single-entity basis only since it generally cannot own subsidiaries.

### b. Transition regulations

#### Conversion into REIT status

N/A

### c. Registration duties (and other key taxes)

#### Registration duties (and other key taxes)

- Real property acquisition tax (favourable rate can be applied)
- Registration tax (favourable rate can be applied)
- Consumption tax
- Fixed asset tax and city planning tax

Real property acquisition tax and registration tax are levied on an acquisition of real estate. Such taxes can be reduced under special treatment applicable to J-REITs that can satisfy certain requirements.

The sale of a building is subject to Japanese consumption tax, but the sale of land is not. Additionally, leasing of real estate for commercial purposes is subject to consumption tax, but leasing of residential real estate is not.

Fixed asset tax is levied based upon the government assessed values of the land and buildings owned on January 1 each year. City planning tax may similarly be levied depending on location. Separately identified depreciable fixtures within a building would also be subject to fixed asset tax.

## 4 Tax treatment at the shareholder level

The tax treatments in the domestic shareholders and foreign shareholders sections below relate to listed J-REITs.

### a. Domestic shareholders

	Company shareholders	Individual shareholders	Withholding tax
Dividends	<ul style="list-style-type: none"> <li>- Included in taxable income subject to the standard effective corporate tax rate</li> <li>- Dividend received deduction (DRD) are not applicable</li> <li>- Credit should ordinarily be available for withholding tax on the dividends against the corporate tax liability, with any excess refunded</li> </ul>	<ul style="list-style-type: none"> <li>- In principle, subject to inclusion in taxable income subject to progressive income tax rates; however, taxpayers typically elect to be taxed separately only through withholding tax</li> </ul>	Company shareholder - 15.315% withholding tax (to 2037, and 15% thereafter) Individual shareholder - 20.315% withholding tax (to 2037, and 20% thereafter)
Capital gains from share disposition	Included in taxable income subject to the standard effective corporate tax rate	Subject to taxation separately from other income, to which progressive income tax rates apply, at 20.315% (to 2037, and 20% thereafter)	N/A

## Company shareholders

### Dividends

For company shareholders, dividends from a listed J-REIT are subject to Japanese withholding tax at a tax rate of 15.315% (until 2037 when the rate becomes 15%). Dividend income is aggregated with other income and is subject to tax at the normal effective corporate tax rate of approximately 34.59%. The withholding tax can typically be credited against corporate income tax liability, with any excess amount refunded. Unlike dividends from ordinary Japanese companies, dividends from a J-REIT do not qualify for the dividend received deduction since they are tax-deductible at the J-REIT level.

### Capital gains

Capital gains are not distinguished from ordinary income and are subject to corporate tax at the normal effective corporate tax rate. There is no withholding tax on capital gains arising from the disposition of J-REIT shares.

## Individual shareholders

### Dividends

Although the basic principle is that dividends from a listed J-REIT must be reported in a tax return and aggregated with other types of taxable income, most taxpayers choose to have the dividends taxed separately from ordinary income and have the standard progressive tax rates replaced by the withholding tax as the final tax liability, as described below.

For individual shareholders, dividends from a listed J-REIT are subject to Japanese withholding tax at a rate of 20.315% (until 2037 when the rate becomes 20%). Individual shareholders can elect to have the dividends taxed separately from ordinary income, typically with the final tax liability being the withholding tax. However, individual shareholders owning 3% or more of the total outstanding shares of a J-REIT as of the record date are taxed on the dividends on the standard progressive tax rates together with other income and the withholding tax rate for such taxpayers, which is generally creditable against the final income tax liability, should be 20.42% (until 2037, and 20% thereafter).

### Capital gains

Capital gains from a disposition of listed J-REIT shares through a Japanese securities company is subject to individual income tax separately from ordinary income. The standard rate of 20.315% will apply (until 2037 from when the tax rate becomes 20%). This tax is usually paid by filing a tax return, with certain exceptions for qualified securities account holders, who pay the tax through withholdings from the qualified account.

### Withholding tax

For company shareholders, dividends from a listed J-REIT are subject to withholding tax at the rate of 15.315% (until 2037 when the rate becomes 15%). The withholding tax can typically be credited against the corporate income tax liability, with any excess amount refunded.

For individual shareholders, dividends from a listed J-REIT are subject to withholding tax at the rate of 20.315% (until 2037 when the rate becomes 20%). However, individual shareholders owning 3% or more

of the total outstanding shares of a J-REIT as of the record date are subject to withholding tax at 20.42% until 2037, and 20% thereafter.

## b. Foreign shareholders

This section relates to shareholders who do not have a permanent establishment (PE) in Japan and are not tax residents in Japan. Foreign shareholders with a Japan PE would generally be taxed in a similar manner as discussed in the Domestic shareholder section above.

	Individual shareholder	Withholding tax	
Dividends	Withholding tax is the final levy for foreign company shareholders	Withholding tax is the final levy for foreign individual shareholders	Company shareholder - 15.315% withholding tax (to 2037, and 15% thereafter) - Tax treaties may provide tax some tax relief Individual shareholder - 15.315% withholding tax (to 2037, and 15% thereafter) - Tax treaties may provide some tax relief
Capital gains from share disposition	<ul style="list-style-type: none"> <li>- Taxed in limited cases only for foreign company shareholders</li> <li>- Subject to national corporation taxes at a rate of approximately 24% (see detail below)</li> <li>- Tax treaties may provide some tax relief</li> </ul>	<ul style="list-style-type: none"> <li>- Taxed only in limited cases for foreign individual shareholders</li> <li>- Taxed at 15.315% (until 2037, and 15% thereafter).</li> <li>- Tax treaties may provide some tax relief</li> </ul>	- N/A

## Company shareholders

### Dividends

For foreign company shareholders without a PE in Japan, dividends from a listed J-REIT are subject to a withholding tax at a tax rate of 15.315% (until 2037 when the rate becomes 15%) as the final tax liability. Such shareholders are not subject to Japanese corporate income tax on dividend income. Tax treaties may provide some tax relief.

### Capital gains

Capital gains arising from a disposition of J-REIT shares are not subject to withholding tax. A J-REIT is treated as a Japanese Real Property Holding Corporation ('JRPHC') if at least 50% of its total assets consist of real estate located in Japan, which is typically expected to be the case with a J-REIT. Foreign company shareholders without a PE in Japan are only subject to Japanese corporate tax on the capital gains arising from the disposition of shares of a J-REIT that is a JRPHC if on the day immediately preceding the first day of the fiscal year during which the disposition takes place the disposing

shareholder, together with its affiliates (including a partnership in which the shareholder is a partner) owned more than a certain percentage of the total outstanding shares of the J-REIT. The threshold percentage for listed J-REIT shares is 5%. The disposing shareholder, if taxed, must file a corporate tax return and the rate of tax is 24.2208% (approximately 24%). This rate will be changed to 25.5896% (approximately 26%) for fiscal periods commencing on or after October 1, 2019.

Tax treaties may provide some tax relief.

## Individual shareholders

### Dividends

For foreign individual shareholders without a PE in Japan, dividends from a listed J-REIT are subject to a withholding tax at the rate of 15.315% as the final tax liability (until 2037 when the rate becomes 15%). However, such shareholders who own 3% or more of the total outstanding shares of a listed J-REIT are subject to a 20.42% withholding tax as the final tax liability (up until 2037 and 20% thereafter). Tax treaties may provide some tax relief.

### Capital gains

Foreign individual shareholders without a PE in Japan are subject to tax on capital gains arising from a disposition of J-REIT shares only in limited circumstances, similar to foreign company shareholders (see above). Relevant gains should be subject to individual income tax at the rate of 15.315% (until 2037 and 15% thereafter) and would necessitate the filing of a related income tax return.

Tax treaties may provide some tax relief. ■

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GLOBAL  
REIT SURVEY

ASIA - PACIFIC

# Malaysia

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UNIT TRUST

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction

	Enacted year	Citation	REIT type
Unit trust	<ul style="list-style-type: none"> <li>- The Securities Commission (SC) had issued 'Property Trust Funds' guidelines in 2002, which were superseded by the issuance of REIT guidelines in January 2005</li> <li>- Further updates were issued by way of guidance notes issued in 2005, 2006 and 2007</li> <li>- All of the above were further superseded by the revised guidelines on REITs issued by the SC on August 21, 2008, with subsequent amendments made in 2012</li> <li>- In 2018, the SC issued a new set of guidelines for listed REITs and the existing guidelines on REITs were revised and made applicable to unlisted REITs</li> <li>- The new 2018 guidelines now incorporate the requirements relating to Islamic REITs</li> </ul>	<ul style="list-style-type: none"> <li>- Capital Markets and Services Act, 2007 (CMSA)</li> <li>- SC Guidelines on REITs of 2012</li> <li>- Malaysia Income Tax Act, 1967 (MITA)</li> <li>- SC Guidelines for Islamic REITs of 2005</li> <li>- SC Guidelines on REITs of 2018</li> <li>- SC Guidelines on Listed REITs of 2018</li> </ul>	Trust type

The Real Estate Investment Trust is a part of Malaysian law. Specific REIT guidelines have been issued, and REIT-specific tax provisions have been introduced. The REIT guidelines were amended in 2005, 2006, 2007, 2008, 2011, 2012 and 2018.

Malaysian Islamic REIT:

The Islamic REIT is a collective investment scheme in real estate, by which the unitholders conduct permissible activities according to Sharia Law. Specific Islamic REIT guidelines were issued in 2005, and the new 2018 guidelines on REITs now incorporate the requirements relating to Islamic REITs.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Malaysia	17	3	EUR 6,384	0.15%

## Top REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
IGB Real Estate Investment Trust	EUR 1,438	16.17%	4.77%	0.06%
Pavilion Real Estate Investment Trust	EUR 1,182	8.89%	4.80%	0.03%
Sunway Real Estate Investment Trust	EUR 1,170	11.99%	5.06%	0.06%

\*All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Registered trust
- Trustees must be approved by the SC
- Management company
- Real estate held by the trust must be managed by a qualified property manager
- Appoint a Sharia committee or a Sharia advisor (for Islamic REITs only)

In Malaysia, the establishment and registration of a trust require the approval of the SC. A trustee must be appointed for a REIT, and the appointment of the trustee must also be approved by the SC. Furthermore, the trustee must also be registered with the SC.

The trust must be managed and administered by a management company approved by the SC. The management company (except where the management company is licensed by the SC) must be a subsidiary of (a) a company involved in the financial services industry in Malaysia, (b) a property development company, (c) a property investment holding company or (d) any other institution that the SC may permit.

Foreigners can hold up to 70% of the equity of the management company. At least 30% of the equity of the management company must be held by local (i.e. Malaysian resident) shareholders. As in previous years, a minimum shareholders' reserve of MYR 1 million (approximately USD 0.24 million, based on an exchange rate of MYR 4.1325 to USD 1 in April 2019) must be maintained by the management company at all times.

Real estate held by the REIT must be managed by a qualified property manager who has been approved by the trustees.

### Malaysian Islamic REIT:

Same requirements as above and additionally a Sharia committee or a Sharia advisor must be appointed to ensure that any property acquired by an Islamic REIT is Sharia-compatible.

## b. Legal form/minimum initial capital

Legal form	Minimum share capital
Unit trust	MYR 100 million (approximately USD 24 million, based on an exchange rate of MYR 4.1325 to USD 1 in April 2019)

### Legal form

A REIT takes the form of a unit trust fund. It must be registered in Malaysia and approved by the SC.

### Minimum initial capital

The minimum fund size is MYR 100 million (approximately USD 24 million, based on an exchange rate of MYR 4.1325 to USD 1 in April 2019).

If any trustee member of the REIT is a tax resident in Malaysia in the basis period for a tax year, the REIT will be a tax-resident person for Double Taxation Treaty purposes. There is uncertainty as to whether a distribution from a REIT would fall under the dividend article, business profit article or the other income article. Pending the amendment to existing Double Taxation Treaty to be in line with OECD's proposal on REIT's distribution, the REIT's distribution is likely to be categorised as 'other income' unless the non-resident recipient can demonstrate otherwise (e.g. business profits).

## c. Unit holder requirements/listing requirements

Unit holder requirements	Listing mandatory
No requirements	No

### Unit holder requirements

There are no requirements.

There is no restriction on foreign unitholders in the REIT, but foreigners cannot hold more than 70% of the equity in the REIT's management company.

### Listing requirements

A REIT can be either listed or unlisted. A REIT seeking to list its units must comply with the listing requirements, as detailed in chapter 4 of the Bursa Malaysia Securities Berhad (LR) and chapter 12 of the 2018 REIT guidelines for listed REITs. These requirements include the following:

- The initial size of a REIT proposing a primary listing on the Main Market of Bursa Securities must be at least RM500 million;
- The applicant must have at least 25% of the total number of units for which listing is sought in the hands of a minimum number of 1,000 public unitholders holding not less than 100 units each;
- For the purpose of calculating the required minimum public holding, holdings by the management company, its directors and any person connected with such a management company or directors shall be disregarded;

- The applicant must ensure that at least two directors or one-third (or the nearest number) of the board of directors of the applicant, whichever is higher, are independent directors; and
- The management company of the REIT is subject to the SC's approval and a prospectus of the public offering is to be issued and registered with the SC. Subsequently, an application is to be made with Bursa (the Malaysian Stock Exchange) for a listing of and quotation for the units.

#### d. Asset levels/activity test

##### Restrictions on activities/investments

- Restriction applies on the level of investments
- Additional restrictions for Islamic REITs

#### Non-Listed REIT

A non-listed REIT may only invest in the following:

- real estate;
- single-purpose companies (a 'single purpose company' means an unlisted company whose principal assets comprise of real estate);
- real estate related assets;
- non-real estate related assets; and
- cash, deposits and money market instruments.

At least 50% of the non-listed REIT's total asset value must be invested in real estate and/or single-purpose companies investing in real estate at all times.

A non-listed REIT's investment in non-real estate-related assets and/or cash, deposits and money market instruments must not exceed 25% of a REIT's total asset value.

A non-listed REIT is not permitted to conduct the following activities:

- advancing of loans, financing facilities or any other credit facility;
- property development; and
- acquisition of vacant land.

#### Listed REIT

A listed REIT may only invest in the following:

- real estate;
- non-real estate related assets; and
- cash, deposits and money market instruments.

At least 75% of a listed REIT's total asset value must be invested in real estate that generates recurrent rental income at all times.

A listed REIT is not permitted to conduct the following activities:

- (a) advancing of loans or any other credit facility; and
- (b) acquisition of vacant land (except for the purpose of property development activities).

All REITs may invest in real estate-related assets and non-real estate-related assets, and these assets may consist of foreign investments traded in or under the rules of a foreign market (a market where the regulatory authority is a member of the International Organisation of Securities Commissions (IOSCO)).

### Malaysian Islamic REIT:

Further restrictions apply to the Islamic REIT. Islamic REITs are permitted to acquire real estate for the purpose of various activities. However, the fund manager must ensure that the rental income from non-permissible activities under Sharia Law is less than 20% of the total turnover of the Islamic REIT.

Further, an Islamic REIT must reduce the percentage of the Shariah Non-Compliant Rental from less than the 20% Threshold to less than 5% of the Islamic REIT's total turnover (the 5% Threshold) by the end of the 10th financial year post listing.

The Islamic REIT cannot accept new projects which are composed of fully non-permissible activities or purchase existing projects which are composed of non-permissible activities.

Non-qualifying/permissible rental activities are financial services that are based on *riba* (interest). Such activities include gambling/gaming, the manufacture or sales of non-halal products or related products, conventional insurance, entertainment activities that are non-permissible according to the Sharia, the manufacture or sale of tobacco-based products or related products, stock brokerage or share trading in Sharia non-compatible securities and other activities deemed non-compliant according to Sharia.

### e. Leverage

#### Leverage

Borrowing may not exceed 50% of the total asset value

The basic rule is that the total borrowings may not exceed 50% of the total asset value of the fund unless authorised by the unitholders by way of an ordinary resolution.

A Malaysian REIT can only borrow from institutions that are licensed (or deemed to be licensed) under the Financial Services Act 2013 and Islamic Financial Services Act 2013. It can also issue debentures.

### f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of total income	N/A	Annually

## Operative income

Malaysian REITs are not required to make any minimum distribution of income, but REITs will only benefit from a tax exemption provided at least 90% of their total income for the year of assessment is distributed to its investors. Effective year of assessment 2017, such exemption only applies to REITs that are listed on Bursa Malaysia.

There is no requirement in the MITA for capital gains to be distributed every year. The 90% threshold applies to the total income of the REIT. Total income refers to the income of a REIT that would ordinarily be chargeable to tax. It should be noted that there is no capital gains tax in Malaysia, except for real property gains tax (RPGT) for disposal of real properties and shares in real property companies. With effect from January 1, 2019, the RPGT rates for disposals by a REIT are between 10% and 30% depending on the length of the holding period of the real properties or shares in real property companies as follows:

Date of disposal	RPGT rates
Within 3 years from the date of acquisition	-30%
In the 4th year	-20%
In the 5th year	-15%
In the 6th year and subsequent years	-10%

## g. Sanctions

Penalties/loss of status rules
Various sanctions possible, including revocation of approval

Where a person breaches the provisions of the CMSA or fails to comply with, observe, enforce or give effect to any written notice, guidelines issued or conditions imposed by the SC, the SC may take one or more of the following actions:

- Direct the person in breach to comply with, observe, enforce or give effect to such rules, provisions, written notice, condition or guideline;
- Impose a penalty in proportion to the severity or gravity of the breach but in any event not exceeding MYR 500,000 (approx. USD 121,000, based on an exchange rate of MYR 4.1325 to USD 1 in April 2019);
- Reprimand the person in breach;
- Require the person in breach to take such steps as the SC may direct to remedy the breach or to mitigate the effect of such breach, including making restitution to any other person aggrieved by such breach; or
- any other actions in accordance with the CMSA.

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/Services Tax/WHT

Current income	Capital gains	Withholding tax (WHT)	Sales tax & service tax (SST)
Tax-exempt if 90% of the total income is distributed	Not taxable except for RPGT for disposal of real properties and shares in real property companies	<ul style="list-style-type: none"> <li>- Creditable for taxable income</li> <li>- Not refundable for non-taxable income</li> </ul>	<ul style="list-style-type: none"> <li>- Income from the leasing of real properties and disposal of real properties is not subject to services tax</li> </ul>

#### Current income

REITs listed on Bursa Malaysia will not be taxed on their income, provided that at least 90% of their total income for the year of assessment is distributed to its unitholders. For Malaysian WHT purposes, it is a requirement for the REIT to withhold a portion of the distribution at the applicable rate (see below) and to distribute the net amount to the unitholder. If the REIT is subject to income taxes on its total income, the amount distributed is taxable in the hands of unitholders as if it was received gross. However, the investors are eligible to claim tax credits.

A corporate tax deduction on start-up expenses incurred during REIT establishment (e.g. consultancy, legal and valuation fees) is available.

With effect from the 2008 year of assessment<sup>1</sup>, a company disposing of an industrial building (on which capital allowances have been claimed previously) to REITs will not be subject to balancing adjustments while REITs would continue to claim capital allowances on such buildings based on the residual expenditure of the building in the tax returns of the seller. With effect from the 2013 year of assessment, these rules will only be applicable to a company which holds greater than the 50% of the residual profits (i.e. profits after-tax depreciation) of the REITs available for distribution, or greater than 50% of any residual assets (assets after depreciation) of the REITs available for distribution on a winding up.

#### Capital gains

With effect from January 1, 2019, gains from the disposal of real properties and shares in real property companies by a REIT are subject to RPGT between 10% and 30% depending on the holding period of the real properties or shares in real property companies as follows:

Date of disposal	RPGT rates
Within 3 years from the date of acquisition	-30%
In the 4th year	-20%
In the 5th year	-15%
In the 6th year and subsequent years	-10%

<sup>1</sup> The year of assessment or effective year of assessment refers to the tax year. The tax year follows the company's or REIT's accounting period.

## Tax suffered at source on dividend income

Malaysia does not levy dividend withholding taxes.

With effect from January 1, 2014, all companies are on the single-tier tax system. Under this system, tax paid on profits of a company is a final tax and dividends distributed by a company into which the REIT invests (usually a minority interest) are exempt in the hands of the REIT.

If an overseas jurisdiction levies a withholding tax, the REIT will not be able to obtain credit for such tax if the income is exempt in Malaysia. If, however, the income is taxable, it may be possible for the REIT to claim a credit in respect of the foreign tax suffered.

## Accounting rules

The financial statement of a REIT shall be prepared in accordance with applicable approved accounting standards (FRS), applicable statutory requirements, the deed and any regulatory requirements.

## Indirect taxes

The GST regime was repealed on August 31, 2018, and has been replaced with a sales tax and a service tax (“SST”) which both came into effect from September 1, 2018. Sales tax is imposed on goods manufactured in Malaysia whereas service tax is imposed on taxable services which are prescribed in the service tax legislation.

Service tax is charged and levied on any taxable service provided by a registered person in carrying on his business or any imported taxable service. The rate of service tax is 6%.

The list of taxable persons and taxable services are specifically prescribed in the First Schedule of the Service Tax Regulations 2018 (‘the Regulations’).

Leasing of real properties and disposal of real properties and shares in real property companies by a REIT are not taxable services prescribed in the Regulations. Accordingly, these activities are not subject to service tax.

### b. Transition regulations

#### Conversion to REIT status

N/A

### c. Registration duties

#### Registration duties

Stamp duty exemption

There is a stamp duty exemption on the transfer of properties to an approved REIT. Other than stamp duty, there are currently no other duties/taxes imposed on the transfer of properties in Malaysia to a REIT.

SST does not apply to the transfer of properties (unlike the GST regime).



## 4 Tax treatment of the unit holder's level

### a. Domestic unit holder

Corporate unitholder	Individual unitholder	Withholding tax	GST
<ul style="list-style-type: none"> <li>- Income not taxed at REIT level: 18% (17% from the year of assessment 2019 onwards)/24% income tax on distributions; no tax credit is available</li> <li>- Income taxed at REIT level: 18% (17% from the year of assessment 2019 onwards)/24% income tax on distributions; however, tax credits are available</li> <li>- No capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- Income not taxed at REIT level: final withholding tax levy at a rate of 10% applies from January 1, 2016 to December 31, 2019; no tax credit is available</li> <li>- Income taxed at REIT level: 0-28% income tax (prevailing rates for the year of assessment 2016) on gross income from REIT distributions in the hands of individual unitholders; such income carries a tax credit</li> <li>- No capital gains tax</li> </ul>	<ul style="list-style-type: none"> <li>- No withholding tax levied on distributions to Malaysian resident corporate unitholders</li> <li>- Withholding tax applies to Malaysian resident individual unitholders at 10% if the income was not previously taxed at the REIT level</li> </ul>	<ul style="list-style-type: none"> <li>- Distribution received from a REIT is not subject to service tax</li> </ul>

### Corporate unit holder

Distribution from income on which the REIT is exempt from tax:

Income distributed from the REIT will be taxed at the prevailing corporate tax rate of 24%. A preferential tax rate of 18% (17% from the year of assessment 2019 onwards) on the first MYR 500,000 of chargeable income will apply if the corporate unitholder is a 'Small and Medium Enterprise' ('SME') for the purposes of the MITA.

With effect from the year of assessment 2009, the definition of an SME has been re-defined as a company resident in Malaysia that has paid-up ordinary share capital of MYR 2.5 million or less at the beginning of the basis period of a year of assessment provided:

- (i) Not more than 50% of the paid-up ordinary share capital of the corporate unitholder is directly or indirectly owned by a non-SME;
- (ii) The corporate unitholder does not own directly or indirectly more than 50% of the paid-up ordinary share capital of a non-SME; and
- (iii) Not more than 50% of the paid-up ordinary share capital of the corporate unitholder is owned by a company that also owns more than 50% of the ordinary share capital of a non-SME.

No tax credit is available to the unitholder where the distribution of income from the REIT is exempt from tax.

Distribution from income on which the REIT has been taxed (i.e. where the relevant conditions have not been met):

The amount distributed from the REIT will be grossed up to take into account the tax already paid at the REIT level and the corporate unitholder will be taxed on the gross distribution at the prevailing corporate tax rate of 24%. However, such distributions carry a tax credit in respect of tax chargeable to the REIT in relation to the distributed income, which is available to be offset against the income tax chargeable to the corporate unitholder on the grossed-up amount of the distributed income.

## Capital gains tax

There is no capital gains tax in Malaysia, except for RPGT for disposals of real properties or shares in real property companies. Disposal of REIT units, however, will not be subject to RPGT.

## Individual unit holder

Distribution from income on which the REIT is exempt from tax:

Distributions made by a REIT to individual unitholders are subject to a final withholding tax of 10% (this rate applies to the period from January 1, 2016 to December 31, 2019). Individual unitholders who receive the net amount distributed need not account for any further income tax liability.

Distribution from income on which the REIT has been taxed:

The amount distributed from the REIT will be grossed up to take into account the underlying tax of the REIT and the individual unitholder will be taxed on the gross distribution at progressive tax rates ranging from 0% to 28% (prevailing rate for the year of assessment 2017).

Such distributions carry a tax credit, which will be available to offset against the tax chargeable on the individual unitholder.

## Capital gains tax

There is no capital gains tax in Malaysia, except for RPGT for disposals of real properties or shares in real property companies. Disposal of REIT units, however, will not be subject to RPGT.

## Withholding tax

A REIT does not need to withhold tax when making distributions to a resident company; such companies would need to declare the REIT distributions as taxable income, and the income will be taxed at the prevailing corporate tax rate of 24%.

For resident individuals, a 10% withholding tax is applicable if the amount distributed was tax-exempt at the REIT level.

Effective December 30, 2017, a person can apply for a refund with respect to the WHT on income distributed by the REIT if such person is exempt from tax.

## Indirect taxes

The investor/unitholder is entitled to receive distributions from their investment in the REIT. The distribution income is not subject to SST.

The issue, holding and redemption of units under a trust fund, and, the transfer of ownership of securities is not subject to service tax. Provision of services relating to financial services for the use or provision of brokering is subject to service tax at 6%.

## b. Foreign unit holder

Corporate unit holder	Individual unit holder	Withholding tax
<ul style="list-style-type: none"> <li>- Withholding tax at 24% effective from January 1, 2016</li> <li>- Withholding tax at 10% for institutional investors from January 1, 2016 to December 31, 2019, if a distribution from income on which the REIT is exempt from tax</li> </ul>	Withholding tax at 10% from January 1, 2016 to December 31, 2019, if a distribution from income on which the REIT is exempt from tax	No specific relief available

### Corporate unit holder

Distribution from income on which the REIT is exempt from tax:

Distributions to non-resident companies are subject to withholding tax of 24% from January 1, 2016 onwards.

Distributions to non-resident institutional unitholders are subject to a final withholding tax of 10% (this rate applies to the period from January 1, 2016 to December 31, 2019).

Distribution from income on which the REIT has been taxed:

**Non-resident companies:** A non-resident company would only be required to file a tax return in Malaysia if the company has a taxable presence/permanent establishment (as defined under the relevant double tax treaty) in Malaysia. Where the non-resident company is obligated to file a Malaysian tax return, the amount distributed from the REIT will be grossed up to take into account the underlying tax of the REIT, and the non-resident company will be taxed on the gross distribution at the prevailing corporate tax rate of 24%, with a tax credit given on the underlying tax of the REIT.

If the non-resident company has no obligation to file a Malaysian tax return (i.e. there is no permanent establishment/taxable presence), the non-resident company will receive any distributions net of the tax suffered by the REIT. The non-resident company will also not be entitled to the tax credit from the income distributed from the REIT.

No withholding tax would be imposed on the non-resident company on income from the REIT that has been taxed previously.

**Non-resident institutional unitholders:** An institutional investor is defined as 'a pension fund, collective investment scheme or other such persons approved by the Minister'. A non-resident institutional unitholder would only be required to file a tax return in Malaysia if the unitholder has a taxable presence/permanent establishment (as defined under the relevant double tax treaty) in Malaysia. Where the non-resident institutional unitholder is required to file a Malaysian tax return, the amount distributed from the REIT will be grossed up to take into account the underlying tax of the REIT, and the non-resident institutional unitholder will be taxed on the gross distribution at the appropriate tax rate, with a tax credit given on the underlying tax of the REIT.

If the non-resident institutional unitholder has no obligation to file a Malaysian tax return, the non-resident institutional unitholders will receive any distributions net of the 24% corporate tax. The non-resident will also not be entitled to the tax credit from the income distributed from the REIT.

No withholding tax would be imposed on the non-resident institutional unitholder on income from the REIT which has been taxed previously.

## Individual unit holder

Distribution from income on which the REIT is exempt from tax:

Distributions to non-resident individuals are subject to a final withholding tax of 10% (this rate applies to the period from January 1, 2016 to December 31, 2019).

Distribution from income on which the REIT has been taxed:

The amount distributed from the REIT will be grossed up to take into account the underlying tax of the REIT, and the non-resident individual unitholder will be taxed on the gross distribution at 28% (prevailing rate from the year of assessment 2016 onwards) if their tax returns are filed in Malaysia. Where the non-resident individual does not file a tax return, he will not be entitled to the tax credit from the income distributed from the REIT.

## Withholding tax

If withholding tax is levied, such tax will be a final tax for Malaysian purposes. As such, unitholders receiving the net amount distributed need not account for any further income tax liability in Malaysia.

Effective December 30, 2017, a person can apply for a refund with respect to the WHT on income distributed by the REIT if such person is exempt from tax.

No specific relief is available under tax treaties. However, depending on the practice of the receiving country, treaty protection may be sought under general unilateral double-taxation elimination rules.

## 5 Tax treatment of the foreign REIT and its domestic unit holder

Foreign REIT	Corporate unitholder	Individual unitholder	SST
Taxation subject to Double Tax Treaty	Tax-exempt	Tax-exempt	Distribution received from a foreign REIT is not subject to service tax

### Foreign REIT

The income of the foreign REIT will only be taxed in Malaysia if it is accrued in or derived from Malaysia, subject to the provisions of the relevant double tax treaties between Malaysia and the jurisdictions in which the foreign REIT is established.

### Corporate unitholder

Distributions received from foreign REITs would be regarded as foreign-sourced income and exempt from Malaysian tax pursuant to Paragraph 28, Schedule 6 of the Malaysian Income Tax Act, 1967 unless the recipient is a resident company carrying on the business of banking, insurance, or sea or air transport.

### Individual unitholder

Same as corporate unitholders. ■

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# New Zealand

UNIT TRUST and PIE

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
- Unit trust	2007	- The Trustee Act 1956	- Trust type
- Portfolio Investment Entity ('PIE')	2007	- Companies Act 1993 - Income Tax Act 2007 - Financial Markets Conduct Act 2013	- Corporate type - (shows some characteristics of a REIT)

New Zealand does not have any specific REIT regime, and it is not expected that any such specific regime will be introduced in the near future. Some unit trusts and companies investing in real property interests and meeting the eligibility criteria may elect to enter the 'Portfolio Investment Entity' (PIE) regime. As noted below, income derived by a PIE may be able to be allocated to individuals and taxed once at the PIE level for some New Zealand resident individual investors, at a prescribed investor rate between 10.5% and 28%, with no further New Zealand tax on distribution.

The primary aim of the PIE regime is to provide an income tax treatment for New Zealand resident individuals investing through collective investment vehicles, which is similar to the treatment which would apply if they invested directly. To this end, PIEs disposing of certain Australasian shares will not be taxed on those proceeds, and net taxable income allocated to New Zealand resident individual investors will generally be taxed at the PIE level at rates reflecting, or lower, than their marginal personal tax rates with no further tax on allocation of other gains or on distribution.

Unlisted PIEs can also elect to be 'foreign investment PIEs'. The aim of these rules is to achieve New Zealand tax costs for non-resident investors in unlisted PIEs that would not exceed the New Zealand tax costs if they invested directly, including a possible zero tax cost in respect of a PIE's foreign-sourced income. To qualify for these rules, elections must be made by PIEs to be 'foreign investment PIEs' and by investors to be 'notified foreign investors'. Both types of 'foreign investment PIE' may invest in overseas land, but not in New Zealand land, although 'foreign investment variable-rate PIEs' may hold limited interests in New Zealand companies which own New Zealand land.

Unit trusts are sometimes used for investing in real property (as well as for other investments), particularly (but not necessarily) where funding is sought from the public. There is no minimum or maximum limitation on the type of asset held by a unit trust or on the amount invested. Discretionary trusts may be used but are more appropriate for private investments and would not be used where funds are sought from the public.

Trusts are created under New Zealand's trust law and are generally regulated by the terms of the trust deed. The Trustee Act 1956 applies to all trusts, while the Financial Markets Conduct Act 2013 applies where units in a unit trust are offered to the public.

Overseas Investment Office consent may be required for overseas investors in New Zealand land or other assets. Overseas companies carrying on business in New Zealand are required to register with the New Zealand Companies Office and must comply with annual return filing and financial statement and audit requirements.

## Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
New Zealand	6	1	EUR 4,514	0.12%

## Top REIT\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield	% of Global REIT Index
Kiwi Property Group	EUR 1,352	27.49%	6%	0.12%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Registration of the trust with the Registrar of Companies
- Issue of a registered prospectus

Unit trusts are generally established by means of an initial settlement on terms expressed in a trust deed. Where units in a unit trust are offered to the public, the Financial Markets Conduct Act 2013 requires registration of the trust deed with the Registrar of Companies and issue of a registered investment statement and prospectus. The trust must have a corporate manager, which deals with investors and manages the trust's investments, and a trustee, who must not be under the same control as the manager. The trustee and manager may also be subject to Financial Markets Authority oversight and may need to register and comply with other legislation affecting financial advisers and service providers.

Some companies and unit trusts investing in real property interests and meeting the eligibility criteria are able to elect to enter the PIE regime. No specific licence or approval is required to enter the PIE regime, but the entity must meet the various statutory criteria as to investors' rights to investment proceeds, the number and type of investors, the extent of each investor's interests, and the types of investment and income.

### b. Legal form/minimum initial capital

Legal form	Minimum share capital
<ul style="list-style-type: none"> <li>- Unit trust or company</li> <li>- Portfolio Investment Entity (PIEs)</li> </ul>	No



## Legal form

Unit trusts or companies investing in real property interests.

PIEs may be New Zealand resident companies or unit trusts, superannuation funds (superannuation schemes registered with the Government Actuary under the Financial Markets Conduct Act 2013 or under the KiwiSaver legislation), group investment funds (established under the Public Trustee or Trustee Companies legislation) or certain life insurance funds.

## Minimum share capital

There is no minimum or maximum limitation on the amount of capital for a company, unit trust or a PIE.

### c. Unit holder requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- No restrictions for unit trusts or companies which are not PIEs</li> <li>- Restrictions apply to the number and type of investor/unitholder in a PIE</li> </ul>	No

No restrictions apply for unit trusts or companies that are not PIEs.

## Unit holder requirements for PIEs

- If the entity is not listed on the NZ Stock Exchange, the portfolio investor class must generally include one or more of the following:  
at least 20 non-associated persons, none of whom holds more than 20% of the total portfolio investor interests in the class;
- a PIE or a foreign PIE equivalent investment vehicle;
- an entity which would meet the PIE criteria but has not elected to become a PIE;
- a life insurer;
- the NZ Superannuation Fund;
- the Accident Compensation Corporation or a Crown entity subsidiary of same;
- the Earthquake Commission;
- a 'public unit trust' if it has at least 100-unitholders (whose interests do not exceed 25% each or who are unit trust managers) or if it can otherwise be regarded as 'widely held' or if its units are held by widely-held investment vehicles.

Unlisted unit trusts with at least 100 members, which meet certain 'public unit trust' criteria or are otherwise considered to be 'widely held', and certain superannuation funds may not need to meet the above specific criteria.

If the entity is listed on the NZ Stock Exchange, all the following investor criteria must be met:

- the entity must not have more than one portfolio investor class;
- each investor must be a member of that class; and
- each portfolio investor interest must be a share/unit traded on the stock exchange.

The general 20% maximum holding for investors was initially extended to 40% for certain institutional investors where the entity was a listed company or unit trust and no maximum limit applied to such investors where the entity was not a listed company or unit trust. A transitional provision protected PIE eligibility where interests of between 20% and 40% in a listed company or unit trust had been held since May 17, 2006. Subsequent amendments have removed the 40% maximum limit for those institutional investors with retrospective effect from the 2008-09 income year. Further amendments also allow tax-exempt charities to hold more than 20% interests (from August 29, 2011).

## Listing requirements

The NZ Stock Exchange Listing requirements apply if shares or units are to be traded on the stock exchange.

Some PIE eligibility criteria vary according to whether or not the entity is listed. The taxation of income allocated to NZ resident individual investors at the investors' prescribed investor rates applies only where the PIE is not an NZ-listed company or unit trust.

### d. Asset level/activity test

#### Restrictions on activities/investments

- No limitations if not PIEs
- Diverse thresholds for PIEs

No limits apply to the activities or investments of unit trusts or companies which are not PIEs.

At least 90% of the value of a PIE's assets must be one or more of the following:

- land;
- financial arrangements (such as debts and debt-type instruments);
- excepted financial arrangements (such as shares and units in unit trusts); or
- rights or options over the above types of assets.

At least 90% of the income derived by a PIE must be derived from the above types of property and must consist of any one or more of the following:

- dividends (or equivalent payments under certain share-lending arrangements);
- financial arrangement accrual income (including interest and related premiums and foreign exchange variations);
- rent (from non-associated parties);
- property disposal proceeds;
- income under the 'foreign investment fund' (FIF) rules;
- allocated PIE income; or
- distributions from superannuation funds.

The above rules are modified for 'foreign investment PIEs' to the effect that neither 'foreign investment zero-rate PIEs' nor 'foreign investment variable-rate PIEs' may invest in, or derive income from, interests

in New Zealand land, although ‘foreign investment variable-rate PIEs’ may hold limited interests in New Zealand companies which own New Zealand land. Virtually all income of ‘foreign investment zero-rate PIEs’ must be sourced outside New Zealand, with only minimal amounts of certain types of New Zealand-sourced income allowed.

Investments by the PIE in shares in a company or units in a unit trust must generally:

- carry voting interests of no more than 20% in a company or have a market value of no more than 20% of the total market value of the units in a unit trust; or
- where the PIE’s interest exceeds 20%, the total market value of that and all the PIE’s other investments of more than 20% in companies or unit trusts must not exceed 10% of the total market value of all the PIE’s investments.

The 20% interest or 10% investment value limitation does not apply to investments by the PIE in any of the following:

- another PIE;
- a foreign PIE equivalent investment vehicle;
- an entity that meets the PIE criteria but has not elected PIE status;
- a land investment company (a company or unit trust which is not a PIE and which owns land (directly or indirectly through another company) representing at least 90% of the market value of all the land investment company’s property for certain periods during the relevant income year).

An entity carrying on a business of life insurance is not eligible to be a PIE except in respect of separate identifiable funds holding investments which are subject to life insurance policies where the policy benefits are directly linked to the value of the funds’ investments.

An entity will not be eligible to be a PIE if it is NZ resident under New Zealand’s domestic income tax legislation but is regarded as not being NZ resident under the provisions of a double tax treaty.

Where a listed company or unit trust is a PIE, it must apply the maximum imputation (franking) credits available to all distributions.

If an entity has previously ceased being a PIE, it cannot elect to be a PIE again until at least five years have passed.

## e. Leverage

### Leverage

No specific restriction

There are generally no restrictions on debt levels for entities investing in real property, other than:

- The need for arm’s length terms where any related party debt is provided;
- Possible thin capitalisation limitations for interest (and related foreign exchange) deductions if a single overseas person (together with associates) holds (directly or indirectly) or controls at least 50% of the New Zealand company or unit trust (for these purposes, the ‘safe harbour’ New Zealand group debt percentage is 60%)<sup>1</sup>; and

<sup>1</sup> Recently enacted legislation extends the scope of the thin capitalisation rules from April 1, 2015 and also the calculation of the thin capitalisation percentage from July 1, 2018.

- For trusts other than unit trusts, there must be sufficient connection between the borrowings and the derivation, or possible derivation, of New Zealand taxable income

There are also possible thin capitalisation limitations for interest (and related foreign exchange) deductions for New Zealand resident entities which hold (directly or indirectly) or control an income interest of at least 10% in a 'controlled foreign company' (which may include a foreign unit trust). These thin capitalisation limitations extend to New Zealand residents with income interests of at least 10% in certain 'foreign investment funds' (foreign companies or unit trusts) which are subject to the active income or Australian exemptions from the attribution of their income.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
No requirement but taxation of income not allocated	No requirement	Annually

##### Operative income

Unlisted PIEs will allocate taxable income to investors. If taxable income is not allocated to investors for each period, it will be taxed at the PIE's tax rate. Distributions of income by unlisted PIEs are not taxable to investors while distributions by listed PIEs may be fully or partly taxable to some investors.

##### Capital gains

Unlisted PIEs are able to allocate capital gains to investors without a tax cost on allocation or subsequent distribution. Distributions of capital gains by listed PIEs may be fully or partly taxable to some investors to the extent any imputation credits are attached.

#### g. Sanctions

Penalties/loss of status rules
Loss of PIE status and loss of PIE tax treatment

If an entity loses PIE status, the income tax treatment of its disposals of certain Australasian shares would generally become taxable again, income would initially be taxed at the company or unit trust level and rate, distributions to New Zealand resident individual investors would revert to being fully taxable at their marginal tax rates and distributions to non-residents could be subject to non-resident withholding tax.

## 3 Unit trust tax treatment

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Subject to the standard corporate tax rate (28%)	Gains may be taxable depending on circumstances	Generally subject to a resident withholding tax of 33%, reduced by the amount of imputation (franking); credits attached

## Current income

Unit trusts treated as companies for income tax purposes are subject to income tax at the standard corporate rate (28%) and, if solely tax resident in New Zealand, are subject to the imputation (franking) regime, whereby they can pass the benefit of income tax paid to unitholders by attaching imputation credits to distributions.

For trusts other than unit trusts, the trustees are subject to tax at 33% on income that is not paid, applied to or vested in beneficiaries on a current year basis. The extent to which income from non-New Zealand sources is taxable in New Zealand generally depends on complex rules relating to the residence of settlors or deemed settlors of such trusts. Where trusts meet certain ('complying trust') criteria (including being liable to full New Zealand income tax on all income flowing through the trust which is not treated as current year beneficiary income), no further New Zealand income tax or withholding tax will apply to subsequent distributions of retained earnings or capital gains.

PIEs which are listed companies or unit trusts will be taxed on all taxable income at 28%.

PIEs (other than listed companies or unit trusts) will allocate their taxable income to investors and account for tax at an investor's elected rate of either 28%, 17.5%, 10.5% or 0%. For investors who have notified the correct tax rate to the PIE, the tax paid by the PIE on their behalf will be a final tax and represents a favourable tax treatment for New Zealand resident individual investors with a marginal personal tax rate of 33%. The PIE regime is also intended to remove effective over taxation for individuals investing through companies or unit trusts where their marginal personal tax rate is less than the current corporate or unit trust tax rate of 28%.

As noted above, reduced tax rates (between 28% and 0%) may apply to income attributed to non-resident investors who are 'notified foreign investors' in unlisted PIEs which elect to be 'foreign investment PIEs' (see section 1).

For New Zealand income tax purposes, companies, unit trusts and PIEs generally recognise rental or other business income on an accrual basis and dividends on a cash basis. Income (and expenditure) relating to debt instruments and other debt-type financial arrangements is subject to specific rules which generally require recognition on an accrual basis and treat all related gains (whether of an income or capital nature) as taxable although not all losses on such financial arrangements may be deductible.

No tax depreciation can be claimed on most buildings from the beginning of taxpayers' 2011-2012 income years. Tax depreciation can continue to be claimed on commercial building 'fit out' items (but not on dwelling 'fit out' that is part of a building).

New Zealand resident entities may generally claim credits against their New Zealand income tax liabilities for foreign income taxes paid on foreign-sourced income up to the amount of New Zealand income tax payable on the particular income. Excess foreign tax credits cannot be refunded or carried forward or back to any other income year. Unlisted PIEs may utilise foreign tax credits in determining the tax payable at the PIE level on income allocated to investors. Investors in such PIEs may be able to utilise foreign tax credits allocated to them if they are directly taxable on their allocated PIE income (see section 4).

## Capital gains

While New Zealand has no specific capital gains tax, gains on disposal of property interests can be taxable in a number of situations specified in the income tax legislation. The circumstances when personal property interests, such as shares or units in unit trusts, may be treated as 'revenue account property' for income tax purposes, with disposal proceeds treated as taxable income, are outlined in section 4 below. Disposals of direct interests in land can be taxable in a wider range of circumstances, also including, for example, certain situations where subdivisions or other developments are carried out, or where zoning or resource management matters arising since acquisition contribute to profit, or where the vendor was associated with entities carrying on business as land dealers, developers or builders at the time the land was acquired.

## Withholding tax

Distributions received by New Zealand resident companies or unit trusts from other New Zealand resident companies or unit trusts are generally subject to a resident withholding tax of 33%, reduced by the amount of imputation (franking) credits attached. Such withholding tax is deducted on account of the recipient's annual income tax liability and is not a final tax. It may be refunded if there is an excess of tax paid over the recipient's net income tax liability on an annual return basis. Imputation (franking) credits cannot be refunded in cash, however.

From 1 April 2017, a fully imputed dividend, paid from one New Zealand company to another, is not liable for resident withholding tax if the company paying the dividend chooses not to deduct resident withholding tax.

In certain circumstances, taxpayers may obtain resident withholding tax exemption certificates from Inland Revenue so that no withholding tax needs to be deducted, although the dividends may still be taxable on an annual return basis.

No resident withholding tax would apply to dividends where the New Zealand companies or unit trusts are regarded as tax group companies, that is, broadly, where they are at least 66% commonly owned, although the dividends would still be taxable on an annual return basis unless the companies or unit trusts are 100% commonly owned.

Where the New Zealand companies or unit trusts are 100% commonly owned, dividends between them will generally be totally exempt from income tax and no withholding tax will apply.

Where PIEs receive dividends from other New Zealand companies or unit trusts, credits for resident withholding tax deducted and imputation credits may be utilised in determining the tax payable at the PIE level or, in certain circumstances relating to unlisted PIEs, may be allocated to investors or rebated to the PIE.

For dividends received by foreign entities from New Zealand companies or unit trusts, please refer to the comments in section 4.2.

For dividends received by New Zealand resident companies or unit trusts from foreign REITs, please refer to the comments under the 'Corporate shareholders' heading in section 5.

## Other taxes

The Goods and Services Tax (GST) treatment of investment trusts and related costs needs to be considered and managed. This tax is a VAT. GST may apply to transfers or other supplies of goods (which may include land) and services in New Zealand at the standard rate of 15%, although sales of tenanted commercial properties may be zero-rated in certain circumstances and supplies of domestic dwellings may be exempt from GST. Certain supplies between GST-registered parties, which consist wholly or partly of land, are generally zero-rated for GST purposes if the recipients are acquiring the land for use in making GST-taxable supplies and not for use as their (or certain relatives') principal place of residence. In such circumstances, the recipients (rather than the suppliers) will generally be liable to account for any GST at the standard 15% rate if it turns out that the supplies should not have been zero-rated.

Initial GST input tax claims must generally be based on the proportion of a taxpayer's estimated GST-taxable use compared with GST-exempt or other use, rather than on the previous principal purpose basis.

GST issues should be considered before any structures are established or land transactions are entered into in order to ensure that they can be managed appropriately.

## Accounting rules

Companies and unit trusts which offer units to the public are generally subject to the accounting requirements of the Financial Reporting Act 1993 and are generally required to apply NZ International Financial Reporting Standards (NZ IFRS).

## Tax residence and double tax treaties

Companies, unit trusts and PIEs that are New Zealand tax resident under domestic law will generally be regarded as New Zealand residents under New Zealand's double tax treaties. The ability of non-resident REITs to invoke and apply New Zealand's double tax treaties in respect of any New Zealand-sourced income may depend on their legal structure, their tax status in their home jurisdictions and the wording of particular treaties.

### b. Transition regulations

#### Conversion to PIE status

Deemed disposal and re-acquisition of certain Australasian share investments at market value immediately before the PIE election is effective

A PIE will be taxable at the general corporate/unit trust rate of 28% on taxable gains arising from the deemed disposal of certain Australasian share investments at market value immediately before its election to become a PIE is effective. The PIE may spread the resulting tax liability evenly over three years, and will not be liable for provisional tax penalties or tax interest charges in respect of that liability.

### c. Registration duties

#### Registration duties

None

No stamp duties, transfer taxes or other levies apply on the acquisition of land in New Zealand or where an entity elects to become a PIE.

## 4 Tax treatment at the unit holder's level

### a. Domestic unit holder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Distributions of companies and unit trusts taxed at the normal income tax rate</li> <li>- Distribution of a PIE: allocated PIE income taxed at normal income tax rate, with no tax on distributions from unlisted PIEs</li> <li>- Distributions from listed company or unit trust PIEs may be taxable dividends to the extent imputation, or foreign dividend payment credits are attached</li> <li>- Disposals not taxable unless units held on revenue account</li> <li>- Taxable disposals taxed at the normal income tax rate</li> </ul>	<ul style="list-style-type: none"> <li>- Distributions of companies and unit trusts are taxed at the normal income tax rate</li> <li>- Distribution of an unlisted PIE: Allocated PIE income is taxed at a 10.5%, 17.5% or 28% final tax with no tax on distributions</li> <li>- Distributions from listed PIEs are not taxable unless NZ resident individual or trustee taxpayers elect to treat as taxable</li> <li>- Disposals are not taxable unless units are held on a revenue account</li> <li>- Taxable disposals taxed at the normal income tax rate</li> </ul>	<p>Up to 33% on distributions, reduced by imputation credits attached</p>

### Corporate unit holder

Distributions from companies and unit trusts are generally treated as dividends for New Zealand income tax purposes, with no distinction between distributions representing current income and distributions representing capital gains. On liquidation, certain distributions of realised and unrealised capital gains to resident corporate unitholders may be excluded from being dividends.

In certain circumstances, amounts distributed as returns of share or unit capital or on buybacks of shares or units may be excluded from treatment as dividends, and thus be free of New Zealand income tax.

Corporate investors in unlisted PIEs will be required to include their allocated PIE income in their own returns and account for tax themselves at the relevant rate applicable to their net taxable income from all sources. PIE distributions will not be taxed to New Zealand corporate investors except to the extent that the distributions are fully imputed or foreign dividend payment credited dividends from NZ-listed companies or unit trusts. Corporate PIE investors may offset taxable PIE income allocations or distributions against tax losses from other sources.

Disposals of units held in companies, unit trusts or PIEs by resident corporates are not taxable unless they constitute 'revenue account property'. Shares or units may be 'revenue account property' if the holder is a trader or dealer in such types of property, if the holder has acquired the specific shares or units for the dominant purpose of disposal, or if acquisition and disposal of the shares or units is part of carrying on or carrying out a profit-making undertaking or scheme. Any gains which are taxable on this basis are taxed at the standard corporate rate (28%).

### Individual unit holder

Distributions from companies and unit trusts are generally treated as dividends for New Zealand income tax purposes, with no distinction between distributions representing current income and distributions representing capital gains. On liquidation, certain distributions of realised and unrealised capital gains to individual unitholders may be excluded from being dividends.



In certain circumstances, amounts distributed as returns of share or unit capital or on buybacks of shares or units may be excluded from treatment as dividends and thus be free of New Zealand income tax.

Distributions from listed PIEs to New Zealand resident individual or trustee holders are not taxable unless those holders choose to treat them as taxable dividends (for example, if the imputation or foreign dividend payment credits attached would exceed their personal income tax liability). Allocations of income by unlisted PIEs to New Zealand resident individual holders will not be taxed further where the PIE income has been allocated and taxed at the appropriate prescribed investor rate at the PIE level. Distributions from unlisted PIEs are not taxable.

As described above, disposals of units held in companies, unit trusts or PIEs by resident individuals are not taxable unless they constitute ‘revenue account property’. Any gains which are taxable on this basis are taxed at individuals’ normal income tax rates.

## Withholding tax

Dividend distributions from New Zealand companies or unit trusts to resident investors are generally subject to 33% withholding tax, reduced to the extent imputation (franking) credits are attached. However, a company paying a dividend to another company may choose not to deduct resident withholding tax if the dividend is fully imputed. Such withholding tax (but not the imputation credits) may be refunded if the recipient’s annual tax liability is less than the tax deducted on their behalf. No withholding tax applies to dividends from PIEs to resident investors.

### b. Foreign unit holder

Corporate unit holder	Individual unit holder	Withholding tax
<ul style="list-style-type: none"> <li>- A 28% tax rate on unlisted PIE allocations</li> <li>- A 0% tax rate on allocations to ‘notified foreign investors’ by ‘foreign investment zero-rate PIEs’</li> <li>- Tax rates of between 28% and 0% on allocations to ‘notified foreign investors’ by ‘foreign investment variable-rate PIEs’</li> <li>- A 28% tax rate on taxable disposals</li> <li>- Disposals are not taxable unless units held on a revenue account</li> </ul>	<ul style="list-style-type: none"> <li>- A 28% tax rate on unlisted PIE allocations</li> <li>- A 0% tax rate on allocations to ‘notified foreign investors’ by ‘foreign investment zero-rate PIEs’</li> <li>- Tax rates of between 28% and 0% on allocations to ‘notified foreign investors’ by ‘foreign investment variable-rate PIEs’.</li> <li>- Disposals are not taxable unless units held on a revenue account</li> <li>- Taxable disposals are taxed at normal individual income tax rates</li> </ul>	<ul style="list-style-type: none"> <li>- In principle, a 30% withholding tax on distributions, reduced to 15% to the extent imputation (franking) or similar credits are attached</li> <li>- A 0% if fully imputed distributions are paid to a foreign unitholder who holds at least 10% voting interest or who holds lesser interest, but tax treaty reduces New Zealand tax rate below 15%</li> <li>- Tax treaty relief may be available for distributions and disposals</li> </ul>

### Corporate unit holder

Distributions from New Zealand companies and unit trusts to non-resident corporate investors are generally treated as dividends for New Zealand income tax purposes and subject to non-resident withholding tax (NRWT), regardless of whether the distributions represent current income or capital gains. On liquidation, certain distributions of realised and unrealised capital gains to non-resident corporate holders may be excluded from being dividends unless they hold or can acquire or control at least 50% of the company or unit trust.

In certain circumstances, amounts distributed as returns of share or unit capital or on buybacks of shares or units may be excluded from treatment as dividends and may thus be free of New Zealand income tax for all non-resident corporate holders.

Where an unlisted company or unit trust is eligible for and elects to be a PIE, as noted above, non-resident investors will have a 28% tax rate applied by such PIEs to their allocated income. Actual distributions by unlisted PIEs will not generally be taxed further.

Lower tax rates (between 28% and 0%) may apply to income allocated by ‘foreign variable-rate PIEs’ to ‘notified foreign investors’, the rates depending on the combination of types and sources of the PIE’s income for the period. A zero tax rate may apply to income allocated by ‘foreign investment zero-rate PIEs’ to ‘notified foreign investors’. If ‘foreign investment PIEs’ derive partly imputed (franked) dividends from New Zealand resident companies, they may choose to deduct NRWT on distributions to ‘notified foreign investors’ which represent the unimputed (unfranked) amounts, instead of paying tax for them on an attributed income basis.

Distributions by New Zealand listed PIEs to non-resident corporate investors are intended to be treated as dividends, subject to withholding tax and potentially supplemented under the supplementary dividend tax credit (SDTC) regime to the extent imputation or foreign dividend payment credits are attached. The SDTC provisions do not apply if dividends are paid to non-residents with voting interests of at least 10% or if a tax treaty reduces the New Zealand tax rate below 15%. No further New Zealand income tax or withholding tax applies to any excesses over the dividend amounts which are distributed by New Zealand listed PIEs.

As described above, disposals of units held in New Zealand companies, unit trusts or PIEs by non-resident corporate holders are not taxable unless they constitute ‘revenue account property’. Any New Zealand-sourced gains which are taxable on this basis are taxed at the standard corporate rate (28%, unless an applicable double tax treaty provides relief from New Zealand income tax).

Investments in companies or unit trusts holding real property interests may be treated as real property interests themselves under some of New Zealand’s double tax treaties.

Income tax exemptions for overseas venture capital investors on the sale of units do not apply where the underlying New Zealand investments involve owning or developing real property.

## Individual unit holder

Distributions from New Zealand companies and unit trusts to non-resident individual investors are generally treated as dividends for New Zealand income tax purposes and subject to non-resident withholding tax. No distinction is drawn between distributions representing current income and distributions representing capital gains. On liquidation, certain distributions of realised and unrealised capital gains to non-resident individuals may be excluded from being dividends, regardless of their level of ownership or control.

In certain circumstances, amounts distributed as returns of share or unit capital or on buybacks of shares or units may be excluded from treatment as dividends and may thus be free of New Zealand income tax for all non-resident individual holders.

Where an unlisted company or unit trust is eligible for and elects to be a PIE, as noted above, non-resident investors will have a 28% tax rate applied by such PIEs to their allocated income. Actual distributions by unlisted PIEs will not generally be taxed further.

Lower tax rates may apply to income allocated by ‘foreign variable-rate PIEs’ to ‘notified foreign investors’, the rates depending on the combination of types and sources of the PIE’s income for the period. A zero tax rate may apply to income allocated by ‘foreign investment zero-rate PIEs’ to ‘notified foreign investors’. If ‘foreign investment PIEs’ derive partly imputed (franked) dividends from New Zealand

resident companies, they may choose to deduct NRWT on distributions to ‘notified foreign investors’ which represent the unimputed (unfranked) amounts, instead of paying tax for them on an attributed income basis.

Distributions by New Zealand listed PIEs to non-resident individual investors are intended to be treated as dividends, subject to withholding tax and potentially supplemented under the SDTC regime, to the extent imputation or foreign dividend payment credits are attached. No further New Zealand income tax or withholding tax applies to any excesses over the dividend amounts which are distributed by New Zealand listed PIEs.

As described above, disposals of units held in New Zealand companies, unit trusts or PIEs by non-resident individuals are not taxable unless they constitute ‘revenue account property’. Any New Zealand-sourced gains which are taxable on this basis are taxed at normal individual income tax rates unless an applicable double tax treaty provides relief from New Zealand income tax.

Investments in companies or unit trusts holding real property interests may be treated as real property interests themselves under some of New Zealand’s double tax treaties.

## Withholding tax

‘Non-resident withholding tax’ (NRWT) is deductible from dividends (including distributions from unit trusts) at 30%, unless:

- limited by an applicable double tax treaty, (typically to 15% or potentially to 0% in some situations); or
- imputation (franking) or similar credits are attached to the dividend, in which case the NRWT rate is reduced to 15% to the extent the dividend is so credited.

NRWT may be at a zero rate if fully imputed (franked) non-cash dividends, such as certain bonus issues (if allowed by the terms of the trust deed), are made. A 0% NRWT rate also applies to fully imputed cash dividends paid to non-residents who hold voting interests of at least 10% or who hold lesser interests, but a tax treaty reduces the New Zealand tax rate below 15%. The cost of NRWT can be offset by credits arising under New Zealand’s SDTC regime.

Non-resident investors need to consider their ability to claim foreign tax credits in their home jurisdiction for NRWT deducted, particularly where a New Zealand company or unit trust pays supplementary dividends to non-residents under the SDTC regime.

Where an unlisted company or unit trust is eligible for and elects to be a PIE, as noted above, non-resident investors will have a 28% tax rate applied by such PIEs to their allocated income and no withholding or other income tax will generally apply to distributions from such PIEs to non-residents. As noted above, ‘foreign investment PIEs’ which derive partly imputed (franked) dividends from New Zealand resident companies may elect to apply NRWT to distributions to ‘notified foreign investors’ which represent the unimputed (unfranked) amounts, instead of paying tax on an attributed income basis.

Any actual distributions to non-resident investors by listed PIEs are intended to be subject to NRWT only to the extent imputation (franking) or similar credits are attached.

## 5 Tax treatment of foreign REITs and their domestic unit holders

Foreign REITs	Corporate unit holder	Individual unit holder
<ul style="list-style-type: none"> <li>- 28% Corporate tax</li> <li>- Treaty relief might apply</li> </ul>	May be taxable under CFC or FIF regime	May be taxable under CFC or FIF regime

### Foreign REITs

Overseas Investment Office consent may be required for overseas investors in New Zealand for purchase of land or other assets. Overseas companies carrying on business in New Zealand are required to register with the New Zealand Companies Office and must comply with annual return filing and financial statement and audit requirements. These may vary based on the size of the company's operations overseas and in New Zealand.

Where units in a unit trust are offered to the public:

- The Financial Markets Conduct Act 2013 regulates structural matters and requires (i) a management company to manage the investments and issue units and (ii) a trustee company (which is not controlled by the same persons who control the management company) to hold legal title to the assets;
- Specific legislation regulates the offering of units to the public, prospectus and related requirements;
- The Financial Reporting Act 1993 regulates accounting and audit requirements; and
- The NZ Stock Exchange Listing requirements apply if units are to be traded on the stock exchange;

The trustee and manager may also be subject to Financial Markets Authority oversight and may need to register and comply with other legislation affecting financial advisers and service providers.

New Zealand sourced rentals or business income will be taxable under New Zealand domestic law at the basic corporate income tax rate of 28%, subject to any limitation by an applicable double tax treaty.

Subject to any double tax treaty limitations, New Zealand sourced dividends, interest or royalties paid to non-residents are generally subject to non-resident withholding tax at the basic rates of 30% for dividends (reduced to 15% to the extent imputed (franked), to 0% if the dividend is a fully imputed non-cash dividend or a fully imputed cash dividend paid to non-residents with at least 10% voting interest or to those with lesser interests if a tax treaty reduces their New Zealand tax rate below 15%), 15% for interest (a minimum tax unless the parties are not associated) and royalties (a minimum tax).

### Corporate unit holder

Depending on the extent of New Zealand ownership of a non-resident REIT which is a company or unit trust, New Zealand corporate holders may be taxable on attributed income under New Zealand's 'controlled foreign company' (CFC) or 'foreign investment fund' (FIF) regimes.

New Zealand resident corporate unitholders are generally exempt from New Zealand income tax on distributions received from non-resident companies or unit trusts if they hold at least 10% income interests and the distributions do not relate to fixed-rate foreign equity and are not deductible (directly or indirectly) outside New Zealand, apart from certain Australian investments. Investments in non-resident companies or unit trusts of greater than 10% may potentially be taxable under the FIF or CFC regimes depending on the underlying activity of the non-resident company. Fixed-rate foreign equity and deductible foreign distributions are taxable on receipt or crediting. If the income interests held by a New Zealand resident corporate are less than 10%, distributions will be taxable on receipt or crediting if the interests fall within certain FIF regime exemptions.

## Individual unit holder

If the non-resident REIT falls within New Zealand's definition of a company or unit trust for tax purposes, individual New Zealand resident holders would generally be taxable on any distributions at their marginal personal tax rates, regardless of the source of the REIT's income.

Depending on the extent of New Zealand ownership of the non-resident REIT, individual New Zealand holders may be taxable on attributed income under New Zealand's CFC or FIF regimes. Where the individual is taxable in respect of the investment under the FIF regime, the treatment of distributions and any foreign withholding tax will depend on the particular method applied to calculate the FIF income. ■

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REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type	REIT market
Pakistan REITs	September 12, 2007, and then April 16, 2015, then December 4, 2018	<ul style="list-style-type: none"> <li>- Pakistan – Companies Act, 2017 (Repealed Companies Ordinance, 1984 ['Co Ord'])</li> <li>- Real Estate Investment Trust Regulations, 2015</li> </ul>	<ul style="list-style-type: none"> <li>- Developmental.</li> <li>- Rental REIT</li> <li>- Hybrid</li> </ul>	As per the report published by SECP on February 28, 2019, Four Real Estate Investment Trust Management Company has already been operated in the market with the total assets of PKR 5.67 billion

The Federal Government issued a notification vide SRO 1073(I)/2007 dated September 12, 2007 ['Notification'], under sub-clause (viii) of clause (a) of section 282A of the repealed Companies Ordinance 1984, (saving are provided to these section as per section 509 of Companies Act, 2017) notifying that real estate investment trust management services to be carried-out by Non-Banking Finance Companies ['NBFC'].

NBFCs, including Real Estate Investment Trust ['REIT'], are regulated directly by the Securities and Exchange Commission of Pakistan ['SECP'] under Part VIII A of the Companies Ordinance, 1984, now Companies Act, 2017, which adopts section 282A to 282N mutatis mutandis from the Companies Ordinance, 1984 as mentioned in section 509 of the Companies Act, 2017 for the promotion of the real estate sector.

As a consequence of the notification read with sub-section (2) of section 282B of the Co Ord, SECP had promulgated the Real Estate Investment Trust Regulations 2008 ['Regulations 2008'] vide S.R.O. 94(I)/2008 dated January 31, 2008, in 2015, SECP has introduced a new regulatory framework, thus repealing 2008 Regulations replacing it by notifying Real Estate Investment Trust Regulations 2015 to vide S.R.O. 328(I)/2015 dated April 16, 2015 ['Regulations'] for the regulation of REIT Management Companies ['RMC']; and registration and regulation of Real Estate Investment Trust schemes ['REIT scheme'] and matters connected thereto. These regulation issued on April 16, 2015, subsequently be amended to vide notification S.R.O. 1473 (I)/2018 dated December 4, 2018.

The salient features of the regulations are:

- The paid-up capital requirement of REIT Management Companies (RMCs) has been brought down from PKR 200 million to PKR 50 million;
- The minimum fund size requirement of PKR 2 billion has been reduced to bring it in-line with the listing regulations of stock exchanges<sup>1</sup>;
- The minimum stake of RMC or through an arrangement with Strategic Investors in a REIT scheme has been stipulated to 25% through recent amendments, and each strategic investor shall hold not less than 5% in a REIT scheme;
- Simplification of the approval process and allowing a performance fee for REIT managers;
- A criterion for a rental track record has been prescribed for REIT eligible properties;
- Through the recent amendment, a new chapter under the regulation has been introduced regarding the appointment of trustees;

<sup>1</sup> Presently under chapter IV regulation 7(1) of the Karachi Stock Exchange's Listing Regulations, the minimum capital requirement for getting company listed is 200 million. Other stock exchanges in the country may have different threshold.



- The dividend to the unitholders shall be paid in cash;
- The limit of the performance fee, in the case of a Developmental REIT scheme, has been extended to 20% from 15%.

The RMC launches REIT schemes, which are registered under the scheme of these regulations. These REIT schemes are close-ended trusts with tax treatment similar to that of mutual funds in Pakistan in terms of tax exemptions.

### Sector summary\*

Listing country	Number of REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
Pakistan	1	0	EUR 123	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- License application to the SECP
- Incorporation of NBFC
- Appointment of a trustee & property valuer in accordance with the regulations

The following is the graphical summary of events for the incorporation of an NBFC leading to the establishment of an RMC and the registration of a REIT scheme.

#### Obtaining permission to form a NBFC

- For the purposes of seeking permission to form NBFC, application is required to be filed with Specialized Companies Division (SECP) alongwith the following documents:
  - Form I of NBFC Rules 2003 along with all relevant supporting documents;
  - Fee as per Schedule III of REIT Regulations 2015; and
- Compliance to Fit and Proper Criteria of REIT Regulations 2015, along with all relevant supporting documents.

#### Permission Granted by SECP

- Incorporation of NBFC as a public limited company at the Company Registration Office ['CRO'] as per the prescribed procedures, forms and fees.



Upon receipt of license granted by the CRO

- Application to the Company Registration Office [‘CRO’] for Grant of License to carry out REIT Management Service being an NBFC along with the following:
  - form II of NBFC Rules 2003 along with all relevant supporting documents and
  - the fee as per Schedule III of REIT Regulations 2015.

License Granted by SECP

- SECP grant the license to established REIT Management Company (RMC).

## b. The RMC

Subsequent to obtaining a license, a REIT Management Company is incorporated as a public limited company under the Companies Act, 2017 (Repealed Companies Ordinance, 1984).

NBFC/RMC must commence its business within one year from the date of issuance of the license – as is specified in sub-rule (3) of rule 6 of the NBFC (Establishment and Regulations) Rules 2003.

The RMC must maintain adequate financial, technical, procedural, organisational, human resources, internal controls, compliance procedures and prepare accounts in conformity with the International Accounting Standards (IAS).

The RMC shall make a public offering of at least 25% of units of the REITs scheme.

The promoters<sup>2</sup> of an RMC must have at least 25% of the paid-up share capital, and should not withdraw their investment without prior approval of the SECP and must be kept unencumbered.

## c. Conditions applicable to RMC

The conditions which are applicable to RMC, inter alia, are:

- The minimum paid-up capital, at the time of applying for a license as an NBFC, should at least be PKR 50 million and submit evidence that it has equity of at least PKR 50 million.
- Promoters, proposed directors and Key Executives satisfy the prescribed fit and proper criteria;
- In the case of the Developmental REIT, the proposed construction period should not be more than five years, and the same shall be part of the business plan, offering document and all relevant marketing material;
- The RMC shall:
  - (i) obtain and submit to the SECP, a due diligence certificate, from a lawyer who is amongst the panel of lawyers approved for the said purposes by the Commission, expressly confirming that:
    - a. the title of the real estate which is the subject matter of the REIT scheme is free from all legal disputes with respect to title and no case is pending on any account including outstanding dues, duties, taxes, or permissible use before any court or authority;
    - b. the real estate is not in conflict with any applicable environmental laws and all approvals/No objection etc. in this respect is duly procured, and the real estate is not protected as a special and heritage property;

<sup>2</sup> refers to a person (as defined by the NBFC’s Rules) who has made an application to the SECP to form a REIT management company under the proposed Rule-4

- c. the real estate is free from all encroachments and encumbrances except for charges created by any Financial Institution(s) as defined in the Ordinance. Provided that the outstanding amount of loan against real estate including principal and interest does not exceed 40% of the value of the real estate as determined by the concerned Financial Institution(s);
  - d. the legal opinion with respect to the validity and legitimacy of terms and conditions governing the transferability, duration, continuation, cancellation of the underlying lease arrangement and legitimacy of the lease agreements with tenants of the real estate, wherever relevant; and
  - e. all necessary approvals, permissions, NOCs of the concerned local authorities required as per applicable general, special and local laws have been obtained, as specifically may apply to a REIT scheme.
- (ii) provide an affidavit on a stamp paper confirming that RMC has reviewed the land record with the relevant custodian of the land and that the title of the real estate is clear, no dues are outstanding with respect to the real estate, that no injunction orders have been passed against the proposed real estate by any legal forum;
  - (iii) provide, for leasehold real estate, documentary proof confirming that the remaining validity of the lease period is not less than 15 years over and above the life of the proposed REIT scheme and where the life of the scheme has not been proposed the remaining lease period shall not be less than 30 years;
  - (iv) submit an undertaking confirming that there is no litigation and encroachment related to the real estate;
  - (v) submit the confirmation issued by the concerned authorities including the revenue authorities that no injunction orders have been passed against the proposed real estate;
  - (vi) submit an undertaking to retire the full outstanding debt against the real estate before transferring real estate in the name of the trustee of the REIT scheme;
  - (vii) submit to the Commission the details of charges created by Financial Institution(s) against real estate along with loan repayment schedule as agreed with the lenders;
  - (viii) submit copies of title documents, permissions, NOCs of the concerned local authorities required as per applicable general, special and local laws;
  - (ix) submit to the Commission, such other documents or information as may be required by the Commission, on a case to case basis; and
  - (x) propose trustee of the REIT scheme who fulfils eligibility criteria as specified in these regulations along with its consent.

#### d. Registration of REIT scheme

After RMC is established, the SECP may on an application, if it is satisfied, register the proposed REIT scheme, the prerequisites to the application are:

- Obtain approval from the SECP in respect of: the real estate which is to be transferred to the proposed REIT scheme; a) the name of the REIT scheme; b) appointment of a trustee; c) Valuation Report of the real estate; d) business plan of the REIT scheme; e) the draft Trust Deed.

The REIT scheme should at least have a fund size of in line with listing requirements of the stock exchange which is presently under chapter V regulation 5.2 of the Pakistan Stock Exchange's Listing Regulations, the minimum capital requirement for getting company listed is PKR 200 million.

- In the case of a Developmental REIT scheme:
  - ensure that a binding purchase agreement has been executed for transfer of title of the real estate in the name of the trustee of a REIT scheme; and
  - have obtained all requisite approvals from the concerned authorities to carry out the Project and the Lawyer's opinion, who is amongst the panel of lawyers approved by the Commission, shall confirm the same.
- In the case of a Rental REIT Scheme:
  - ensure that a binding purchase agreement has been executed for the transfer of title of the real estate in the name of the trustee of a REIT scheme;
  - ensure that all requisite approvals from the concerned authorities including the completion certificate have been obtained, all dues are clear, and the real estate does not have any defect which may render it ineligible for rent or subsequent;
  - sale by the REIT scheme and the Lawyer's opinion, who is amongst the panel of lawyers approved by the commission, shall confirm the same;
  - ensure that the real estate: (i) has at least last twelve months' successful tenant occupancy record, backed by signed lease agreements and verifiable from a bank statement and books of accounts wherever applicable, (ii) has at least 80 per cent tenant occupancy at the time of application and (iii) provide all relevant documents including tenant lease agreements, if required by SECP.
- If the RMC intends to convert a Developmental REIT scheme into a Rental REIT scheme, the RMC shall submit the revised Business Plan duly approved by the unitholders through a special resolution as defined in the Ordinance. obtain a due diligence certificate from a lawyer that the real estate is vested in the trustee free from defects and encumbrances.

Upon complying with the prerequisites, supra, the RMC will submit an application for the registration of a proposed REIT scheme to the SECP along with the prerequisite documents, named above, and other appendages referred to in regulation 9 of the regulations.

The SECP may register the proposed REIT scheme if it is satisfied that prescribed conditions in the regulations have duly been fulfilled.

#### e. Legal form – the REIT scheme

The REIT scheme is a closed-end trust, and the trustees whereof should not be connected persons, associated companies or associated undertakings of the RMC.

All REIT assets are to be held by the trustee on behalf of the unitholders. All real estate and other assets of the REIT scheme should be acquired in the name of the trustee. A trustee and property valuer must be appointed with the prior approval of SECP for every REIT scheme. The real estate management company shall appoint a property valuer with the consent of the trustees.

A trustee of a REIT scheme may be a scheduled bank, development financial institution having a long-term rating of 'AA-' by a credit rating agency, a subsidiary of a scheduled bank, a foreign bank, a central depository company or any other person as the SECP may notify from time-to-time.

Trust deeds should be in accordance with Schedule I of the regulations, and provide for the time and modality of the extinguishment of the REIT scheme and the manner in which proportionate shares of the sale proceeds shall be transferred to its unitholders.

## f. The fees

### Management fee

The RMC will be entitled to receive an annual management fee:

	Annual Management Fee not exceeding
• Development REIT scheme	1% to 3% of the initial REIT fund based on fund size
• Rental REIT scheme	3% of the annual operating income of the REIT scheme
• Hybrid REIT scheme	A combination of development and rental portions proportionally

### Annual monitoring fee

Annual Monitoring Fee to be paid annually to the SECP for the life of the REIT Scheme as under:

	Annual Management Fee not exceeding
• Development REIT scheme	0.2% of the initial REIT fund
• Rental REIT scheme	0.1% of the initial REIT Fund
• Hybrid REIT scheme	Combination of development and rental portions proportionally

### trustee fee

	trustee's Fee not exceeding
• Development REIT Scheme	0.2% of the initial REIT fund
• Rental REIT Scheme	0.6% of the annual operating income of the REIT Scheme
• Hybrid REIT Scheme	Combination of development and rental portions proportionally

### Fee to quality assurance manager or property manager

Fee as negotiated by the RMC.

## g. Unit holder requirements/listing requirements

Unit holder requirements	Listing mandatory
None	Yes

The maximum number of units that may be subscribed by investors through the Initial Public Offering [IPO] shall not exceed 5% of the REIT fund.

### Listing requirements

The RMC must apply to list units of the REIT fund on the stock exchange(s). The units of the REIT fund should be listed in accordance with the listing regulations of the relevant stock exchange(s) and should be freely tradable.

- The units of the REIT scheme shall be listed on the stock exchange(s);
- No units can be offered to the public unless offering document has been cleared by stock exchange(s) and approved by the SECP;
- RMC shall hold minimum 5% and Strategic Investor, collectively or individually, shall hold minimum 20% cent units of the REIT scheme in an account marked as blocked throughout the life of the REIT scheme until its winding up, and these units shall not be sold, transferred or encumbered;
- The RMC after the publication of three audited financial statements of the REIT scheme demonstrating acceptable performance may apply to the Commission for the transfer of its holdings to a Strategic Investor;
- In the case, there are more than one Strategic Investors, each one of them shall hold not less than 5% units of the REIT scheme at all times. Provided that the strategic investor may, after five years of the launch of REIT scheme, transfer their holding of the REIT scheme to another Strategic Investor with the approval of the Commission; and
- The par value of each unit shall be PKR 10.

### h. Asset level/activity test

#### Restrictions on activities/investments

- Investments should only be made in real estate
- Restriction on transferring ownership of controlling shares, merger and take-over
- Restriction on obtaining management of another REIT scheme
- Investment in vacant land for development purposes is allowed
- Restriction on investing in unlisted securities and commodities

### Restriction on activities

A REIT Management Company – which manages the assets of a trust – shall only invest in real estate; however; it may invest any surplus funds in government securities or keep such funds as a deposit with scheduled commercial banks having not less than ‘AA (double A)’ long-term rating with a stable outlook.

A REIT Management Company is not allowed to acquire management of another REIT scheme without prior approval from the SECP. Similarly, it is not allowed to transfer ownership of controlling shares, merge with, acquire or take-over any other company unless received prior approval from the SECP.

The REIT funds or REIT assets shall not be used directly or indirectly for:

- lending or making an advance not connected to objects or furtherance of the REIT scheme;
- acquiring any asset that involves the assumption of any liability that is unlimited;

- affecting a short sale in any security;
- purchasing any asset in a forward contract;
- purchasing any asset on margin;
- participating in a joint account with others in any transaction;
- trading in commodities or becoming involved in commodity contracts; or
- acquiring any security of which another REIT fund.

#### i. Leverage

Leverage
<ul style="list-style-type: none"> <li>- A REIT Management Company shall not borrow against any REIT assets</li> <li>- REIT Management Company may arrange unsecured borrowing not exceeding 30% of the value at which the land has been transferred to a Developmental REIT scheme or 30% of the value of the real estate in the case of Rental REIT to meet the shortfall arising out of, cost overruns in the case of a Developmental REIT and for Capex to keep the real estate in working condition in the case of a Rental REIT</li> </ul>

#### j. Profit distribution obligations

Operative income	Capital gains	Timing
90% of the annual accounting income	90% of the annual accounting income	Annually

A REIT Management Company shall distribute not less than 90% of the profits arising out of the REIT scheme to the unitholders as a dividend in each financial year.

The dividend shall be paid in cash.

#### k. Sanctions

Upon observing that the REIT Management Company is not pursuing its business according to the laws, rules and guidelines of the SECP, the SECP may:

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Cancel or suspend the registration of the REIT scheme</li> <li>- Remove the trustee in the circumstances as stipulated in the regulation</li> <li>- Remove the valuer in the circumstances as stipulated in the regulation</li> <li>- Impose a fine</li> </ul>

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt, if 90% of the nett income distributed other than bonus shares and capital gains [Clause 99 Part I 2nd Schedule]	Capital gains arising to a person on the sale of immovable property to a REIT Development scheme with the object of development and construction of residential buildings are tax-exempt [Clause 99A Part I 2nd Schedule]	<ul style="list-style-type: none"> <li>- No tax withholding on receipt of dividend income, profit on debt (interest), commission or capital gains on listed securities [Clause 47B Part IV 2nd Schedule]</li> <li>- Other withholding tax due can be avoided subject to the availability of exemption certificate, which is provided by the Federal Board of Revenue on a case by case basis</li> </ul>

#### Current income

Income of a duly registered REIT scheme is exempt from tax subject to distribution of a minimum of 90% of its accounting income of that year, reduced by capital gains whether realised or unrealised, among the unitholders. For the purposes of determining distribution, at least 90% of accounting income, bonus shares or units or certificates shall not be taken into account.

Taxable at corporate tax rate if profit distribution of at least 90% as stated above is not made.

#### Capital gains

Generally, capital gains on moveable assets held for 12 months or less are taxable at the full corporate tax rate. Capital gains on the sale of moveable assets held for more than 12 months are exempt from tax up to 25% of the total gain. The remaining 75% gain is taxable at the corporate tax rate. The effective tax rate works out to be 21.75 % [29% X 75%] in this case. Kindly note that currently, the corporate rate of tax is 29% for the tax year 2019, which will be reduced by 1% every year until 2023 i.e. reduced to 25%.

Capital gains on the sale of immovable property are subject to tax at the following reduced rate:

S. No.	Holding Period	Rate
1.	Where the holding period of immovable property is up to one year	10%
2.	Where the holding period of immovable property is more than one year but not more than two years	7.5%
3.	Where the holding period of immovable property is more than two years but not more than three years	5%
4.	Where the holding period is more than three years	0%

Capital gains to a person on sale of immovable property to the REIT Development scheme are only exempt up to June 30, 2020.

If the immovable property is purchased and sold for business purpose, the gains would be liable to corporate income tax at 29% for the tax year 2019.

Stamp duty is charged based on a schedule of charges, at the time of the transfer of the property.

### Withholding tax

No withholding is required to be made on payments to the registered REIT companies on account of any dividend, profit on debt (interest), commission or capital gains on listed securities. Other withholding obligations would be applicable on payments received by registered REIT companies. However, based on the general exemption from tax (subject to 90% distribution of profits), an exemption certificate from withholding of tax can be obtained from the tax authorities by the registered REIT company. A refund of excess tax payment is possible.

### Accounting rules

No accounting rules prescribed.

## b. Transition regulations

### Conversion into REIT status

N/A

No rules prescribed.

## c. Registration fees/ stamp duties

The registration charges and stamp duties in the provinces of Sindh and Punjab are as under:

Registration duties		Sindh	Punjab
a)	Registration on purchase by REIT Scheme	Nil	Nil
b)	Registration on sale by REIT Scheme	0.5%	0.5%
c)	Stamp Duty on REIT property purchases	0.5%	0.5%
d)	Stamp Duty on REIT property sales	1%	1%



## 4 Tax treatment at the unit holder's level

### a. Domestic unit holder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- A 12.5% tax on a dividend from the stock fund; however, in the case of other funds, including REIT schemes, is 15%* – final levy</li> <li>- tax on capital gains ranges from 0% to 15% – see table below</li> </ul>	<ul style="list-style-type: none"> <li>- A 12.5% tax on a dividend from the stock fund; however, in the case of other funds, 12.5%* or 7.5% if the dividend was received from a REIT – final levy</li> <li>- tax on capital gains ranges from 0% to 15% – see table below</li> </ul>	<ul style="list-style-type: none"> <li>- A 12.5% withholding tax on a dividend from the stock fund for a company and individual both; however, in the case of other funds, 12.5% for filer and 15% for non-filer; for individuals and for companies, 15% for filer and 25% for non-filer; also, for individuals, in the case of a rental REIT, 7.5% is applicable</li> <li>- tax on capital gains ranges from 0% to 15% – see table below</li> </ul>

*In the case of a Developmental REIT scheme with the object of development and construction of residential buildings is set up by thirtieth day of June, 2020, tax imposed on a dividend received by a person from such a Developmental REIT scheme shall be reduced by 50% for three years from the date of setting up of the said scheme.*

### Capital gain tax for both company and individual unit holder [Domestic and Foreign]

Holding period [in months]	If the security was acquired prior to July 1, 2016		If the security is acquired after July 1, 2016	
	Filer	Non-filer	Filer	Non-filer
Less than 12	15%	18%	15%	20%
12 to 24	12.5%	16%	15%	20%
More than 24 [securities purchased on or after July 1, 2013]	7.5%	11%	15%	20%
More than 48 [securities purchased before July 1, 2013]	0%	0%	0%	0%

### Corporate unit holder

Subject to tax on a dividend received at 12.5% from the stock fund; however, in the case of other funds 15%. Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability.

### Individual unit holder

Subject to tax on a dividend received at 12.5%.

Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability.

## Withholding tax

The registered REIT company would be required to withhold tax at the rate of 12.5% to the individual unitholder; however, the tax liability will be 12.5% in the case of corporate unitholder. A 12.5% withholding tax on a dividend from the stock fund; however, in the case of other funds, 15%. Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability with reference to the rates of the filer. Please note that an exemption has been provided for person receiving a dividend at 50% from a Development REIT for three years from the date of setting up of the said scheme till June 30, 2020.

### b. Foreign unit holder

Corporate unit holder	Individual unit holder	Withholding tax
<ul style="list-style-type: none"> <li>- A 12.5% tax on a dividend from the stock fund; however, in the case of other funds, including REIT schemes, is 15%* – final levy</li> <li>- tax on capital gains ranges from 0% to 15% – see table below</li> </ul>	<ul style="list-style-type: none"> <li>- A 12.5% tax on a dividend from the stock fund; however, in the case of other funds, 12.5%* or 7.5% if the dividend was received from a REIT – final levy</li> <li>- tax on capital gains ranges from 0% to 15% – see table below</li> </ul>	<ul style="list-style-type: none"> <li>- A 12.5% withholding tax on a dividend from the stock fund for a company and individual both; however, in the case of other funds, 12.5% for filer and 15% for non-filer; for individuals and for companies, 15% for filer and 25% for non-filer; also, for individuals, in the case of a rental REIT, 7.5% is applicable</li> <li>- Tax on capital gains ranges from 0% to 15% – see table below</li> <li>- Tax treaty relief is available under various tax treaties Pakistan has with other countries</li> </ul>

## Capital gain tax for both company and individual unitholder

Holding period [in months]	If the security was acquired prior to July 1, 2016		If the security was acquired after July 1, 2016	
	Filer	Non-filer	Filer	Non-filer
Less than 12	15%	18%	15%	20%
12 to 24	12.5%	16%	15%	20%
More than 24 [securities purchased on or after 1 July 2013]	7.5%	11%	15%	20%
More than 48 [securities purchased before 1 July 2013]	0%	0%	0%	0%

### Corporate unit holder

Subject to tax on a dividend received at 12.5% from the stock fund; however, in the case of other funds 25%. Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability.

## Individual unit holder

Subject to tax on a dividend received at 12.5%. Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability.

## Withholding tax

The registered REIT Company would be required to withhold tax at the rate of tax at 12.5% to the individual unitholder; however, the tax liability will be 12.5%.

In the case of a corporate unitholder 12.5%, the withholding tax on a dividend from the stock fund; however, in the case of other funds 15%.

Tax withholding on capital gains on redemption of securities ranges from 0% to 15% (see above table) which will be the final discharge of tax liability with reference to the rates of the filer. Please note that an exemption has been provided for person receiving a dividend at 50% from Development REIT for three years from the date of setting up of the said scheme till 30 June 2020.

Tax treaty relief is not possible as the tax rate is already quite low.

## 5 Tax treatment of foreign REITs and their domestic unit holder

Foreign REIT	Corporate shareholder	Individual shareholder
A 29% corporate tax on Pakistan source income, i.e. applicable corporate rate of tax for the tax year 2019	<ul style="list-style-type: none"> <li>- A 29% tax on dividends</li> <li>- Tax on capital gains will be at 29% and 21.75% if the holding period is more than one year</li> </ul>	<ul style="list-style-type: none"> <li>- The taxability of s dividend is at the rate applicable to the individual based on income slabs</li> <li>- Tax on capital gains will be at the normal rate (maximum rate is 29%), and a 3/4 portion will be only be taxed if the holding period is more than one year</li> </ul>

### Foreign REIT

Foreign REITs would not be liable to the tax benefits prescribed in the tax law as they are restricted to REIT companies registered in Pakistan.

A foreign REIT would be taxed on its Pakistan source income at a tax rate of 29% for the tax year 2019.

### Corporate unit holder

In the case of foreign REIT, the applicability of tax deductions is missing; therefore, no withholding has been made and dividend income in the hands of the company will be taxed under the normal tax regime.

Any capital gains will be taxed as discussed in paragraph 3.1 above. However, in this case, the domestic corporate unitholder is entitled to the foreign tax credit in Pakistan. Further, the provision of the double tax treaty will also be applied.

## Individual unit holder

In the case of foreign REIT, the applicability of tax deduction is missing; therefore, no withholding has made and dividend income in the hands of the company will be taxed under the normal tax regime.

Any capital gains in the hands of individual unitholder will be taxed as discussed for corporate unitholder in paragraph 3.1 above. However, in this case, the domestic individual unitholder is entitled to the foreign tax credit in Pakistan. Further, the provision of the double tax treaty will also be applied. ■

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ASIA - PACIFIC

# Philippines

REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

Enacted year	Citation	REIT type	REIT market
2009	Republic Act 9856	Corporate type	No REITs established as of May 2019

The Real Estate Investment Trust (REIT) Act of 2009, otherwise known as Republic Act 9856, was enacted on December 17, 2009, without the signature of the President of the Philippines, in accordance with Article VI, Section 27(1) of the Philippine Constitution. The REIT Act is a synthesis of Senate Bill No. 2639 and House Bill No. 6379 that were approved by the Senate and the House of Representatives on September 29, 2009, and September 30, 2009, respectively.

The REIT Act became effective on February 09, 2010. On May 13, 2010, the Securities and Exchange Commission (SEC) approved the Implementing Rules and Regulations (IRR) in relation to the REIT Act.

## 2 Requirements

### a. Formalities/procedure

Key requirements
Registration with the Securities and Exchange Commission (SEC)

The shares of the REIT must be registered with the Securities and Exchange Commission (SEC) and listed in accordance with the rules of the Stock Exchange.

### b. Legal form/minimum share capital

Legal form	Minimum share capital
Stock corporation	PHP 300 million

A REIT shall be set up as a stock corporation, i.e. as a Real Estate Investment Company (REIC). The stock corporation should be established in accordance with the Corporation Code of the Philippines and the rules and regulations promulgated by the Securities and Exchange Commission of the Philippines, or organised under the laws of a foreign country, principally for the purpose of owning income-generating real estate assets and real estate securities.

The majority of the members of the board of directors must be residents of the Philippines. At least two directors (or 33.3% of the total number of directors in the case that the REIT has more than six directors) on the board of directors of a REIT shall be independent directors.

A REIT established under Philippine laws is deemed to be tax resident in the Philippines and will be able to benefit from any Double Taxation Treaties that the Philippines may have in place.

A REIT formed under the laws of a foreign country will likewise be deemed a Filipino tax resident if it is engaged in trade or business within the Philippines. Under Philippine laws 'doing business' includes, among others: participation in the management, supervision or control of any domestic business, firm,

entity or corporation in the Philippines; any other act or acts that implies a continuity of commercial dealings or arrangements, and contemplate to the extent that the performance of acts or works, or the exercise of some of the functions normally incident to and in progressive prosecution of commercial gain or of the purpose and object of the business organisation. If the above criteria are met, then the foreign REIT will be able to benefit from Double Taxation Treaties that the Philippines may have in place.

A REIT must have a minimum paid-up capital of PHP 300 million. In order to prevent companies from using REITs merely to convert ownership in existing infrastructure to liquid assets, there is an existing proposal to restrict payment of existing debts being made out of paid-up capital (i.e. these debts must be paid out of income generated by the business), thereby preventing companies from deleveraging by using REITs to pay off existing debts.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
At least 1,000 shareholders with at least 50 shares each (who in aggregate own at least 40% of share capital in the year of listing, and should be increased to 67% within three years of listing)	Yes

A REIT must be listed in accordance with the rules and regulations of a Stock Exchange and must be regulated as a public company. To qualify as a public company, the REIT must, upon and after listing have at least 1,000 shareholders, each owning at least 50 shares of a class of shares and who in the aggregate own at least 40% of the share capital of the REIT in the year of listing provided, that the minimum ownership is increased to 67% within three years of listing.

Compliance with the minimum public ownership requirement must be duly certified by the Public Registrar upon listing, on the date of any dividend declaration, on the date of any corporate action requiring shareholder approval and other relevant times as may be required by the SEC.

In order for a REIT to be allowed to own land located in the Philippines, it must comply with foreign ownership limitations imposed under Philippine laws, that is: such ownership is restricted to persons or entities considered as Filipino citizens (individuals) or Philippine nationals (which stretches to include Filipino citizens, domestic partnerships or associations wholly owned by Filipino citizens and corporations organised under the laws of the Philippines of which at least 60% of the share capital is owned by Filipino citizens). For land ownership purposes, a corporation shall be deemed as a Philippine national if 60% of its share capital and vote entitlement are owned by Filipino citizens.

### d. Asset level/activity test

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- In the case of investment in income-generating real estate outside the Philippines, the investment does not exceed 40% of the deposited property</li> <li>- At least 75% income-producing real property in the Philippines required</li> <li>- Must not undertake property development</li> <li>- May hold real estate through unlisted special purpose vehicle (SPV)</li> </ul>

A REIT may only invest in:

- Real estate, whether freehold or leasehold, in or outside the Philippines. A REIT can invest in income-generating real estate outside the Philippines to the extent that this investment does not exceed 40%



of the REIT's Deposited Property and that special permission is obtained from the SEC. An investment in real estate may be by way of direct ownership or a shareholding in an unlisted special purpose vehicle (SPV) incorporated to hold or own real estate;

- b. Real estate-related assets, wherever the issuers, assets, or securities are incorporated, located, issued or traded;
- c. Managed funds, debt securities and shares issued by listed local or foreign non-property corporations;
- d. Government securities issued on behalf of the Philippine Government, governments of other countries and securities issued by supranational agencies;
- e. Cash and cash equivalents;
- f. Such other similar investment outlets as the SEC may allow

Republic Act 9856 likewise provides that:

- a. At least 75% of the Deposited Property of the REIT must be invested in, or consist of, income-generating real estate;
- b. A REIT must not undertake property development activities whether on its own, in a joint venture with others, or by investing in unlisted property development companies, unless it intends to hold the developed property upon completion. The total contract value of property development activities undertaken and investments in uncompleted property developments should not exceed 10% of the Deposited Property;
- c. Not more than 15% of investable funds of the REIT may be invested in any one issuer's securities or any one managed fund, except with respect to government securities where the limit is 25%;
- d. A REIT may invest not more than 5% of its investable funds in certain financial products, such as, but not limited to, credit default swaps, credit-linked notes, collateralised debt obligations, total return swaps, credit spread options, and credit default options, and only upon special authority from the SEC;
- e. A REIT may invest in local or foreign assets, subject to the terms of its articles of incorporation. Where an investment in foreign real estate assets is made, the REIT should ensure compliance with the applicable laws and requirements in that foreign country;
- f. When investing as a joint owner, the REIT should make such an investment by acquiring shares or interests in an unlisted SPV set up to hold/own real estate and the REIT should have the freedom to dispose of its interest in such an investment.

## e. Leverage

### Leverage

Shall not exceed 35% of the market value of deposited property

The total borrowings and deferred payments of a REIT shall not exceed 35% of the market value of its deposited property provided; however, the REIT has publicly disclosed its investment-grade credit rating by a duly accredited or internationally recognised rating agency. Its total borrowings and deferred tax payments may exceed 35%, but not more than 70% of the market value of its deposited property. Note that it is necessary to undergo a full valuation of the REIT's assets using an SEC-accredited independent appraisal company at least once a year.



There is currently no distinction between domestic and cross-border situations for leverage purposes.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of its distributable income	<ul style="list-style-type: none"> <li>- Capital gains from the sale of stock of domestic corporations are not included in distributable income since they have already been subjected to final tax</li> <li>- Other types of capital gains are included in distributable income if they have been realised and have not been reinvested by the REIT within one year from the date of sale</li> </ul>	Annually

#### Operative income

A REIT must distribute annually as dividends at least 90% of its distributable income to its shareholders not later than the last day of the fifth month following the close of the fiscal year of the REIT.

‘Distributable income’ is defined as ‘net income as adjusted for unrealised gains and losses/expenses, impairment losses and other items in accordance with internationally accepted accounting standards’. Distributable income excludes proceeds from the sale of the REIT’s assets that are re-invested by the REIT within one year of the date of the sale.

#### Capital gains

To the extent that the gains are realised, they are included in distributable income as determined by the SEC. This is not the case if the gain on the sale of REIT assets is re-invested by the REIT within one year of the date of sale.

Unrealised gains are not included in the distributable income. Also, capital gains realised from the disposal of shares in domestic corporations are not included in distributable income since they have already been subjected to final tax (see section 3.1).

There is currently no distinction between domestic and cross-border profit distribution requirements.

#### g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Revocation of tax incentives</li> <li>- Liability for surcharges and penalties under the tax code</li> </ul>

Delisting of REITs:

- If the REIT is delisted from the local exchange, whether voluntarily or involuntarily, for failure to comply with the provisions of the REIT Act or rules of the Stock Exchange, its tax incentives shall be ipso facto revoked and withdrawn as of the date the delisting becomes final;
- Any tax incentives that may have been availed of by the REIT after the delisting shall immediately be refunded to the Government, together with a fine of between PHP 200,000 and PHP 5 million; and

- c. If the delisting is highly prejudicial to the interest of the investing public, the REIT and/or responsible persons shall refund to its investors at the time of delisting the value of their shares.

#### Revocation of registration of REITs:

- a. If the SEC discovers that the REIT was established so as to seek the benefits of the REIT Act without a true intention to carry out its provisions and/or adhere to the rules of the REIT Act, the SEC shall revoke or cancel the registration of the shares of the REIT; and
- b. The REIT shall pay the applicable taxes to a non-REIT retrospectively, plus interests and surcharges prescribed under the tax code.

## 3 Tax treatment at the level of REIT

### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Only non-distributed current income subject to taxation	Transfer of shares in a domestic corporation subject to special rates of capital gains tax Other types of capital gains are included in gross income	Foreign withholding tax-deductible or creditable Local withholding tax creditable

#### Current income

The taxable net income of a REIT refers to the pertinent items of ‘gross income’ as defined in the tax code minus the following deductions: (a) those deductions enumerated in the tax code; and (b) the dividends distributed by a REIT out of its distributable income as of the end of the taxable year.

The taxable net income is subject to regular corporate income tax (RCIT), at the rate of 30% beginning January 1, 2009. A REIT shall not be subject to the minimum corporate income tax (MCIT).

#### Capital gains

Only retained capital gains which have been realised and which have not been subjected to final tax (see below) are included in the gross income of a REIT, which after the allowable deductions (see above) are subject to the RCIT.

A REIT shall be subject to capital gains tax (CGT) at the rate of 5% for the first PHP 100,000, and 10% for net capital gains in excess of PHP 100,000, realised from the disposal (by the REIT) of shares of a domestic corporation, if such domestic corporation is not listed on the local stock exchange, or even if listed, if the transfer takes place through trades outside the local stock exchange.

#### Withholding tax

Any foreign withholding tax may be utilised as either a deduction from gross income or a tax credit (subject to the applicable limitations). Local income payments to a REIT shall be subject to a lower creditable withholding tax of 1%.

## Other taxes

1. The gross sale of properties and services (e.g. rental receipts) of a REIT will be subject to value-added tax (VAT) at the rate of 12% ('Output VAT'), the amount of which is passed on to the buyers/lessees of the REIT. The REIT can claim, as a credit against its Output VAT, the amount of the VAT passed on to it by its local suppliers of goods and services ('Input VAT'). The REIT's VAT Payable is the excess of its Output VAT over its Input VAT. A REIT shall not be considered as a dealer in securities and shall not be subject to VAT on its sale, exchange or transfer of securities as part of its real estate-related business;
2. A REIT will be subject to the stock transaction tax (STT) on its transfers of shares of stock listed and traded at the local stock exchange, at the rate of 0.5% of the gross selling price or the gross value in money of the shares of stock. If the REIT transfers the listed shares outside the stock exchange, then it will be subject to capital gains tax at the rate of 5% for the first PHP 100,000 of net capital gains and 10% for net capital gains in excess of PHP 100,000;
3. The sale or transfer of any property to REITs, which includes the sale or transfer of security over the asset, shall be subject to 50% of the applicable documentary stamp tax (DST) imposed under the tax code;
4. Any sale, barter, exchange or other disposition of listed shares in the REIT by its investors does not give rise to a DST at the level of the REIT;
5. A REIT will be subject to local business tax at the rates provided in the Revenue Code of the province/city/municipality where the principal office of the REIT is located;
6. A REIT will be subject to a local transfer tax on its transfers of real property, at the rate provided in the Revenue Code of the province/city/municipality where the real property is located.

## Accounting rules

The Philippines has adopted International Financial Reporting Standards.

### b. Transition regulations

#### Conversion into REIT status

'Conversion' may be through a transfer of existing REIT-eligible assets to a REIT

Any gain realised from the transfer of properties to a REIT are not exempt from capital gains tax or regular income tax although the transferor may opt to structure the sale as a tax-deferred exchange pursuant to the provisions of the tax code. A REIT must be a newly incorporated entity. An existing property company is not allowed to merely amend its Articles of Incorporation in order to achieve REIT status.

### c. Registration duties

#### Registration duties

Registration fees, DST, local withholding tax and local transfer taxes

While the transfer of properties to a REIT will give rise to liability for local transfer taxes, such transfer will no longer be subject to 12% VAT pursuant to Sections 40 (c)(2) and 109 (X) of the tax code (as amended by the Tax Reform for Acceleration and Inclusion (TRAIN Law), otherwise known as Republic Act 10963). The registration of the deed of sale with the Register of Deeds requires the payment of registration fees. As discussed above, the transfer of properties to a REIT will be subject to 50% of the applicable DST imposed under the tax code. Local income payments to a REIT shall be subject to a lower creditable withholding tax of 1%.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Distributions tax-exempt	A final 10% withholding tax on dividends received	A final withholding tax for individual shareholders

#### Corporate shareholder

Dividends paid by a REIT to a domestic corporation or a resident foreign corporation are tax-exempt.

Since the REIT's shares are listed on the local stock exchange, the disposal of the REIT shares by a corporate shareholder (i.e. a domestic corporation or a resident foreign corporation) shall be subject to the following taxes:

- Stock transaction tax of 0.5% of the gross selling price or the gross value in money of the shares of stock transferred, if the REIT shares are transferred through trades on the stock exchange; or
- Capital gains tax of 5% (on the first PHP 100,000 of net capital gains) or 10% (on net capital gains exceeding PHP 100,000), if the REIT shares are transferred outside the stock exchange.

#### Individual shareholder

The 10% tax on dividends received by a Filipino citizen or a foreigner resident in the Philippines from a REIT is a final tax, withheld and remitted to the Bureau of Internal Revenue (BIR) by the REIT.

The tax treatment of the transfer of the REIT shares by a Filipino citizen or a foreigner resident in the Philippines is the same as for Corporate shareholders (as set out above).

Dividends received by Filipino investors currently resident overseas from a Philippine REIT are exempt from Philippine income tax for seven years from August 11, 2011, which is the date that the tax-specific IRR was passed, bringing into force the tax provisions of the 2009 REIT Act.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
10%	10%	Tax treaty relief available

#### Corporate shareholder

Unless a foreign corporation is entitled to claim a preferential withholding tax rate of less than 10% pursuant to an applicable tax treaty, a 10% final withholding tax on dividends to foreign corporate shareholders shall be levied. The default rate under the tax code is 35%, reduced to 15% under a tax sparing provision of the tax code, and to 10% under certain tax treaties. It should be noted that there are currently no tax treaties with the Philippines in force that reduce withholding tax to below 10%.

The tax treatment of the disposal of the REIT shares by a foreign corporate shareholder is the same as for a corporate shareholder as per Section 4.1 above.

## Individual shareholders

A 10% final withholding tax shall be levied on dividends paid by REITs to foreign individual shareholders. The default rate under the tax code is 20% for non-residents engaged in trade or business in the Philippines, and 25% for non-residents not engaged in trade or business in the Philippines. Most tax treaties reduce these rates to 10% or 15%.

The tax treatment of the disposal of the REIT shares by a foreign individual shareholder is the same as for a corporate shareholder as per Section 4.1 above.

## Withholding tax

Tax treaty relief is available, although in practice this is unlikely to apply as the rates under domestic legislation are lower than treaty rates.

# 5 Tax treatment of foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Subject to taxation, unless there are applicable preferential rates or exemptions under tax treaties	Subject to taxation	Subject to taxation

## Foreign REIT

If the Philippine source income of a foreign REIT is not derived from a Philippine REIT, then it will be subject to Philippine tax in the same manner as any non-resident, subject to preferential treaty rates or exemptions applicable to foreign trusts or corporations, depending on how the foreign REIT is organised.

## Corporate shareholder

Dividends received by a local corporation from a Foreign REIT are included in its gross income that, after allowable deductions, is subject to the RCIT

## Individual shareholder

Dividends received by a local individual (Filipino resident citizen or a foreigner resident in the Philippines) from a Foreign REIT are included in Gross income which after allowable deductions, is subject to regular income tax at the rate applicable to such individual. ■

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# Singapore

S-REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
S-REIT	1999	<ul style="list-style-type: none"> <li>- Securities and Futures Act</li> <li>- Code on Collective Investment Schemes</li> <li>- Property Fund Guidelines</li> <li>- Income Tax Act</li> </ul>	Trust

The REIT regime in Singapore is principally regulated by the Securities and Futures Act (Cap. 289), the Code on Collective Investment Schemes (the 'Code') issued by the Monetary Authority of Singapore (MAS), the Property Fund Guidelines appended to the Code and the Income Tax Act.

The Property Fund Guidelines apply to a collective investment scheme that invests or proposes to invest primarily in real estate and real estate-related assets. The scheme may or may not be listed on the Singapore Exchange.

The first set of regulatory guidelines for property funds was issued by the Monetary Authority of Singapore in May 1999.

The first Singapore REIT was listed on the Singapore Exchange in July 2002. To date, there are 44 REITs and Property Trusts listed on the Singapore Exchange with a market capitalisation of approximately SGD 100 billion.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index**	Sector Mkt Cap (EUR m)	% of Global REIT Index
Singapore	37	10	EUR 58,904	2.26%

## Top five S-REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Ascendas Real Estate Investment Trust	EUR 6,302	29.60%	5.14%	0.45%
CapitalLand Mall Trust	EUR 6,296	38.55%	3.87%	0.36%
CapitalLand Commercial Trust	EUR 5,281	39.15%	4.01%	0.30%
Mapletree Commercial Trust	EUR 3,926	45.31%	4.37%	0.23%
Mapletree Logistics Trust	EUR 3,738	40.42%	4.11%	0.22%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

\*\* The number considers only those REITs covered by the REIT regime in Singapore and owning properties mainly in the same country.



## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Formal advance ruling and/or tax transparency/exemption application has to be submitted
- Listing on the Singapore Exchange is necessary to qualify for tax exemption

Singapore REITs (S-REIT) listed on the Singapore Exchange are eligible for favourable tax treatment, subject to certain conditions. To be listed on the Singapore Exchange, a REIT must comply with the applicable rules, regulations and guidelines set out in Securities and Futures Act (Cap. 289), the Code (including the Property Fund Guidelines) and the Singapore Exchange Listing Manual.

Some of the favourable tax treatments are granted on application. In other words, a formal advance ruling and/or tax transparency/exemption application has to be submitted to the Singapore tax authorities and/or the Singapore Ministry of Finance. In recent years, certain application procedures are simplified.

### b. Legal form/minimum initial capital

Legal form	Minimum initial capital
Trust	SGD 300 million

#### Legal form

An S-REIT must be constituted as a trust.

An S-REIT may be managed externally or internally.

#### Minimum initial capital

For listing on the Singapore Exchange, a REIT, if it is denominated in Singapore Dollars (SGD), must have a minimum asset size of at least SGD 300 million.

### c. Unit holders requirements/listing requirements

Unit holder requirements	Listing mandatory
At least 25% of the REIT's capital has to be held by at least 500 public unitholders (SGD-denominated REITs)/Spread of holders required (non-SGD denominated REITs)	In principle, not required but necessary for the various tax concessions



## Unitholder requirements

For Singapore Dollar-denominated REITs listed on the Singapore Exchange, at least 25% of its capital must be held by at least 500 public unitholders. In the case of foreign currency-denominated REITs listed on the Singapore Exchange, a spread of holders necessary for an orderly market is required.

There is no distinction made between resident and non-resident unitholders in respect of ownership. There are no restrictions on foreign unitholders.

## Listing requirements

REITs need not be listed, but only a REIT that is listed on the Singapore Exchange is eligible for tax concessions. A REIT listed on a foreign exchange will not be eligible for the various tax concessions in Singapore and therefore appropriate tax planning should be considered.

### d. Asset level/activity test

#### Restrictions on activities/investments

- At least 75% of the REIT's deposited property should be invested in income-producing real estate
- No property development activities or investment in unlisted property development companies are allowed unless the REIT intends to hold the developed property upon completion
- Investments in vacant land and mortgages (except for mortgage-backed securities) are prohibited
- Investments in property development activities and uncompleted property development (local and foreign) must not exceed 10% of its deposited property; this limit can be increased up to 30%, subject to the REIT meeting certain conditions
- Investments in permissible investments must not exceed 5% of its assets in any one issuer's securities or any one manager's funds
- Should not derive more than 10% of its revenue from sources other than rental and other specified sources (e.g. interest, dividends, other permissible investments of the REIT etc)

The Property Fund Guidelines state that a REIT may invest in:

- a. real estate, whether freehold or leasehold, in or outside Singapore;
- b. real estate-related assets;
- c. listed or unlisted debt securities and listed shares of or issued by non-property corporations;
- d. government securities and securities issued by a supra-national agency or a Singapore statutory board; and
- e. cash and cash-equivalent items.

A REIT is also subject to restrictions on its investment activities, such as:

- a. at least 75% of its deposited property should be invested in income-producing real estate;
- b. not undertaking property development activities nor investing in unlisted property development companies, unless the REIT intends to hold the developed property upon completion;
- c. not investing in vacant land or mortgages (except for mortgage-backed securities);
- d. the total contract value of property development activities and investments in uncompleted property developments should not exceed 10% of the REIT's deposited property (this limit can be increased up to 30%, subject to the REIT meeting certain conditions);

- e. not more than 5% of the REIT's deposited property should be invested in permissible investments (c), (d) and (e) listed above issued by any one issuer's securities or any one manager's funds;
- f. not deriving more than 10% of its revenue from sources other than rental payment from the tenants of the real estate held by the REIT or interest, dividends, and other similar payments from special purpose vehicles and other permissible investments of the REIT.

A REIT may invest in real estate by way of direct ownership or a shareholding in an unlisted special purpose vehicle (SPV) constituted to hold/own real estate. When investing in real estate as a joint owner, the REIT should make its investment by investing directly in the real estate as a tenant-in-commonor by acquiring the shares or interests in an unlisted SPV constituted to hold/own real estate. The SPV can take the form of a company, trust or partnership, etc.

#### e. Leverage

Leverage
Single-tier leverage limit of 45%

A single-tier leverage limit of 45% of an S-REITs' deposited property has been introduced. There is no longer a requirement for the REIT to obtain a credit rating.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
At least 90% of tax transparent income	Not required	<ul style="list-style-type: none"> <li>- Annually or</li> <li>- Semi-annually or</li> <li>- Quarterly</li> </ul>

#### Operative income

Strictly, there are no legal or regulatory requirements for a REIT to distribute any pre-determined percentage of its income as distributions for a given financial year. However, in order to enjoy tax transparency treatment, the trustee of the REIT is required to distribute at least 90% of its taxable 'specified income' in the same year in which the income is derived by the trustee and for both the trustee and manager to jointly comply with certain conditions. With effect from April 01, 2012, REIT distributions may be made to unitholders in the form of units in the REIT, subject to meeting certain conditions.

'Specified income' refers to the following:

- a. rental income or income from the management or holding of immovable property but excluding gains from the disposal of immovable property;
- b. income that is ancillary to the management or holding of immovable property but excluding gains from the disposal of immovable property;
- c. income that is payable out of rental income or income from the management or holding of immovable property in Singapore, but not out of gains from the disposal of such immovable property;
- d. rental support payment that is based on an open market value basis and is paid to the trustee on or after December 29, 2016 by:

- i. the seller who sold to the trustee the property or any interest in the owner of the property;
  - ii. a person who wholly owns (directly or indirectly) the seller; or
  - iii. any other person approved by the Comptroller; and
- e. distributions from an approved sub-trust of the REIT out of income referred to in (a), (b) and (d) above.

The REIT may qualify for tax exemption on certain foreign-sourced income that is remitted into Singapore from investment in overseas properties.

## Capital gains

Not required.

## g. Sanctions

### Penalties/loss of status rules

Loss of tax transparency treatment if REIT is no longer listed on the Singapore Exchange

If not less than 90% of a REIT's specified income is distributed in the same year in which the income is derived, then the amount of the specified income that is not distributed will be subject to tax at the corporate tax rate (currently 17%) in the hands of the trustee. If less than 90% of the REIT's specified income is distributed in the same year in which the income is derived, all of its specified income will be subject to tax.

# 3 Tax treatment at the level of REIT

## a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Eligible rental income exempt from tax	No tax imposed on gains of a capital nature	No foreign withholding tax refunds in respect of tax-exempted income

### Current income

As noted above, for rental and property-related income (e.g. car park charges, service fees) no tax is imposed at the REIT level if it has been accorded tax transparency treatment. If specified income is not distributed, then the consequence noted above will ensue (i.e. specified income that is not distributed will be subject to tax at the corporate tax rate of 17% in the hands of the trustee).

Foreign-sourced dividends received in respect of underlying rental income from investment in foreign properties may be exempt from Singapore income tax if certain conditions are met.

## Capital gains

Singapore does not impose a tax on gains of a capital nature. However, gains that are of an income or revenue nature will be taxed at the prevailing corporate tax rate, currently 17%.

Gains or losses (unless the REIT's activities are such that it can be said to be carrying on a business of dealing in properties) from the sale of property are likely to be treated as capital gains or losses. Where the REIT is construed to be in the business of dealing in properties, then the gains would be taxed at the trustee level at the prevailing corporate tax rate, currently 17%.

## Withholding tax

The foreign-sourced income of the S-REIT may qualify for tax exemption under general tax rules. Foreign withholding tax on such income (if exempted from tax) will not be credited or refunded if such income is tax exempted.

## Other taxes

See under no. 3.3 below.

## Accounting rules

Local GAAP, which closely mirrors IFRS, apply. The income will be determined on an accrual basis.

### b. Transition regulations

#### Conversion into REIT status

N/A

### c. Registration duties

#### Registration duties

- Stamp duties from 0.2-34.2%
- Goods and Services Tax may be applicable
- No capital duty

The sale or transfer of immovable property located in Singapore is usually subject to Singapore stamp duty of up to 3%-4% depending on the classification of the property. This stamp duty is generally referred to as Buyer's Stamp Duty ('BSD') because the buyer is liable to pay the stamp duty unless otherwise agreed between the buyer and the seller. In addition to BSD, Additional Buyer's Stamp Duty ('ABSD') and Seller's Stamp Duty (introduced as measures to cool the Singapore property market) may also apply to certain types of immovable properties.

ABSD is imposed in addition to the BSD that a buyer of residential property has to pay. It applies to direct purchases of Singapore residential property and is payable by property buyers. ABSD for entities (i.e. non-individuals) is imposed at 10% (for Contracts, agreements or documents of transfer dated between December 8, 2011 to January 11, 2013) or 15% (for Contracts, agreements or documents of transfer dated

on or after January 12, 2013 to July 5, 2018) or 25% (for Contracts, agreements or documents of transfer dated on or after July 2018). An additional 5% ABSD applies to buyers who are property developers.

SSD is payable by the seller of a property and may apply to the transfer of residential and industrial property located in Singapore. SSD is imposed at 5% to 15% (depending on how long the seller has held the property for) for transfers of Singapore industrial property, which were acquired by the seller on or after January 12, 2013, and sold/disposed within three years. For transfers of Singapore residential property, SSD of between 4% to 16% (depending on when the seller acquired the property and how long the seller held it for) generally applies if a property is held by the seller for four years or less. In addition, for residential properties acquired on and after March 11, 2017, no SSD is payable on disposal if the properties are held for more than three years. It is important to ensure that the seller has paid any applicable SSD. This is because, if the seller is liable but did not pay the SSD, the Agreement between buyer and the seller for the purchase of the property would not be considered as duly stamped (i.e. the Agreement cannot be admitted as evidence in court in the event of disputes) even if buyer paid the BSD and applicable ABSD.

The conveyance, assignment or sale of shares in a Singapore-incorporated company is also subject to Singapore stamp duty of 0.2% of the purchase consideration or its net asset value, whichever is higher.

Additional conveyance duties (ACD) may apply to the buying or selling of shares or units (equity interest) on or after March 11, 2017 in property-holding entities (PHEs) that own primarily residential properties in Singapore. The ACD provision applies to the purchase or sale of equity interests by persons or entities who are significant owners of the PHE or who become one after the purchase.

The transfer of Singapore properties may qualify as a transfer of a going concern and hence will not be subject to Goods and Services Tax (GST), which is currently 7%, or the S-REIT may avail itself of a concession that allows it to self-account for the Goods and Services Tax otherwise payable on the acquisition.

S-REITs that derive primarily dividend income or distributions (which are not taxable supplies for GST purposes) can claim input tax on business expenses incurred between February 17, 2006, and December 31, 2025. To facilitate fundraising by REITs through the use of SPVs, the GST concession has been enhanced to include SPVs set up solely to raise funds for the REITs and that do not hold qualifying assets of the REITs whether directly or indirectly. The enhanced concession will apply to GST on the expenses incurred to set up the SPVs as well as the GST on the business expenses of such SPVs.

## 4 Tax treatment at the unitholder's level

### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- 17% corporate tax on specified income</li> <li>- Distributions out of capital gains and income taxed at REIT's level are not taxable</li> <li>- Distributions out of non-income (e.g. operating cash flows) are regarded as a return of capital</li> <li>- Gains on the disposal of units are not taxable if capital in nature</li> </ul>	<p>All distributions and gains from the disposal of units are generally not taxable unless the individual is carrying on a trade, business or profession dealing with securities</p>	<p>No withholding tax is imposed on distributions to the domestic unitholder</p>

## Corporate unitholder

Distributions out of specified income are taxed at the prevailing corporate tax rate of 17%. Distributions made to corporate unitholders out of income previously taxed at the trustee level will be exempt from Singapore tax. However, no tax credit will be available for tax paid by the REIT.

If disposal gains are determined to be capital in nature and hence not taxed at the trustee level, the distribution made out of such gains should also not be taxed in the hands of corporate domestic unitholders unless they hold the units in the REIT as trading assets. If the gains are determined to be of an income nature or 'trading gains' and hence taxed at the trustee level, the distribution made out of such post-taxed profits is exempt from tax in the hands of the unitholder.

A return of capital is not taxed but will go towards reducing the cost base of units. For unitholders who hold the units as trading assets, the gains on disposal will be calculated using the reduced cost base.

Singapore does not impose a tax on gains of a capital nature. Gains realised on the sale of the REIT units are not taxable unless the gains are considered to be trading gains or gains or profit of an income nature (e.g. if the unitholder holds the units as trading assets). Corporates who hold REIT units as trading assets are subject to Singapore income tax at the prevailing corporate tax rate, currently 17%.

There is no stamp duty on the sale of REIT units that are listed on the Singapore Exchange.

## Individual unitholder

All distributions made by a REIT to unitholders who are individuals (beneficially entitled to these distributions) regardless of their nationality or place of residence, are generally exempt from Singapore income tax (if the distribution is regarded to be arising from investment rather than from trading in securities), unless they are derived through a partnership in Singapore or from the carrying on of a trade, business or profession dealing in securities.

If disposal gains derived by the REIT are determined to be capital in nature and hence not taxed at the trustee level, the distribution should also not be taxed in the hands of individual unitholders. If the gains are determined to be of an income nature or 'trading gains' and hence taxed at the trustee level, distributions out of such gains are exempt from tax in the hands of the individual unitholder.

A return of capital is not taxed as such distributions are capital in nature.

Singapore does not impose a tax on gains that are capital in nature. Gains realised on the sale of the REIT units by an individual unitholder are not taxable, unless the gains are considered to be trading gains or gains or profit of an income nature. Individuals who hold REIT units as trading assets are subject to Singapore income tax at their respective tax rates (ranging from 0% to 22%).

## Withholding tax

Distributions to domestic unitholders (e.g. domestic individuals, Singapore-incorporated and tax resident companies) are not subject to withholding tax if certain conditions and procedures are complied with.

One of the conditions requires unitholders to disclose their tax status on a prescribed form provided by the trustee. This will allow the REIT manager to ascertain whether tax has to be deducted on distributions made to certain unitholders. The REIT must pay any applicable tax withheld to the Singapore tax authorities by the 15th of the second month following the date of payment.

## b. Foreign unitholder

Corporate unit holder	Individual unit holder	Withholding tax rate
<ul style="list-style-type: none"> <li>- Final withholding tax on current income distributions</li> <li>- Withholding tax is not applicable on distributions of tax-exempt income (e.g. foreign dividends)</li> <li>- Distributions out of capital gains are generally not taxable</li> </ul>	<p>Distributions and gains from the disposal of units are generally exempt from tax unless the individual is carrying on a trade, business or profession dealing with securities</p>	<ul style="list-style-type: none"> <li>- Withholding tax rate reduced from 17% to 10% on distributions to non-resident non-individuals during the period from February 18, 2005 to March 31, 2025.</li> <li>- No treaty relief is available</li> </ul>

### Corporate unitholder

Current income distributions are subject to withholding tax at the prevailing corporate tax rate, currently 17%. A reduced rate of 10% applies for distributions made out of specified income during the period from 18 February 2005 to March 31, 2025.

If disposal gains derived by the REIT are determined to be capital in nature and hence not taxed at the trustee level, the distribution out of such gains is also not taxed in the hands of corporate foreign unitholders. If the gains are determined to be 'trading gains' and hence taxed at the trustee level, distributions made from such after-tax gains are also exempt from tax in the hands for the corporate unitholder.

Withholding tax is not applicable on distributions of specified tax-exempt income (e.g. foreign dividends received in respect of underlying foreign-sourced income from investments in foreign properties which qualify for exemption from Singapore income tax).

Distributions out of the return of capital are not taxed.

Disposal gains are generally not taxable unless the corporate unitholders are considered to be trading in nature (e.g. if the unitholder holds the units as trading assets in a business carried on in Singapore).

### Individual unitholder

Current income distributions are generally exempt from tax unless they are derived through a partnership in Singapore or from the carrying on of a trade, business or profession dealing in securities.

Withholding tax is not applicable on the distribution of tax-exempt income (e.g. foreign dividends received in respect of underlying foreign-sourced income from investments in foreign properties which are exempt from Singapore income tax).

If disposal gains derived by the REIT are determined to be capital in nature and hence not taxed at the trustee level, distributions out of them are also not taxed in the hands of individual foreign unitholders. If the gains are determined to be 'trading gains' and hence taxed at the trustee level, distributions out of them are also exempt from tax in the hands of the individual unitholder.

Distributions out of the return of capital are not taxed.

Generally, disposal gains are not taxable, unless they are considered to be trading in nature, for example, if the unitholder is carrying on of a trade, business or profession dealing in securities.

## 5 Tax treatment of foreign REITs and domestic unitholders

Foreign REIT	Corporate unit holder	Individual unit holder
Taxed under normal Singapore tax rules	Tax-exempt	Tax-exempt

### Foreign REIT

A foreign REIT will be taxable under normal Singapore tax rules. Therefore, if it invests in Singapore properties, it will not be eligible for tax transparency status and will pay tax on its net rental income in Singapore.

### Corporate unitholder

Distributions made by a foreign REIT (only if it is constituted as a trust) out of income derived from a direct holding of Singapore properties which has been assessed to tax as income from a trade or business may be treated as capital in the hands of unitholders. In other words, no further tax should be imposed on the distributions received by Singapore corporate unitholders.

Any gain derived from the sale of units in the foreign REIT will not be subject to tax, as long as the gain is not derived from the carrying on of a trade or business in Singapore. Investors who trade or deal in the units are subject to tax on any gain derived from the disposal of units if the gains are regarded as Singapore sourced income.

### Individual unitholder

Individual unitholders (except where the units are held by the individual through a partnership) are not taxed in Singapore on foreign REIT distributions.

Any gain derived from the sale of units in the foreign REIT should not be subject to tax, as long as the gain is not derived from the carrying on of a trade or business in Singapore. Investors who trade or deal in the units are subject to tax on any gain derived from the disposal of units if the gains are regarded as Singapore sourced income. ■

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GLOBAL  
REIT SURVEY

ASIA - PACIFIC

# South Korea

REIC

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIC	2001	Real Estate Investment Company Act	Corporate type

The Real Estate Investment Company Act (REICA) was enacted in 2001. It lays the groundwork for Real Estate Investment Trusts ('REITs') in Korea. REICA governs Self-managed REITs (REIC), Entrusted management REITs (or referred to as Commissioned REITs) and Corporate Restructuring REITs (CR-REITs), the three REIT regimes in Korea.

There are seven listed REITs in Korea as of May 2019. The Self-managed REITs are corporate type REITs.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
South Korea	7	0	EUR 1,414	0.00%

\*Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

# 2 Requirements

## a. Formalities/procedure

Key requirements
Approval from the Ministry of Land, Infrastructure and Transport

A REIT must obtain a business license from the Ministry of Land, Infrastructure and Transport ('MOLIT').

## b. Legal form/minimum share capital

Legal form	Minimum share capital
<ul style="list-style-type: none"> <li>- Joint-stock company (general REIT, REIC)</li> <li>- Entrusted management REITs and CR-REIT: special purpose company</li> </ul>	<ul style="list-style-type: none"> <li>- Self-managed REITs (REIC): KRW 7 billion</li> <li>- Entrusted management REITs and CR-REITs: KRW 5 billion</li> </ul>

## Legal form

A REIT can only be established as a stock corporation (called a Chusik Hoesa) under the Korean Commercial Code and REICA.

Entrusted management REITs and CR-REITs are paper companies (special purpose company). CR-REITs have finite lives, which should be stated in Articles of Incorporation, and should be dissolved when the period elapses.

The seat of a REIT must be established in Korea.

### Minimum share capital

Under REICA, KRW 0.5billion is required as the minimum capital for obtaining a business license in case of Self-managed REITs and KRW 0.3billion is required in case of Entrusted management REITs and CR-REITs (Corporate Restructuring REITs). After this official permission, REIT should increase its equity capital within six months up to the following. The preparation period may be extended if it takes time to implement the methods and procedures set forth in other Acts.

Self-managed REITs (REIC): KRW 7 billion.

Entrusted management REITs and CR-REITs (Corporate Restructuring REITs): KRW 5 billion.

### c. Shareholders requirements/listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- AA shareholder may not own more than 50% of the shares in case of Self-managed REIT and Entrusted management REITs</li> <li>- There are no restrictions on foreign shareholders</li> </ul>	Yes

### Shareholder requirements

There are shareholding limitations as follows:

1. One shareholder and anyone who is specially related with the former shall not possess in excess of 50% in case of Self-managed REITs and Entrusted management REITs (hereinafter referred to as the 'upper limit of possession of stocks per person') of the total stocks issued by a REIT with an exception provided by Enforcement Decree of REICA;
2. Where a stockholder and the especially related person (hereinafter referred to as the 'same person') possess stocks of a REIT in excess of the upper limit of possession of stocks per person in violation of paragraph (1), the extent of exercise of voting right shall be limited to the upper limit of possession of stocks per person;
3. At least 30% of the shares must be offered to the public within two years from official permission (When the amount of investment in real estate development project accounts for 30% or more of the real estate development company's total asset, the date of permission refers to the day of approval or authorisation for the real estate development project)

However, the above-mentioned limitations do not apply to the case where certain shareholders (ex. Korean National Pension Corporation, etc.) hold 30% or more shares in REICA.

Currently, there are no special restrictions on foreign shareholders.

### Listing requirements

When a REIT becomes qualified to meet the listing standards under the Financial Investment Services and Markets Act, the REIT must list its stocks on the securities market of the Korea Stock Exchange or register them with the Korea Securities Dealers Association and make them traded either in the securities market of the Korea Stock Exchange or in the association brokerage market of the Korea Securities Dealers Association.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- 70% must be invested in real estate
- 80% must be invested in real estate, real estate-related securities and cash
- Not clear whether there are any restrictions for investment abroad either directly or indirectly
- Asset-management company must have performance in invest or management for 3 years
- Investment in a single property is possible
- Investment in residential property is allowed
- Investment in subsidiaries is not allowed since REIT cannot acquire more than 10% of voting shares in other companies

As of the end of each quarter, 80% or more of the total assets of a REIT must be real estate, real estate-related securities and cash, and 70% or more of the total assets of a REIT must be real estate (including buildings under construction).

In addition to those requirements, 70% or more of the total assets must be corporate recovery-related real estate in case of a CR-REIT. Corporate recovery-related real estate includes real property which a company sells to repay its debts to a financial institution, real property which a company sells to implement agreements with a financial institution providing debts to the company and real property which a company sells for corporate recovery under relevant laws.

When calculating the rate of investment in the real estate development project, the price of land possessed by a real estate company is included in the total asset but is excluded from the total amount of investment in the development project. In case of newly constructing or reconstructing buildings.

For REITs, the minimum holding period of domestic real estate is one year unless for the certain case of unsold housings and the minimum holding period of overseas real estate is the period as stipulated under the Articles of Association, respectively. For CR-REITs there are no restrictions. Also, an asset-management company must have performed in investment or management for three years; if not fulfilled, the authorisation would be cancelled.

A REIT is not allowed to hold more than 10% of voting shares in other companies with an exception, including a merger and an acquisition of a business.

Currently, there is no clear rule on a REIT holding real estate in a foreign jurisdiction, and thus, legal advice is required.

#### e. Leverage

##### Leverage

Maximum Debt: Equity ratio of 2:1

A REIT can borrow funds or issue bonds within twice the equity value. If there is a special resolution by the general stockholders' meeting, a REIT can borrow funds or issue bonds within ten times the equity value.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
90% or more of distributable income	Included in operative income	Depends on the Articles of Association

### Operative income

A REIT must distribute 90% or more of distributable income. (A self-managed REIT must distribute 50% or more distributable income until the end of 2018).

There is no difference between a domestic and cross-border profit distribution. The timing of the distribution depends on the Articles of Association.

### Capital gains

Capital gains are subject to the distribution obligation.

## g. Sanctions

Penalties/loss of status rules
<ul style="list-style-type: none"> <li>- Imprisonment penalty</li> <li>- Fine not exceeding KRW 50 million</li> <li>- Revoke the establishment of REIT</li> </ul>

If the required asset level is not met, there is imprisonment penalty and a fine not exceeding KRW 50 million. Also, the Minister of Land, Transport and Maritime Affairs may revoke the establishment of REIT status if the required profit distribution is not met.

Any deviation from its obligations according to the applicable law results in regulatory action (i.e. penalty, withdrawal of the license, etc.).

Where the same person possesses stocks in excess of the upper limit of possession of stocks per person, the Minister of Construction and Transportation may order him to dispose of the stocks that are in excess of the upper limit of possession of stocks per person.

In case where the same person holds stocks in excess of the upper limit of possession of stocks per person after making his investment in kind, notwithstanding the provisions of paragraph (3), the Minister of Construction and Transportation may order him to dispose his stocks that are in excess of the upper limit of possession of stocks per person during the period ranging from not less than one year to not more than one year and six months from the date on which the stocks are issued after the investment in kind is made.

Where the Minister of Construction and Transportation finds that a REIT fails to list its stocks on the securities market of the Korea Stock Exchange, or register with the Korea Securities Dealers Association without sound reasons, he may order the REIT to be listed or register its stocks within a period of time to be designated by him.

### 3 Tax treatment at the level of the REIT

#### a. Corporate income tax

Current income	Capital gains	Withholding tax
Income technically tax-exempt, if 90% distribution requirement met	Income technically tax-exempt, if 90% distribution requirement met, but in certain cases 11% capital gains surtax	<ul style="list-style-type: none"> <li>- No withholding tax levied on domestic distribution</li> <li>- Entitled to claim a foreign tax credit with a certain ceiling of the tax credit</li> </ul>

#### Current income

Entrusted-management REIT and CR-REIT can claim a dividend paid deduction, if 90% of the distributable income is distributed as dividends and thus, technically, the corporate income tax of REIT can be nil.

Otherwise (REIC) the company is subject to corporate income tax at a rate of 10% for the first taxable income up to KRW 200 million and 20% for the second taxable income up to KRW 20 billion and 22% for third taxable income up to KRW 20 billion and 25% for over the KRW 300 billion thresholds. 10% of corporate income tax is additionally levied on a local resident as local income tax.

#### Capital gains

Under Korean Corporate Income Tax Law, the treatment of capital gains constitutes as ordinary income subject to the ordinary corporate income tax rate. There is no tax on capital gains if the 90% distribution obligation is met.

In addition, the capital gains surtax at a rate of 11% could be imposed on the sale of certain tainted assets such as housing or non-business purposes land. The 11% capital gains surtax should be imposed additionally also if the 90% distribution obligation is met.

#### Withholding tax

If a REIT receives a distribution of a domestic company, no withholding tax is levied. The REIT is entitled to claim a foreign tax credit with a certain ceiling of the tax credit.

#### Other taxes

There are no other taxes levied on corporate income.

#### Accounting rules

A financial statement single (not consolidated) should be prepared in accordance with Korean GAAP or Korean IFRS.

## b. Transition regulations

### Conversion into REIT status

N/A

## c. Registration duties

### Registration duties

- Acquisition tax
- Registration tax

In general, when real estate in Korea is purchased by a company or constructed in Korea, 4.6% or 3.16% acquisition tax is imposed on the purchase price. There is no more registration tax when real estate is registered for the reason of the acquisition of real estate.

On the other hand, the acquisition tax will be levied in accordance with a certain formula respectively if (i) the real estate is newly constructed or is used for head office in Seoul Metropolitan Area (SMA) or (ii) the real estate acquired by a company which has been registered in SMA for less than five years and is located in the SMA.

In addition, the capital registration tax is levied at the rate of 0.48% to 1.44% of the total par value amount of paid-in capital.

# 4 Tax treatment at the shareholder's level

## a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Subject to corporate income tax and resident surtax</li> <li>- No difference between current income dividend and capital gains dividend</li> <li>- Capital gains on disposal are subject to the ordinary income tax rate</li> </ul>	<ul style="list-style-type: none"> <li>- A withholding tax of 15.4% final levied if interest and dividend income do not exceed KRW 20 million</li> <li>- Capital gains are tax-exempt if certain thresholds are met</li> </ul>	<ul style="list-style-type: none"> <li>- No withholding tax for a domestic corporation</li> <li>- A final withholding tax on distributions of 15.4% for Korean individual residents</li> </ul>

### Corporate shareholder

A dividend is subject to corporate income tax. There is no difference between current income dividend and a capital gains dividend under the Korean tax law.

A return of capital distribution (capital redemption/retirement) may be a deemed dividend: the sum of funds and the value of other assets acquired by a shareholder in return for the retirement of stocks and redemption of capital in excess of the acquisition costs of the capital would be deemed as dividends. The deemed dividend is subject to corporate income tax.



“Under Korean Corporate Income Tax Law, the treatment of capital gains constitutes as ordinary income subject to the ordinary corporate income tax rate.”

### Individual shareholder

There is no difference between current income dividends and a capital gains dividend under Korean Law. The withholding tax of 15.4% is a final levy if interest and dividend income do not exceed KRW 20 million. If the aggregate interest and dividend income exceed KRW 20 million, the individual is subject to the ordinary individual income tax rates ranging from 6.6% to 46.2%.

A return of capital distribution (capital redemption/retirement) may be a deemed dividend: the sum of funds and the value of other assets acquired by a shareholder in return for the retirement of stocks and redemption of capital in excess of the acquisition costs of the capital would be deemed as dividends. The deemed dividend is subject to withholding tax.

Individuals who hold less than 1% of listed REIT shares and also proceeds from the sale of the listed REIT shares are less than KRW 1.5 billion (1 billion on and after 2020.04.01 to 2021.03.21 and 0.3 billion on and after 2021.04.01), are exempted from the income tax on capital gains. Otherwise, individuals are subject to income tax.

### Withholding tax

If the shareholder is a domestic corporation, the dividend paid by a REIT is not subject to withholding tax. If the shareholder is a Korean individual resident, the dividend paid by a REIT is subject to 15.4% withholding tax.

If the shareholder is a foreign resident or corporation, the dividend paid by a REIT is generally subject to 22% withholding tax. Such withholding tax could be reduced depending on the applicable tax treaty between Korea and the country where the shareholder is a resident.

In general, withholding tax should be collected when the dividend is paid. The dividend which is declared by a REIT but not paid to its shareholders within three months from the date of declaration of the dividend is deemed to be paid at the end of such three-month period.

#### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- A withholding tax of 22%</li> <li>- Can be reduced according to a tax treaty</li> </ul>	<ul style="list-style-type: none"> <li>- A withholding tax of 22%</li> <li>- Can be reduced according to a tax treaty</li> </ul>	Tax treaty relief is available

### Corporate shareholder

A dividend is subject to Korean withholding tax at a rate of 22% and can be reduced according to a tax treaty. There is no difference between current income dividend and a capital gains dividend.

A return of capital distribution (capital redemption/retirement) may be a deemed dividend: the sum of funds and the value of other assets acquired by a shareholder in return for the retirement of stocks and



redemption of capital in excess of the acquisition costs of the capital would be deemed as dividends. The deemed dividend is subject to Korean withholding tax at a rate of 22% and can be reduced according to a tax treaty.

Capital gains realised on the sale of the REIT shares are subject to the Korean withholding tax. The withholding tax rate for residents in non-treaty countries for REIT shares is the lower of 22% of the gain or 11% of the gross proceeds, and the foreign shareholder is required to file a tax return on the capital gains taxed at the rate of 22% (the withheld tax is creditable). However, there is an exception. Capital gains earned by a non-resident from the transfer of listed REIT shares through the Korean Stock Exchange or KOSDAQ are tax-exempt if such non-resident, together with its certain related parties, hold or have held less than 25% of the REIT shares at all times during the calendar year of the share transfer and the immediately preceding five calendar years.

### Individual shareholder

For a foreign individual, the dividend paid by a REIT is subject to a 22% withholding tax, but the withholding tax can be reduced depending on a tax treaty. There is no difference between current income dividend and a capital gains dividend.

The treatment of a return of capital distribution and capital gains realised on the sale of REIT shares earned by an individual shareholder is not different from a corporate shareholder.

### Withholding tax

For a foreign individual or company, the dividend paid by a REIT is subject to a 22% withholding tax, but the withholding tax can be reduced depending on a tax treaty.

In general, withholding tax should be collected when the dividend is paid, but the dividend which is declared by a qualified REIT but not paid to its shareholders within three months from the date of declaration of the dividend is deemed to be paid at the end of such three-month period.

## 5 Treatment of the foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
Tax privileged with its Korean rental income	No specific tax privilege	No specific tax privilege

### Foreign REIT

A foreign REIT should report its Korean sourced rental income to the Korean tax authorities and should pay Korean income tax as if the REIT is a Korean resident (i.e. a Korean permanent establishment of the foreign REIT is created).

### Corporate shareholder

A Korean corporate shareholder of a foreign REIT is subject to corporate income tax on the distribution received by the foreign REIT and can claim a foreign tax credit.

## Individual shareholder

A Korean individual shareholder of a foreign REIT is subject to individual income tax on the distribution received by the foreign REIT and can claim a foreign tax credit. ■

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A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
Taiwan REIT/REAT	Enacted in 2003 Last amended in 2017	Real Estate Securitisation Act	Trust type

In Taiwan, the Real Estate Securitisation Act (RESA) was enacted in 2003 and was last amended in 2017. The REIT (Real Estate Investment Trust) and REAT (Real Estate Asset Trust) structures are legally regulated by the RESA. The REIT and REAT structures are both in the form of a trust. The distinction is that a REIT will accept funds from investors, which will be invested in specified properties, whereas a REAT will accept properties from a settler and then issue beneficiary certificates representing those properties.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Taiwan	7	0	EUR 3,100	0.00%

\* EPRA, June 2018.

# 2 Requirements

## a. Formalities/procedure

### Key requirements

The trustee shall submit certain documents to the competent authority (the Financial Supervisory Commission) for approval or effective registration

According to Article 6 of the RESA, to publicly-offer or privately-place REIT Beneficial Securities, the trustee shall submit the following documents to the competent authority for approval or effective registration:

- REIT plan;
- REIT trust agreement;
- comparison table of the REIT trust agreement against the model of a standard trust agreement published by the industry association;
- prospectus or investment memorandum;
- documentation evidencing that the operating and managerial personnel of the REIT Fund is in compliance with the regulations prescribed by the competent authority;
- name list, documentation of qualifications, and appointment agreement of the Trust Supervisor, if any;
- minutes of the resolution adopted by the trustee's board of directors for the public offer or private placement of REIT Beneficial Securities;

- explanations regarding the method of managing and disposing of the trust property: Where a real estate management institution is appointed to manage or dispose of trust property, the appointment agreement or other documentary proof is needed;
- case examination tables filled out by the trustee and reviewed by a CPA or lawyer;
- the legal opinion of a lawyer; and
- other documentation as required by the competent authority.

For trustee companies purely engaged in the business of a real estate investment trust or a real estate asset trust, the competent authority may prescribe rules for the minimum issued capital, shareholders' structure, qualifications of the person responsible for the company, the expertise and experience of the company's management, and its business activities.

## b. Legal form/minimum initial capital

	Legal form	Minimum initial capital for trustee
REIT/ REAT	Trust Asset held by the trustee	Depending on the scope of business engaged by the trustee (ranging from NT\$ 300 million to NT\$ 2 billion)

### Legal form

REITs and REATs are established as trusts and are administered by a trustee. The term 'trustee' refers to an institution that may manage and dispose of the trust property and publicly offer or privately place Beneficial Securities of the REIT/REAT, and is limited to the trust enterprises defined in the Trust Enterprise Act. In practice to date, trustees have been local banks or branch offices of foreign banks in Taiwan.

According to the Trust Enterprise Act, except for banks approved by the competent authority to conduct a trust business, a trust enterprise may only be a company limited by shares. The trustee of a REIT or REAT must also meet the following criteria:

- be engaged in the trust business pursuant to the Trust Enterprise Act;
- be established for at least three years; and
- have a credit rating no less than the rating requirement prescribed by the competent authority.

A trust company shall be a public company, which means that it is regulated under the Securities and Exchange Act as well as the Company Act and the shares to such trust company are publicly-offered.

### Minimum initial capital

To apply to establish a trust company, the minimum paid-in capital of ranges from TWD 300 million to TWD 2 billion depending on the scope of business engaged by the trustee. The capital contributions must be made in cash only. The minimum paid-in capital required for a trust company engaging only in real estate investment trust (REIT) business under the RESA is TWD 1 billion; the minimum paid-in capital for a trust company engaging only in real estate asset trust ('REAT') business is TWD 300 million; and the minimum paid-in capital for a trust company engaging in both REIT and REAT business is TWD 1 billion.

### c. Certificate holder requirements/listing requirements

Unitholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- With regard to a public offering, certificates shall be held by at least 50 persons for at least 335 days during a fiscal year; and any five certificate holders shall not own more than ½ of the total value of the certificates issued</li> <li>- With regard to a private placement, the investors should be banks, finance bills enterprises, trust enterprises, insurance enterprises, securities enterprises, other juristic persons or institutions approved by the competent authority; or a natural person, juristic person or fund that meet the requirements as prescribed by the competent authority; and the total investors of the natural person, juristic person and the fund above shall not exceed 35 persons in number</li> </ul>	No

#### Unitholder requirements

With regard to a publicly-offered REIT or REAT, certificates shall be held by at least 50 persons for at least 335 days during a fiscal year; it is not required for the 50 persons to be the original holders of certificates. Any five certificate holders shall not own more than 1/2 of the total value of the certificates issued – except for independent professional investors.

With regard to a privately-placed REIT or REAT, the investors should be banks, finance bills enterprises, trust enterprises, insurance enterprises, securities enterprises, other juristic persons or institutions approved by the competent authority; or a natural person, juristic person or fund that meet the requirements as prescribed by the competent authority. The total investors of the natural person, juristic person and the fund above, shall not exceed 35 persons in number.

According to Article 6 of the Standards for the Establishment of Trust Enterprises (SETE), the same person or same related parties respectively may not hold shares in the same trust company in an amount exceeding 25% of the total number of shares issued. The term 'same person' means the same natural person or the same juristic person; the term 'same related parties' includes the person, his or her spouse, blood relatives within the second degree, and enterprises of which the person or his or her spouse is a responsible person (i.e. Chairman, General Manager or another person in accordance with Taiwan Company Law); and the juristic person controls or is controlled by or is under common control with the juristic person shareholder.

#### Listing requirements

According to Article 3 of the SETE, the trustee company shall be a public company.

For the beneficial securities originally privately placed, they are now allowed opportunity to be listed in Taiwan Stock Exchange or Taipei Exchange. After three years from the delivery date of such beneficial securities, under the conditions that the real estate or related rights of real estate invested in has a stable income, the trustee may apply for listing in Taiwan Stock Exchange or Taipei Exchange with sufficient credit enhancement methods.

The beneficial securities issued by the trustee can be publicly offered or privately placed.

#### d. Asset level/activity test

##### Restrictions on activities/investments

Investment in real estate, related rights of real estate, securities of real estate, as well as other investment objects approved by the competent authority

According to Article 17 of the RESA, the investment or utilisation of REIT funds shall be limited to the following objects:

1. existing real estate with stable income or real estate to be developed (including the foreign real estate held via a foreign special purpose vehicle wholly owned by the REIT trustee and solely for the purpose of investment in foreign real estate);
2. related rights of real estate with stable income or of real estate to be developed. Such “rights” refer to the superficies and other rights approved by the competent authority;
3. securities relating to real estate;
4. permitted utilisation as prescribed in Article 18 of the RESA; or
5. other investment or utilisation objects approved by the competent authority.

The total investment amount of the real estate to be developed and the related rights of real estate shall not be greater than 15% of the net worth of the publicly-offered REIT or 40% of the net worth of the privately-placed REIT with an exempt that for the investment of a privately-placed REIT in public construction, the said ratio could be up to 100%.

The total investment amount in foreign REITs, together with other beneficial certificates issued pursuant to RESA and Financial Asset Securitisation Act shall not be greater than 25% of the net worth of the REIT.

The total investment amount in single foreign REIT shall not be greater than 5% of the net worth of the REIT.

The total investment amount in foreign real estate, together with foreign REITs, shall be less than 50% of the net worth of the REIT.

The total investment amount of cash (including bank deposits), government bond and items 1 to 3 above shall not be lower than 75% of the net worth of the REIT.

The total investment amount in the securities set forth under the Securities and Exchange Act shall not be greater than 40% of its offering limit and TWD 600 million, provided that the investment in item 3 above is not restricted.

The total investment in the short-term commercial paper of any company shall not be greater than 10% of the net worth of the REIT as of the investment date.

The total amount of bank deposits, bank guarantees, bank acceptances or short-term commercial papers with any one financial institution shall not be greater than 20% of the net worth of the REIT or 10% of the net worth of the financial institution as at the investment date.

The total investment in certificates or asset-backed securities issued or delivered by trustee institutions or special purpose companies shall not be greater than 20% of the net worth of the REIT as at the investment date.

According to Article 18 of the RESA, the utilisation of idle funds of the REIT Funds shall be limited to the following objects:

1. bank deposits;
2. purchase of government bonds or financial bonds;
3. purchase of treasury bills or negotiable certificates of time deposit;
4. purchase of commercial paper with a credit rating above a certain level or guaranteed or accepted by banks with a rating above the level stipulated by the competent authority; or
5. purchase of other financial products approved by the competent authority

#### e. Leverage

Leverage
50%

The trustee may borrow money with the trust property serving as collateral pursuant to the terms of the REIT Fund contract; however, the purpose of the borrowed money is limited to the needs of real estate operations and the distribution of profits, interests or other proceeds.

The trustee may grant real estate mortgage rights or other security interests over the trust property acquired with the borrowed money.

To ensure the financial health of the REIT Funds, the competent authority may prescribe an upper limit of the ratio regarding borrowings by the trustee. When the borrowings exceed the upper limit of the ratio, the trustee shall make adjustments to the level of borrowing within the time prescribed by the competent authority. Currently, the upper limit is 50% of the net worth of the REIT depending upon its credit rating.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
Pursuant to the REIT contract	Pursuant to the REIT contract	Within six months after the closing of the fiscal year

According to Article 28 of the RESA, the proceeds derived from the REIT investment shall be distributed pursuant to the scheme provided in the REIT contract within six months after the closing of the fiscal year.

#### g. Sanctions

Penalties/loss of status rules
Transfer REIT/REIT to another trustee

According to Article 55 of the RESA, if the trustee is not in compliance with the related law and regulations, the competent authority may appoint a new trustee for the REIT or REAT.



### 3 Tax treatment at the level of the REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Tax-exempt	Tax-exempt	Refundable if the tax withheld exceeds the payable amount

#### Current Income

The trustee is considered a pass-through entity in terms of tax. Therefore, the income generated from the operation of the REIT funds is not subject to corporate income tax at the trustee level.

#### Capital gains

The trustee is considered a pass-through entity in terms of tax. Therefore, capital gains generated by the operation of the REIT funds are not subject to corporate income tax at the trustee level. However, the Land Value Increment Tax, applicable to the increase in sale value over purchase value of land, will be paid by the REIT upon the sale of the real estate.

#### Withholding tax

According to Article 89-1 of Income Tax Act, withholding tax on the revenue arising from the trust property shall be withheld at source in the name of the trustee at the prescribed rate under the Income Tax Act. The withholding rate applied depends on the category of income. Generally, interest income of REIT will be subject to a 10% withholding rate. Rental revenues received by the trustee will not be subject to withholding if the GUIs (Government Uniform Invoice) issued by the trustee or the tenants are individuals. Withholding tax withheld may be recovered by the trustee from the tax authority if the tax withheld exceeds the payable amount.

#### Other taxes

The trustee is the taxpayer of land value tax imposed on the registered owner of the property under Article 3-1 of the Land Tax Act.

#### b. Transition regulations

Conversion into REIT status
N/A

### c. Registration duties

#### Registration duties

- There are registration fees for the formation of the trustee
- There is no tax/fee/duty imposed on the issuance of the beneficial securities

No duty is imposed on the issue of beneficial securities.

## 4 Tax treatment at the unitholder's level

### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- The distribution shall be consolidated into gross corporate income since January 1, 2010</li> <li>- Capital gains are corporate tax exempt but subject to alternative minimum tax</li> </ul>	<ul style="list-style-type: none"> <li>- The withholding tax is the final levy on distributions</li> <li>- Capital gains are tax-exempt</li> </ul>	A final withholding tax of 10%

#### Corporate unit holder

The distributed amount shall be the beneficiary's interest income.

Capital gains from the sale of beneficiary certificates are exempt from corporate income tax; however, such gain will be subject to the alternative minimum tax (AMT). Taiwan companies or foreign companies having permanent establishments entitling them to tax-exempt capital gains, claiming tax holidays or other tax incentives in Taiwan must calculate AMT income by using taxable income calculated in accordance with the regular income tax system, plus the add-back of certain tax-exempted income. Taiwan companies are required to compare their regular income tax against their AMT income tax and pay whichever is higher. The AMT rate for companies is currently at 12% with an exemption if AMT income does not exceed TWD 0.5 million.

#### Individual unit holder

The distributed amount shall be the beneficiary's interest income.

Capital gains from the sale of beneficiary certificates are exempt from individual income tax.

#### Withholding tax

Distributions to domestic individual unitholders will be subject to 10% withholding tax, which is the final tax for domestic individual unitholders of REITs (the distributions received by the unitholders are not included in the unitholders' personal income tax returns). The 10% withholding tax is not creditable against the unitholder's individual tax payable resulted from other sources of income. Distributions to domestic corporate unitholders will be consolidated into the gross corporate income of the domestic corporate unitholders.

## b. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding tax
A final withholding tax of 15%	A final withholding tax of 15%	No tax treaty relief available

### Corporate unitholder/individual unitholder

Capital gains from the sale of beneficiary certificates by foreign unitholders are exempt from income tax.

### Withholding tax

The distribution to foreign corporate unitholders or foreign individual unitholders will be subject to 15% withholding tax, which is the final tax for the foreign unitholders unless otherwise provided by available tax treaties with specific jurisdictions.

## 5 Tax treatment of foreign REIT and its domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
<ul style="list-style-type: none"> <li>- Investment income is subject to withholding tax</li> <li>- Capital gains are tax-free</li> </ul>	Corporate income tax	Needs further clarification

**The tax implications for foreign REIT and its domestic unitholders are not clear under the current tax regulations. The following analysis is for reference purpose only.**

### Foreign REIT

The tax implications will depend on the nature of the investment income. Except for the preferential rate provided under applicable tax treaties, investment income (including interest and dividends from approved investments) will be subject to a 20% withholding rate. The capital gains attributable to Taiwan securities investments (including government bonds, corporate bonds and shares) are tax-exempt.

### Corporate unitholder

For Taiwan-incorporated profit-seeking enterprises, corporate income is assessed on a worldwide basis. Thus, Taiwanese companies shall include income distributed by foreign REITs for their income tax purposes. Foreign tax relief is applicable under Article 3 of the Taiwan Income Tax Act.

### Individual unitholder

Individual income tax is imposed only on Taiwan-sourced income. An individual's overseas investment income shall be subject to AMT since January 01, 2010. However, based on our oral consultation on a no-name basis with the Ministry of Finance, the income (both the dividends and the profit from selling the position held) received from a foreign REIT investing in Taiwan assets would be considered as individual unitholder's non-Taiwan sourced income. ■

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GLOBAL  
REIT SURVEY

ASIA - PACIFIC

# Thailand

PFPO and REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
PFPO	1992	Securities and Exchange Act B.E. 2535	Fund type
REIT	2007	- Trusts for Transactions in the Capital Market Act B.E. 2550 - Securities and Exchange Act B.E. 2535	Trust type

The Type I Property Fund, the property fund for public offering (PFPO), is the first type of real property mutual fund and is listed on the Stock Exchange of Thailand (SET).

The PFPO is established for the purpose of raising funds from the public to invest in income-producing real property (office buildings, service apartments, industrial factories, etc.).

In late 2012, the Office of Securities and Exchange Commission of Thailand (SEC) has announced a new type of the property trust fund called Real Estate Investment Trusts (“REIT”), trying to supplant the PFPO.

REIT is established to provide a modernized vehicle which differs in many respects from the PFPO to offer more flexibility and impose less restriction. While the PFPO is a juristic structure, REIT is a trust fund structure whereby the ownership of the property is held by a trustee. REIT has more advantages than the PFPO. For example, REIT can invest in real estate located overseas and can borrow up to 60% of total assets if rated as investment grade.

The law regulating the PFPO and REIT is the Securities and Exchange Act B.E. 2535. It was enacted in 1992.

However, REIT is additionally governed by the Trusts for Transactions in the Capital Market Act B.E. 2550.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Thailand	60	1	EUR 13,066	0.05%

## Top REIT\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield	% of Global REIT Index
WHA Premium Growth Freehold & Leasehold REIT	EUR 1,120	111.37%	4.10%	0.05%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedures

#### PFPO

##### Key requirements

- PFPO can only be established and managed by an Asset Management Company (AMC) through a Public Offering
- AMC must be licensed by the Thailand Ministry of Finance

The Type I Property Fund can only be established and managed by an Asset Management Company (AMC) through a Public Offering (PO). Based on the SEC's policy, no new PFPO can be set up from January 1, 2014. Additionally, the existing PFPOs are not allowed to extend their size thereafter.

The AMC must be licensed by the Thailand Ministry of Finance and regulated by SEC.

While the AMC is responsible for setting up and managing the fund, there is a fund supervisor ensuring that the AMC will operate the fund in accordance with the scheme. Also, an expert property service provider is occasionally appointed by AMC to carry on the day-to-day operation of the property.

#### REIT

##### Key requirements

- REIT can be established and managed by REIT Manager (the RM) which can be AMC or the qualified company through a PO
- A trustee is responsible for monitoring the activities of the the RM

REIT can be established by the trust settlor through giving a Trust Certificate (TC) to the beneficial owner. The trust settlor can be the same person as the the RM, which can be an AMC or the qualified company through a PO.

To be the RM, the AMC or qualified company must be the company with expertise in real estate investment and management.

Based on the trust concept, the RM is a responsible person for setting up and managing the REIT. The trustee, who has the legal right over the properties in terms of ownership, is significantly responsible for monitoring the activities of the RM in order to ensure that the RM will operate the REIT in accordance with the scheme, receive profits from properties and distribute them to beneficial owners.

The trustee must be completely independent of the RM, hold a trustee's license authorised by SEC and has registered and paid-up capital from THB 100 million or more.

## b. Legal form/minimum initial capital

### PFPO & REIT

Legal form	Minimum share capital
PFPO: Mutual Fund REIT: Trust	THB 500 million

#### Legal form

The PFPO is a mutual fund under Thai law, however, a REIT is a trust under the Trust Act.

#### Minimum initial capital

A capital of minimum THB 500 million is required.

## c. Unit holder requirements/listing requirements

### PFPO

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- At least 250 unitholders are required for an IPO</li> <li>- At least 35 unitholders are required after SET listing<sup>1</sup></li> <li>- No more than 33.33% of unitholders can be related persons<sup>2</sup></li> <li>- No more than 49% of unitholders can be foreign investors, in the case the property fund directly owns (i) land or (ii) a -condominium more than 49% of the total area including the area owned by other existing foreign owners<sup>3</sup></li> </ul>	Yes

#### Unitholder requirements

The minimum number of unitholders is 250 unitholders for an IPO and 35 unitholders after listing in the SET.

Former property owners and related persons, i.e. three layers above and below (of at least 10% shareholding at each layer) the institutional investors, shall not acquire more than one-third of the total units sold.

The 'small lot first' practice is in place for units allocation. This practice means the fund units will be allocated to those subscribed in small lots first, before being allocated to those subscribed in 'big' lots.

<sup>1</sup> No. 77 (1) of the SEC's Regulation No. SorNor. 25/2552 effective from August 16, 2009 onwards.

<sup>2</sup> SEC's Regulation No. SorNor. 26/2552 effective from August 16, 2009 onwards.

<sup>3</sup> SEC's Regulation No. SorNor. 53/2552 dated October 29, 2009 effective from November 16, 2009 onwards.

<sup>4</sup> SEC's Regulation No. TorJor. 49/2555 dated November 21, 2012 effective from January 01, 2013 onwards.



## Listing requirements

Listing at the SET is mandatory.

## REIT

Unitholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- At least 250 unitholders are required for an IPO and at least 20% of the units must be sold to public investors</li> <li>- At least 35 unitholders are required after the SET listing</li> <li>- At least 15% of the units should be held by public investors in each tranche</li> <li>- No more than 50% of unitholders can be related persons</li> <li>- Foreign investor limit must be complied with the laws related to the real estate invested by the REIT</li> </ul>	Yes

## Unitholder requirements

The minimum number of unitholders is 250 for an IPO and 35 after listing in the SET.

Former property owners and related persons shall not acquire more than 50% of total units sold of each tranche (if any).

No specific percentage for the foreign investment in REIT is provided under the SEC rules. However, if the REIT invests in more than one project, the percentage of foreign investment in the REIT is capped at the lowest percentage allowed by the related laws for foreign ownership among the projects.

## Free float

At least 15 % of the unit must be held by public investors in each tranche.

## Listing requirements

Listing at the SET is mandatory.

## d. Asset levels/activity test

## PFPO

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- 75% of the net asset value invested in property</li> <li>- Property must be at least 80% complete</li> <li>- Property must be located in Thailand</li> <li>- The PFPO cannot purchase real property in dispute</li> <li>- Property insurance is required</li> <li>- AMC must conduct feasibility studies before investment decisions are made</li> <li>- AMC must appoint a property appraiser, property prices are based on appraisals</li> <li>- Property is re-evaluation every two years</li> </ul>

No less than 75% of the net asset value must be invested in property. The fund may only invest in completed property or property that is at least 80% complete. Also, the PFPO may only invest in property which is located in Thailand. Real property in dispute is not allowed to be purchased or leased. Additionally, property insurance is required.

The fund can generate capital gain income of at most 25% of the total income.

The AMC is required to conduct feasibility studies for investment decision-making. Acquisition and disposal prices must be based on an appraisal price. To purchase/dispose property, the AMC must appoint a property appraiser approved by the SET to appraise the property and disclose the results to investors. Properties must be revalued every two years.

A PFPO may invest in subsidiaries.

## REIT

### Restrictions on activities/investments

- 75% of the net asset value invested in real estate ready to generate income
- Investment in any type of real estate is permissible, except real estate involving illegal or immoral business
- Overseas real estate is allowed to invest
- No more than 10% of total assets are allowed to invest in real estate under construction
- Indirect investment may be made through at least 99% of the REIT's own subsidiary
- Property re-evaluation every two years<sup>5</sup>

No less than 75% of the net asset value must be invested in real estate ready to generate income.

No restriction on the type of real estate investment is imposed while investment overseas is allowed. However, the real estate involving illegal or immoral business is not allowed.

The fund may invest in projects under construction (Green field project) up to 10% of the net asset value.

The RM is required to conduct feasibility studies and due diligence for investment decision-making<sup>6</sup>. Acquisition and disposal prices must be based on an appraisal price. Properties must be revalued every two years.

From April 16, 2016, indirect investment through at least 99%<sup>7</sup> of the REIT's own subsidiary may be made, providing that REIT subsidiary also complies with REIT investment regulations.

## e. Leverage

### PFPO

#### Leverage

Borrowing of not more than 10% of its total assets is allowed under specified conditions

The PFPO is allowed to borrow not more than 10% of its total assets. However, the AMC is required to

<sup>5</sup> SEC's Regulation No. SorRor. 26/2555 dated November 21, 2012 effective from January 1, 2013 onwards.

<sup>6</sup> SEC's Regulation No. SorChor. 29/2555 dated November 21, 2012 effective from January 1, 2013 onwards.

<sup>7</sup> SEC's Regulation No. TorJor. 49/2555 dated November 21, 2012, amended on February 20, 2019.

specify the borrowing in the PFPO Management Project and Prospectus and to comply with the specified conditions of SEC<sup>8</sup>.

## REIT

### Leverage

Borrowing of not more than 35% of its total assets is allowed, and extended to 60% of its total assets if rated as investment grade

REIT may apply for a loan facility up to 35% of its total assets, and the limit will be shifted up to 60% of its total assets if rated as investment grade.

## f. Profit distribution obligations

### PFPO & REIT

Operative income	Capital gains	Timing
90% of net profit	90% of net profit	Within 90 days of the end of each accounting period

### Operative income

At least 75% of the total income of the fund must be generated from rental income. At least 90% of the net profit must be distributed to unit holders within 90 days after the end of each annual accounting period<sup>9</sup>.

### Capital gains

Also at least 90% of capital gains are to be distributed. As a maximum, 10% of the net profit can be retained by the fund without being distributed to the unit holders.

## g. Sanctions

### PFPO & REIT

### Penalties/loss of status rules

Units may be delisted as listed securities if they fail to the unit holder requirements

<sup>8</sup> SEC's Regulation No. KorNor. 11/2552 dated July 20, 2009 effective from August 16, 2009 onwards.

<sup>9</sup> SEC's Regulation No. SorRor. 26/2555 dated November 21, 2012 effective from January 01, 2013 onwards.

### 3 Tax treatment at the level of the REIT

#### REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
Not subject to income tax but a 12.5% Land and Building tax on rental income of immovable properties levied	Tax-exempt	N/A

#### Current income

A REIT is not subject to income tax, but it pays a 12.5% Land and Building Tax on the annual rental income of immovable properties.

#### Capital gains

REIT is not subject to income tax.

#### Withholding tax

REIT is not subject to withholding tax.

#### Other taxes

REIT should be subject to VAT on service income, sale of goods and movable properties. Likewise, income from the disposal of immovable properties are subject to Specific Business Tax (SBT). REIT is also subject to Stamp Duty.

REIT has to pay a once-off registration fee of 1% on the amount of rental fee of immovable properties (only if the lease period is more than three years); and 2% transfer fee of the official appraised price for the income on disposal of immovable properties. The official appraised price refers to the value of the immovable properties (according to its type and location) assessed by the Land Department.

#### Accounting rules

REIT is to observe the Thai Generally Accepted Accounting Principles.

#### PFPO

## b. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Not subject to income tax, but a 12.5% Land and Building tax on rental income of immovable properties levied</li> <li>- From May 24, 2017, PFPO is subject to VAT, SBT and SD</li> </ul>	Tax-exempt	N/A

### Current income

PFPO is not subject to income tax, but it pays a 12.5% Land and Building Tax on the annual rental income of immovable properties.

### Capital gains

Capital gains are not taxed at the level of PFPO

### Withholding tax

On distributions to a PFPO, no withholding tax is levied.

### Other taxes

From May 24, 2017, PFPO is subject to VAT, SBT and SD<sup>10</sup>.

The PFPO is to pay a once-off registration fee of 1% on the amount of rental fee of immovable properties (only if the lease period is more than three years); and 2% transfer fee of the official appraised price for the income on disposal of immovable properties. The official appraised price refers to the value of the immovable properties (according to its type and location) assessed by the Land Department. The 2% transfer fee is reduced to 0.01% for the transfer of immovable properties to the property fund<sup>11</sup>.

### Accounting rules

The PFPO is to observe the Thai Generally Accepted Accounting Principles.

## c. Transition regulations

Conversion into REIT status
<ul style="list-style-type: none"> <li>- No direct conversion to REIT status is allowed</li> <li>- Income incurred from the conversion shall be subject to taxes</li> <li>- PFPO shall be subject to VAT, SBT and SD for the value of the tax base, income, an execution of instrument, respectively, incurred from the conversion</li> </ul>

10 Royal Decree issued under the Revenue Code governing exemption from Value Added Tax (No. 608) B.E. 2559 dated May 24, 2016; Royal Decree issued under the Revenue Code governing designation of business exempt from Specific Business Tax (No. 609) B.E. 2559 dated May 24, 2016; and

Royal Decree issued under the Revenue Code governing exemption from Revenue Taxes (No. 610) B.E. 2559 dated May 24, 2016.

11 Ministerial Regulation No. 47 (B.E.2541) Issued Under the Land Code B.E.2497

No direct conversion to REIT status is allowed. However, a PFPO can perform a conversion by selling its assets to REIT.

The real estate assets must be sold by an existing entity to REIT at market value.

Unitholders shall be subject to the Income Tax (Personal Income Tax or Corporate income tax) on income incurred from the conversion made from January 1, 2018 onwards.

PFPO shall be subject to VAT, SBT and SD for the value of the tax base, income, an execution of instrument, respectively incurred from conversion or creation of real rights or any property rights according to the conversion made from January 1, 2018 onwards.

#### d. Registration duties

Registration duties
Reduced transfer fee of 0.01%

In the case of selling an immovable property, there will be a 2% transfer fee levied on the appraised value of the property. However, if the property is sold to a property fund, such fee can be reduced to 0.01%, capped at THB 100,000. In practice, the responsibility of this property transfer fee would depend on the negotiation between the seller and the buyer, and if the negotiation is finalised, the clause regarding this property transfer fee should be stipulated in the sale and purchase agreement.

In the case of leasing an immovable property, there will be a 1% registration fee levied on the total rental income if the lease period is more than three years.

## 4 Tax treatment at the unitholder's level

### REIT

#### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
<ul style="list-style-type: none"> <li>- Profit distribution from a REIT must be included in the company's income and subject to CIT at the rate of 20%</li> <li>- The same tax implications on profit distribution are applied to capital gains (CIT 20%)</li> </ul>	<ul style="list-style-type: none"> <li>- Income tax of 5-35%</li> <li>- If the unitholder allows the REIT to deduct 10% withholding tax, this withholding tax is the final levy</li> <li>- A resident individual TC holder will be exempt from tax on the gain from the sale of trust units as the TC is traded in the SET</li> </ul>	<ul style="list-style-type: none"> <li>- A 10% withholding tax on distributions to an individual unitholder</li> <li>- A 10% withholding tax levied on distributions to a corporate unitholder</li> </ul>

### Corporate unit holder

The profit distribution from a REIT to a corporate unitholder will be included in the company's income and

subject to CIT at the rate of 20%<sup>12</sup>.

Similar to the profit distribution, 20% income tax is levied on capital gains.

### Individual unitholder

Individual unitholders are to pay 5-35% income taxes on profit distribution. If the unitholder allows the trustee to deduct 10% withholding tax upon payment, the withholding tax is the final levy.

### Withholding tax

If the individual unitholder allows the trustee to deduct 10% withholding tax upon payment, the withholding tax is the final levy. Otherwise individual tax rates are applicable.

10% withholding tax is levied on a corporations TC holder.

## b. Foreign unitholder

Corporate unitholder	Individual unitholder
<ul style="list-style-type: none"> <li>- A 10% withholding tax on profit distribution from REIT</li> <li>- A 15% withholding tax on capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- A 10% withholding tax on profit distribution from REIT</li> <li>- A non-resident individual TC holder will be exempt from tax on the gain from the sale of trust units as the TC is traded in the SET</li> </ul>

### Corporate unitholder

The profit distributed from a REIT will be regarded as income under 40(4) (b) of Thai Revenue Code. Hence, the TC holder which is a foreign company receiving the profit distributed from the REIT will be subject to WHT at the rate of 10%.

In the case a TC holder is a foreign company, the gain received by the TC holder from selling the trust unit will be subject to withholding tax at the rate of 15% in Thailand.

### Individual unitholder

An individual TC holder, both resident and non-resident, should be subject to withholding tax on profit distributed from REIT at the rate of 10%.

An individual TC holder, both resident and non-resident, will be exempt from tax on the gain from sale of trust unit as the TC is traded in the SET.

## PFPO

<sup>12</sup> Corporate income tax rate currently reduced to 20% permanently which beginning on or after January 01, 2016.

### c. Domestic unitholder

Corporate unit holder	Individual unit holder	Withholding tax
<ul style="list-style-type: none"> <li>- Generally, distributions are 50% (unlisted company) or 100% (listed company) tax-exempt</li> <li>- A 20% income tax on capital gains</li> </ul>	<ul style="list-style-type: none"> <li>- An income tax of 5-35%</li> <li>- If the unitholder allows the fund to deduct 10% withholding tax, this withholding tax is the final levy</li> <li>- Capital gains are tax-exempt</li> </ul>	<ul style="list-style-type: none"> <li>- A 10% or 0% withholding tax on distributions to an individual unitholder</li> <li>- No withholding tax levied on distributions to a corporate unitholder</li> </ul>

#### Corporate unitholder

Corporate unitholders may receive a 50% or a 100% exemption on income taxes on profit distribution. A corporate unitholder is 100% exempt if it is a listed company in SET, and 50% exempt if it is a non-listed company and the company holds units in the fund at least three months before and after the distribution of the share of profit. Otherwise normal corporate tax rules apply.

A 20% income tax is levied on capital gains<sup>13</sup>.

#### Individual unitholder

Individual unitholders are to pay 5-35% income taxes on profit distribution. If the unitholder allows the fund to deduct 10% withholding tax upon payment, the withholding tax is final levy.

Individuals are exempt from income tax on capital gains made from the disposal of the fund units.

#### Withholding tax

If the individual unitholder allows the fund to deduct 10% withholding tax upon payment, the withholding tax is the final levy. Otherwise, individual rates are applicable. Capital gains made by an individual are exempt from withholding tax. Withholding tax is not applicable to corporations.

### d. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding tax
N/A	N/A	N/A

#### Corporate unitholder

No Thai taxes are imposed on foreign corporate unitholders on income or on capital gains. The income is viewed by the Revenue Department as commercial income under Section 40(8) of the Revenue Code and not subject to withholding tax when it is paid to a beneficiary overseas. There is no specific exemption, but foreign companies are outside the Thai tax regime.

<sup>13</sup> Corporate income tax rate currently reduced to 20% permanently which beginning on or after January 1, 2016.



## Individual unitholder

No Thai taxes are imposed on foreign individual unitholders on income or on capital gains. The income is viewed by the Revenue Department as commercial income under Section 40(8) of the Revenue Code and not subject to withholding tax when it is paid to a beneficiary overseas. There is no specific exemption, but foreign individuals are outside the Thai tax regime.

## Withholding tax

No withholding taxes are imposed on overseas investors.

# 5 Tax treatment of the foreign REIT and its foreign unit holder

Foreign REIT	Corporate unit holder	Individual unit holder
Same as other foreign companies	N/A	N/A

## Foreign REIT

The Thai tax treatment of a foreign REIT will be the same as that of another foreign individual or company, provided that it is considered as a non-resident entity as supported by the certificate of residency issued by the relevant foreign tax authority.

## Corporate unitholder

Given that it is a foreign unitholder of foreign REIT, no Thai tax would be applicable to any types of income paid from foreign REIT to its foreign unitholders.

## Individual unitholder

Given that it is a foreign unitholder of foreign REIT, no Thai tax would be applicable to any types of income paid from foreign REIT to its foreign unitholders. ■

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## AFRICA & MIDDLE EAST

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### FLAGS LINKED TO CHAPTER



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REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction/history/REIT type

	Enacted year	Citation	REIT type	REIT market
REIT	2006	The Investment Trust Law No. 5	Trust type	Very few listed REITs

The REIT was introduced into the Dubai International Financial Centre (DIFC) as part of The Investment Trust Law No. 5 in August 2006.

The REIT market is still in its infancy, and as of June 1, 2018, there are two publicly listed REITs in Dubai.

Dubai Islamic Bank, in partnership with France's Eiffel Management Limited, launched the first Islamic REIT in Dubai as of December 2010. The venture, by the name of Emirates REIT, was listed on NASDAQ Dubai on April 8th, 2014 and raised USD 201 million through the IPO process.

Emirates REIT is set up as a close-ended investment company (CEIC) in accordance with the DIFC company regulations and operates under the regulation of the Dubai Financial Services Authority (DFSA). Emirates REIT also includes a Shari'a board to advise on Sharia-related matters to ensure the trust is operated in accordance with Shari'a principles.

Emirates NBD REIT was formed by Emirates NBD Asset Management Limited and listed on the Dubai NASDAQ on March 23, 2017. It raised USD 105 million through the IPO process. The Emirates NBD REIT is a closed-ended DIFC investment company and was established to invest in shari'a compliant real estate focused in the UAE.

Although not listed on the Dubai NASDAQ, a USD 200 million Cayman Island-organised Arabian Real Estate Investment Trust (AREIT), has been jointly developed and launched by HSBC Bank Middle East and asset management company Daman. AREIT is managed by AREIT Investment Holdings Limited.

There are other REITs that have been approved by the DFSA and launched (or launching), many of which are not yet listed.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
United Arab Emirates	4	0	EUR 711	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

Key requirements
<ul style="list-style-type: none"> <li>- Required to use a closed-ended legal structure for the investment vehicle</li> <li>- For property funds which intend to be public funds, the Fund Manager may only use either an investment company or investment trust as the investment vehicle of the fund; must ensure that it is listed and traded on an authorised market institution within six months from the date on which the units of the fund are first offered to the public; and must ensure that the constitution of the fund includes provisions that address the issuance, redemption and private placement of units</li> </ul>

Legislation for the REIT structure was issued on August 06, 2006. Key requirements to establish a REIT should be confirmed with the DFSA to ensure the current formalities and procedure.

### b. Legal form/minimum initial capital

Legal form	Minimum initial capital
Public Property Fund	No

#### Legal form

The REIT is a public property fund that is constituted as either an investment trust or an investment company (which is similar to other public property funds).

#### Minimum initial capital

There are no minimum initial capital requirements existing.

### c. Unitholder requirements/listing requirements

Unitholder requirements	Listing mandatory
Detailed information to be confirmed on a case by case basis	Yes

#### Unitholder requirements

Unitholder requirements should be confirmed with the DFSA at the time of listing.

#### d. Asset level/activity test

##### Restrictions on activities/investments

- REITs with any foreign share ownership are restricted to investing in designated freehold areas in Dubai as the non-designated areas allow only UAE and GCC nationals and companies owned entirely by them to own assets in those areas
- REIT is primarily aimed at investments in income-generating real property
- REITs are permitted to develop real estate; property under development must not exceed 30% of the net assets value of the Fund Property of the REIT
- REITs must derive income from two tenants or lessees
- REITs must distribute to unitholders at least 80% of its audited annual net income
- The persons providing oversight functions in respect of the fund must determine if any:
  - I. revaluation surplus credited to income, or
  - II. gains on disposal of real property shall form part of the net income for distribution to unitholders.
- REITs can only invest up to 40% of its total assets in cash and government securities while the remaining balance of the fund is to be invested in real property, property-related assets, or units in another property fund
- REITs may hold real property via an SPV (Special Purpose Vehicle) and should receive the total income generated by the SPV
- REITs should own and control a minimum 50% shareholder stake if entered into a joint property ownership arrangement
- REITs ownership of property outside Dubai is subject to the ownership restrictions of each country into which the REIT is investing

A REIT in the DIFC is permitted to develop real estate for its own account, to trade with real estate or to own residential and/or commercial real estate. The development of real estate is restricted as follows:

1. An operator of a REIT must ensure, subject to (2), that any investment made in respect of property under development whether on its own or in a joint venture is undertaken only where the REIT intends to hold the developed property upon completion.
2. The total contract value of the property under development in (1) must not exceed 30% of the net asset value of the Fund Property of the REIT. Property development activities do not include refurbishment, retrofitting and renovation.

A REIT in the DIFC is permitted to invest in the following assets, subject to complying with any foreign ownership restrictions:

- real property that consists of land and/or buildings, whether freehold or leasehold;
- income-producing property such as schools, residential buildings, office buildings, warehouses, car parks and hospitals;
- property-related assets such as shares, debentures, or warrants which are issued by a body corporate, substantial activity which are related to investments in real property and certificates which confer rights with respect to such investments;
- units in another property fund; and
- cash, government and public securities of up to 40% of its total investments.

#### a. Leverage

##### Leverage

Limited to 70% of the total net asset value



In the DIFC, an operator of a REIT may borrow either directly or through its SPV up to 70% of the total net asset value of the fund.

On May 3, 2015, the DFSA published a modification notice to Emirates REIT permitting the Fund Manager, in respect of the fund, to borrow either directly or through its SPV, up to 50% of the total gross asset value of the fund. The modification also specified a Fund Manager of an Islamic REIT, in respect of the fund, may borrow either directly or through its SPV up to 50% of the total gross asset value of the fund and such borrowings are Shari'a compliant. The modification was published without conditions and effective until further notice.

## b. Profit distribution obligations

Operative income	Capital gains	Timing
80% of annual net income	Included in net income	Annually

### Operative income

REITs in Dubai are required to distribute an amount not less than 80% of audited annual net income to the unitholders.

### Capital gains

Capital gains are included in the annual net income of the REIT. For profit distribution purposes, the inclusion of capital gains is at the sole discretion of the overseeing body of the fund.

## c. Sanctions

Penalties/loss of status rules
Detailed information not yet available

Legislation for the REIT structure has been approved. Because of the limited information available, possible sanctions must be subject to future detailed analysis.

# 3 Tax treatment at the level of REIT

## a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
N/A	N/A	N/A

## Current income

REITs are not subject to tax if they are closed-ended investment companies domiciled in the DIFC. The legislation that exempts the Funds from any corporate tax is effective for 50 years commencing from September 13, 2004.

## Capital gains

Not taxable as specified above.

## Withholding tax

N/A.

## Accounting rules

IFRS rules are applicable.

## VAT

VAT was introduced in 2018 and may be payable on rental income and services provided to the REIT, depending on the asset class. Future detailed analysis would be required based on the asset class of the REIT.

### b. Transition regulations

#### Conversion into REIT status

N/A

### c. Registration duties

#### Registration duties

- Land Registration Fees
- Real Estate Transfer Fees

There is no stamp duty or transfer tax levied on acquisition of freehold property in Dubai. However, there are land registration fees and transfer fees between 1% to 6% paid by the property developer and purchaser depending on the property type and location of the property. The regulations provide that each party incurs 50% of the expense, but the parties are contractually able to agree otherwise.

The real estate registration fee for a real estate purchase of property 'on-shore' in Dubai is 4% of the purchase price (and may vary for other Emirates), applied on the value of the relevant immovable property.

## 4 Tax treatment at the unitholder's level

### a. Domestic unitholder

Corporate unitholder	Individual unitholder	Withholding tax
N/A	N/A	N/A

#### Corporate unitholder

No taxation for domestic corporate unitholders. No taxes apply to the unitholders including dividend tax, capital gains tax, stamp duty or other tax.

#### Individual unitholder

No taxation for domestic individual unitholders.

#### Withholding tax

Dubai does not levy withholding taxes.

### b. Foreign unitholder

Corporate unitholder	Individual unitholder	Withholding Tax
Detailed information not yet available	N/A	N/A

#### Corporate unitholder

Taxation for foreign corporate unitholder requirements would need to be the subject of future analysis with regards to the nature of business of foreign corporate unitholders (subject to the comments in Part 3 above).

#### Individual unitholder

No taxation for foreign individual unitholders.

#### Withholding tax

Dubai does not levy withholding taxes.

## 5 Tax treatment of foreign REIT and its domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
Detailed information is not yet available	Detailed information is not yet available	Detailed information is not yet available

### Foreign REIT

Taxation for a foreign REIT on income from Dubai would need to be the subject of future analysis with respect to the applicability of double tax treaties between the UAE and the foreign REIT's country of residence.

### Corporate shareholder

Taxation for domestic corporate unitholders from the income of a foreign REIT would need to be the subject of future analysis with respect to the applicability of double tax treaties between the UAE and the foreign REIT's country of residence.

### Individual shareholder

Taxation for domestic individual unitholders from the income of a foreign REIT would need to be the subject for future analysis with respect to the applicability of double tax treaties between the UAE and the foreign REIT's country of residence. ■

*Please note: no reliance should be placed on the information above, it is not financial nor legal advice*

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REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIT	2006	Sections 64A2–64A11 of the Israeli Tax Ordinance ('ITO')	Corporate type

The REIT (Real Estate Investment Trust) regime was introduced into the Israeli tax legislation in 2006. The Israeli REIT is a 'flow-through' regime. As a result, each of the REIT investors is taxed on the distributed REIT incomes.

The REIT is governed by Sections 64A2–64A11 of the Israeli Tax Ordinance which determines a detailed settlement about the essence of the REIT, way of operations and tax implications on the REIT's shareholders.

In this model, certain shareholders are exempt from tax on the income from the REIT.

The exempted shareholders include:

1. Retirement fund or a public institution – provided that in respect of the income of the public institution from the sale of land, an exemption of half the tax shall be granted. For the purposes of this paragraph, 'retirement fund' and a 'public institution', as defined in Section 9(2) of the Israeli Tax Ordinance;
2. A resident of a treaty country managing a retirement age savings plan or a long-term savings plan similar to a fund, and any pension fund that is a resident of a treaty country or managed by a resident of a treaty country, provided that profits received from retirement savings plan are exempt from tax in that resident country.

Other corporations that invest in the REIT are subject to corporate tax rates (23% in 2019). Individuals are subject to the individual marginal tax rate of up to 47% at the highest tax bracket, in 2019). Please note that as of January 1, 2017, individuals which their total chargeable income exceeds NIS 649,560 (in 2019), are subject to an additional 3% tax rate on the part of their chargeable income.

## Sector summary\*

Listing country	Number of Listed REITs	Number in EPRA REIT Index	Sector mkt cap (EUR m)	% of Global REIT Index
Israel	5	0	EUR 1,370	0.00%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Special purpose company is required
- Incorporated in Israel; controlled and managed from Israel
- Company's shares are listed for trading in a stock exchange in Israel within 24 months from the date of its incorporation; however, the company's shares can be listed for trading in a stock exchange in Israel within 36 months if the company's valuable assets which are real estate for residential rental purposes or income-yielding real estates for housing for rent are not less than 30% of the entire assets of the company, at a period of 24 months and 36 months from the date of its incorporation
- Certain assets value/ratio should be maintained
- Certain limitations on the company's shareholders holdings ratio should be maintained

The REIT regime applies to a new company that is established for this purpose, or a company commits to become a REIT.

### b. Legal form/minimum share capital

Legal form	Minimum share capital
A public company traded in the Tel Aviv Stock Exchange (TASE)	No

#### Legal form

A REIT must be a public company listed for trade on the Israeli stock exchange (TASE). It must be a tax-resident of Israel. The REIT Subsidiaries can reside outside Israel, but the value of income-yielding real estate assets in Israel and the value of real estate for residential rental purposes assets located in Israel should be no less than 75% of the value of all the company's income-yielding real estate assets and real estate for residential rental purposes assets.

The company must meet these requirements on the testing dates, June 30 and December 31 of each year since its date of incorporation.

The REIT must submit an annual tax return which includes an accountant certificate that the company has met all the requirements of a REIT as mentioned above and hereinafter.

#### Minimum share capital

No minimum share capital is required.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
The REIT's shareholders' means of control should not exceed the limitations described hereinafter	Yes

#### Shareholder requirements

As of three years from the date the company was listed for trading in a stock exchange in Israel, no more than 70% of the company's means of control are held, directly or indirectly, by five shareholders or less.

As of five years from the date the company was listed for trading in a stock exchange in Israel no more than 50% of the company's means of control are held, directly or indirectly, by five shareholders or less.

In addition, as of the sixth year from the date the company was listed for trading in a stock exchange in Israel no single shareholder will hold more than 30% of the company's means of control, and as of the ninth year from the date the company was listed for trading in a stock exchange in Israel, no single shareholder will hold more than 20% of the company's means of control.

The limitations on the company's shareholders apply on directly or indirectly holdings (a shareholder and his relative, as defined in Section 88 of the ITO, are considered to be one shareholder). In addition, members of a benefit fund, persons insured by an insurance company in respect of its insured persons' invest, and unitholders in a joint investment trust fund will be considered as shareholders in the fund.

'Means of control' is defined as one of the following: the right to profit, the right to appoint a director or general manager of the company or similar function, voting rights, the rights to liquidation proceeds, or the power to order or instruct someone who holds any of the rights listed above to act on his behalf.

#### Listing requirements

The company must be listed for trade in the TASE within a period of 24 months or 36 months from the date of incorporation under the provisions described above. The REIT may also be listed for trade abroad (dually).

### d. Asset levels

Restrictions on activities/investments
<ul style="list-style-type: none"> <li>- 95% or more of the value of the REIT's assets must consist of income-yielding real estate assets, real estate for residential rental purposes assets and liquid assets (cash, deposit, securities, bond, etc.)</li> <li>- 75% or more of the value of the REIT's assets must consist of:               <ol style="list-style-type: none"> <li>1. income-yielding real estate assets</li> <li>2. money received from the first issue of the REIT's securities, which were listed for trading in the TASE, during the two years following the day of issue</li> <li>3. money received from an additional issue of the REIT's securities, which were listed for trading in the TASE, during one year following the day of issue</li> <li>4. consideration from the sale of real estate – during one year following the day of sale</li> </ol> </li> <li>- The value of the REIT's assets mentioned exceeds NIS 200 million</li> <li>- The value of income-yielding real estate assets and the value of Israeli real estate for residential rental purposes assets located in Israel should be no less than 75% of the value of all the company's income-yielding real estate assets and real estate for residential rental purposes assets</li> </ul>



A REIT must fulfil all the restrictions stated below:

- 95% or more of the value of the REIT's assets must consist of income-yielding real estate assets, real estate for residential rental purposes assets and liquid assets (cash, deposit, securities, bond, etc.);
- The value of income-yielding real estate assets and the value of Israeli real estate for residential rental purposes located in Israel should be no less than 75% of the value of all the company's income-yielding real estate assets and real estate for residential rental purposes.

The company must meet these requirements on the testing dates, June 30 and December 31 of each year since the date of its incorporation.

75% or more of the value of the REIT's assets must consist of:

1. income-yielding real estate assets;
2. money received from the first issue of the REIT's securities, which were listed for trading in the TASE, during the two years following the day of issue;
3. money received from an additional issue of the REIT's securities, which were listed for trading in the TASE, during one year following the day of issue; and
4. consideration from the sale of real estate during one year following the day of sale.

The value of the REIT's assets mentioned exceeds 200 million NIS.

The company must meet these requirements on the testing dates, June 30 and December 31 of each year since the date of the REIT's listing for trading in the TASE.

'Income-yielding real estate' is defined as real estate that generates income from rent and additional activities, as long as at least 70% of the real estate is developed according to a plan which applies to them, and the real estate is not considered inventory in the fund's books.

Holding of real estate association by REIT does not affect REIT's requirements while the real estate association invests in assets according to the REIT's requirements. In addition, the real estate income will be subject to tax as part of the REIT's income.

## e. Leverage

### Leverage

The REIT's debt should not exceed the ratio from the REIT's total assets as described

The REIT's obligations (other than equity) do not exceed 60% of the income-yielding real estate assets value in addition to 80% of the value of real estate for residential rental purposes assets or income yielding real estates for housing for rent assets and in addition to 20% of the value of other assets it holds.

The company must meet these requirements on the testing dates, June 30 and December 31 of each year since the date of the REIT's listing for trading in the TASE.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
At least 90% of its chargeable income	100% of its capital gain from the sale of income-yielding real estate	<ul style="list-style-type: none"> <li>- Distribution of the chargeable income (other than real estate appreciation or profits from the sale of income yielding real estate) in addition to exempt income and less non-deductible expenses, must take place no later than April 30 of the following year the income was produced or accrued</li> <li>- Distribution of the capital gain must take place during a period of 12 months from the date of the sale of income yielding real estate</li> </ul>

### Operative income

The REIT is obliged to distribute at least 90% of its chargeable income, excluding capital gains and non-deductible expenses and including exempted income, calculated based on generally accepted accounting principles.

The REIT may choose to distribute an additional amount equal to the depreciation expenses.

### Capital gains

The REIT is obliged to distribute 100% of its capital gain from the sale of income yielding real estate.

### Timing

Distribution of the chargeable income must take place no later than April 30 of the following year the income was produced or accrued, since the date of the REIT's incorporation.

Distribution of the capital gain must take place in a period of 12 months from the date of the sale of the income yielding real estate since the date of the REIT's incorporation.

## g. Sanctions

Penalties/loss of status rules
Loss of tax privilege

The REIT will be taxed similarly to an ordinary company from the date in which the requirements are no longer met. However, if the company fails to meet the requirements on a testing date in any given year since the date of the REIT's registration for trading in the TASE, but within a period of up to three months successfully meets the requirements, and continues to do so for a consecutive year, the company will be considered a REIT throughout the entire period. In a case that the company fails to meet the requirements for a consecutive year after the period of three months as mentioned above, the company will cease to be a REIT from the first date it failed to meet the requirements.

REIT that does not meet the requirements or choose to discontinue its REIT status will be taxed as an ordinary company from the date of its election or 90 days from the date of its application to the Israeli Tax Authority, according to the latest, or from the date that requirements are no longer met.

Any decision to discontinue REIT status by choice requires the approval of the company's general meeting. Controlling shareholders or people with a personal interest in the approval shall not be included in the count of voters.

If the company has begun a liquidation process, then it shall cease to be considered a REIT.

### 3 Tax treatment at the REIT level

#### a. Corporate tax /withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- No taxation of distributed chargeable income</li> <li>- Undistributed exceptional income is subject to a 60% tax rate. Distributed exceptional income is subject to a 70% tax rate</li> <li>- Undistributed chargeable income from the sale of real estate held for a period of less than four years will be subject to corporate tax rates or individual marginal tax rates</li> <li>- Chargeable income, as well as capital gain derived from real estate for residential rental purposes assets which not held for a short period, will be subject to a 20% tax rate</li> <li>- Income paid to the shareholders which exceed the chargeable income and beyond to the amount of depreciation expenses will be subject to the capital gain tax rate</li> <li>- Other chargeable income will be subject to the corporate tax rate</li> </ul>	<ul style="list-style-type: none"> <li>- Distributed capital gains are exempted from tax</li> <li>- Undistributed capital gains will be subject to corporate tax rate or individual marginal tax rates</li> </ul>	<p>Upon distribution to the shareholders, a banking corporation or a member of TASE will withhold tax at the following rates:</p> <ul style="list-style-type: none"> <li>- Capital gains: 25%/30% for individuals, the corporate tax rate for companies; however, regarding individuals, chargeable income from the sale of real estate held for a period of less than four years will be withheld at the individual marginal tax rates</li> <li>- Chargeable income or capital gains derived from real estate for residential rental purposes assets which not held for a short period will be subject to a 20% tax rate</li> <li>- Exceptional income is subject to withholding tax at a rate of 70%</li> <li>- Other chargeable income is subject to the regular corporate tax rate or individual marginal tax rates</li> </ul>

#### Current income

The REIT is a 'flow-through' regime. However, the REIT is subject to taxes on undistributed income.

A 70% tax rate applies to 'exceptional income' upon distribution.

'Exceptional income' is defined as:

1. Income from the sale of inventory (real estate or otherwise);
2. Income other than the following to the extent that such income exceeds 5% of the total income of the fund in that tax year:
  - (a) Income from income-yielding real estate assets, income from real estate for residential rental purposes assets and income from the sale of construction rights related to the income-yielding real estate;
  - (b) Income from public traded securities, state bonds and deposits.
  - (c) Inflation income which considered as business profits.

Exceptional income, which is not considered to be a chargeable income by the shareholders, is subject to a 60% tax rate.

Distribution of the exceptional income in later years will be considered a dividend distribution and will be subject to 25/30% withholding tax rate. No credit will be granted to the shareholders for REIT taxation.

### Capital gains

Distributed capital gains are not subject to taxation. The REIT must distribute 100% of its capital gain income. Distribution of capital gain must take place in a period of 12 months from the date of sale of the real estate.

### Foreign taxes

Foreign taxes paid by the REIT will be deducted from the foreign chargeable income that was subject to foreign taxes. However, no foreign tax credit will be granted to the REIT or to the REIT's shareholders.

### Accounting rules

There are no special accounting rules for a REIT. A REIT listed for trade in the TASE must follow the IFRS rules, like any other listed company.

### Losses

The shareholders are not allowed to offset losses of the REIT from their income.

A loss to a shareholder in the sale of the REIT's shares may be offset as stated in Section 92 of the Israeli Tax Ordinance or against the chargeable income of the shareholder that the REIT transferred to him in that year, except for the exceptional income that the REIT transferred to him in that year.

## b. Transition regulations

### Conversion into REIT status

According to the rules mentioned in section 2

## c. Registration duties

### Registration duties

Under certain conditions, reduced real estate 'purchase tax'

Under certain conditions for a transfer of income yielding real estate or real estate for housing for rent purpose by REIT in exchange for share allocation, the REIT will pay a reduced purchase tax of 0.5% of the real estate value. The reduced purchase tax rate also applies to a company which commits to become a REIT according to the requirements abovementioned in section 2.

If the following conditions are not met, the company will pay the full purchase tax rate (in 2019, 6%); the reduced purchase tax of 0.5% also applies to REIT's income yielding real estate or real estate for housing for rent purpose acquiring.

## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- The corporate tax rate is 23% in 2019</li> <li>- The corporate capital gains tax rate is 23% in 2019</li> </ul>	<ul style="list-style-type: none"> <li>- The individual maximum marginal tax rate is 47% in 2019</li> <li>- The individual capital gains tax rate is 25/30%</li> </ul>	As mentioned above

#### Corporate shareholder

The income derived from the REIT is subject to corporate tax. The corporate tax rate in 2019 is 23%.

#### Individual shareholder

The individual's income derived from the REIT is subject to the individual's marginal tax rate. The maximum individual tax rate in 2019 is 47%. Individuals with a total chargeable income that exceeds NIS 649,560 (in 2019) are subject to an additional 3% tax rate on part of their chargeable income.

#### Withholding tax

Upon distributions, the REIT must withhold tax that the shareholders would have paid had their investment been directly in the real estate. The individual or corporate tax rates are based on ordinary income. For example, the withholding tax would be 23% on corporate capital gains or ordinary business income based on the corporate tax rate.

The withholding tax is not a final tax assessment; the shareholder must submit an annual tax return which reflects his actual chargeable income (including losses). Credit will be granted for the withholding tax charged by the REIT.

Distribution of exceptional income will be subject to 70% withholding tax. Distribution of the exceptional income which was not distributed in the year in which it was generated, in later years will be considered as dividend distribution and will be subject to a 25%/30% withholding tax rate.

## b. Foreign shareholders

Corporate shareholder	Individual shareholder	Withholding tax
<ul style="list-style-type: none"> <li>- Withholding tax subject to tax rates applicable for Israeli companies</li> <li>- 'Exceptional income' which is distributed is subject to a 70% tax rate</li> </ul>	<ul style="list-style-type: none"> <li>- Withholding tax subject to tax rates applicable for Israeli individuals</li> <li>- 'Exceptional income' which is distributed is subject to a 70% tax rate</li> </ul>	<ul style="list-style-type: none"> <li>- Final withholding tax</li> <li>- Treaty relief is available to distributions of 'exceptional income' in later years</li> </ul>

### Corporate shareholder

Distributions of current income and capital gains are subject to a withholding tax at the corporate tax rates applicable to Israeli investors. Treaty country resident pension funds and mutual funds are exempt from withholding tax, excluding exceptional income, to the extent that the profits are exempt in their country of residence.

### Individual shareholder

Distributions of current income and capital gains are subject to a withholding tax at the individual income tax rates applicable to Israeli investors.

### Withholding tax

Treaty relief may be granted for the distribution of the exceptional income in later years, which is considered as a dividend distribution.

## 5 Tax treatment of foreign REIT and its domestic shareholder

Foreign REIT	Corporate shareholder	Individual shareholder
<ul style="list-style-type: none"> <li>- Taxation under normal Israeli tax rules</li> </ul>	<ul style="list-style-type: none"> <li>- Taxation at the corporate tax rate of 23% in 2019 if the REIT is a 'flow-through' entity</li> <li>- A dividend is subject to a 25% tax rate if the REIT is not a 'flow-through' entity</li> </ul>	<ul style="list-style-type: none"> <li>- Taxed at 47% in 2019 if the REIT is a flow-through entity</li> <li>- Dividend income will be subject to a 25%/30% tax if the REIT is not a 'flow-through' entity</li> </ul>

### Foreign REIT

A foreign REIT will be taxable under normal Israeli tax rules, based on its legal character (Corporation, Fund, Partnership etc.).

### Corporate shareholders

A corporate shareholder in a foreign REIT, which derived chargeable income from foreign sources, is subject to the corporate income tax rate of 23% in 2019 as long as the REIT is considered a 'flow-through' entity for Israeli tax purposes (regardless of its election under foreign country rules).

Dividend income is subject to a 25%/30% tax rate. If the foreign REIT is not a ‘flow-through’ entity, a tax credit is allowed.

### Individual shareholder

An individual shareholder in a foreign REIT, which derives chargeable income from foreign sources, is subject to individual income tax at the maximum rate of 47% in 2019 as long as the REIT is considered a ‘flow-through’ entity. ■

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AFRICA & MIDDLE EAST

# Kingdom of Saudi Arabia

REITF

2019

A comparison of the  
major REIT regimes  
around the world.





# 1 General introduction/history/REIT type

	Enacted year	Citation	REIT type
REITF	2006	REITs Instructions (October 2016) and amended REITs Instructions (October 2018)	A closed-ended investment fund regulated by the Capital Market Authority (CMA) in KSA

The Board of the CMA formally introduced REITs to The Kingdom of Saudi Arabia when it issued the Instructions for REITs (REITs Instructions) early 2016. The first REIT was listed on the Saudi Stock Exchange (Tadawul) on November 13, 2016. The REITs instruction defines REITs as real estate investment funds offered to the public and listed on Tadawul, with the main objective of investing in “developed and constructed real estate properties capable of generating periodic rental income.”

REITs were introduced as a new financing tool that taps into Saudi Arabia’s large portfolio of real estate assets. This financing tool aims to provide local and international retail investors with a new investment channel through which they can access the Saudi real estate market.

Although tax efficiency has less of an impact on the REITs in the Gulf Cooperation Council (GCC), it offers liquidity and flexibility for investors and real estate companies. REITs provide transparency and diversity to the international institutional investors enabling them to diversify investment and risk. Investors usually seek tradeable assets rather than the illiquid ownership of standalone buildings, investing in a REIT offers transparency and clarity, without the challenges of managing the properties directly or through hiring a property management company.

Since the Tadawul launched the Kingdom’s first REIT in late 2016, the number of listed REITs has grown to 16 with a combined market capitalisation of SAR 13.6 billion (USD 3.5 billion).

The vast majority of existing REITs in KSA have their investments spread across multiple real estate asset classes partly due to a constrained pipeline of institutional grade assets. As the market matures, it is likely that there will be more thematic REITs allowing investors to gain access to specific real estate asset classes that are in line with their risk/ return requirements. To counter the availability of limited institutional grade assets in KSA, REITs are increasingly looking to expand their portfolio abroad in order to obtain the right quality of assets and have more accretive assets in their portfolio. Furthermore, the CMA is placing increasing emphasis on governance and now has clearly stipulated guidance that governs capital increases and mechanisms for merging REITs that should bring in more transparency and improve liquidity in the sector. It is likely that in the next few years REITs with a good asset base, strong management teams and robust governance structures will continue to grow and attract capital whereas the sub-optimal performers will potentially shut down or get acquired by larger REITs.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
KSA	16	2	EUR 2,941.7	0.02%

\* Market cap rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## Top REIT\*

Company name	Mkt cap (EUR m)	1 yr return (EUR) %	Div yield	% of Global REIT Index
JADWA REIT SAUDI	EUR 338.14	6.09%	7.88%	0.01%
AI RAJHI REIT	EUR 248.36	6.57%	3.58%	0.01%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Must be structured as a closed-ended fund
- Regulated and monitored by the Capital Markets Authority (CMA)
- The fund manager may not offer units to the public without making prior arrangements for listing those units on the Exchange in accordance with the listing rules
- All the fund's real estate need to be owned as per valid deeds
- The fund has to appoint a TAQEEM accredited valuer. The fund manager must replace the accredited valuer every 5 years at most

REITs are subject to extensive disclosure requirements compared to other types of real estate investment funds. In order to facilitate a transparent disclosure regime for prospective investors, a REIT's fund manager must make certain disclosures to unitholders and to the CMA without delay, including:

- any material developments that are not publicly available and which a prudent investor may consider when making an investment decision. Material developments include developments that would affect the REIT's activities, assets and liabilities, financial position, and unit price;
- any purchase, sale, mortgage, or lease of real estate assets with a total value that equals or exceeds 10% of the value of the fund's Net Asset Value;
- any losses equal to or greater than 10% of the fund's net assets
- any dispute, including any litigation, arbitration or mediation where the value involved is equal to or greater than (5%) of the fund's net assets
- any change in the composition of the REIT's board of directors or any of its committees;
- any increase or decrease of the REIT's net assets or its gross profit by 10% or more; and the annual audited financial statements of the REIT.

## b. Legal form/minimum initial capital

Legal form	Minimum share capital
Closed-ended investment fund regulated by the CMA	SAR 500 million (approximately EUR 115 million) with a nominal value of SAR 10 for each unit

### Legal form

A REIT in the KSA must be a closed-ended investment fund.

### Share capital

After the CMA has amended the REIT Instructions in October 2018 to refine existing legislation, new REITs must now have a capital of at least SAR 500 million (approximately EUR 115 million) with a nominal value of SAR 10 (approximately EUR 2.3) for each unit.

## c. Shareholder requirements / listing requirements

Shareholder requirements	Listing mandatory
<ul style="list-style-type: none"> <li>- For public listing, a REIT requires at least 200 unitholders from the public who own at least 30% of the total REIT units</li> <li>- A 12-month lock-up period for those unitholders holding 5% or more units of the fund's unit upon establishment</li> <li>- Foreign ownership restricted to 49% when listed on the Tadawul</li> </ul>	Yes – Needs to be listed on the Tadawul

### Shareholder requirements

REITs consist of units, where each unit represents ownership in the underlying real estate.

Unitholders may exercise all rights attached thereto, including the right to vote and the right to subscribe in-kind units and/or tradable rights issued as a result of a capital increase.

A REIT's capital may only be increased either through an in-kind contribution or through the issuance of tradable rights in accordance with the guidelines CMA provided for the purposes of implementing the new Companies Law.

The updated REIT regulations introduced a 12-month lock-in period for those unitholders having their names listed on the fund's terms and conditions, upon establishment, indicating their ownership of 5% or more of the fund's units. This period begins from the start of unit trading in the Saudi stock market, which should contribute to a more stable market price for the unit.

Foreign ownership restricted to 49% when listed on the Tadawul.

## Listing requirements

The fund manager seeking to offer and list REITs units on the Tadawul must submit an application to the CMA. There must be a sufficiently liquid market for the unit that are the subject of the application for registration and admission to listing, amongst others, as follows:

- at least 200 unitholders from the public;
- at least 30% of the total REIT units are owned by unitholders from the public;
- the minimum subscription must not exceed 1000 units per unitholder; and
- public unitholders may only subscribe by way of cash contributions.

The REITs Instructions define public to exclude any unitholder holding units that represent 5% or more of the aggregate units of the REIT, the fund manager or the fund manager's affiliates, or any member of the REIT's board of directors.

In addition to the increased minimum capital requirement for new REITs, assets acquired by the REIT are required to have generated net rental revenues in the last 3 years.

### d. Asset level/activity test

#### Restrictions on activities/investments

- REITs are allowed to invest up to 25% of asset value outside of Saudi Arabia
- Up to 25% of total assets can be invested in property under development
- Investment in vacant ('white') lands is prohibited
- REITs with foreign owners cannot hold assets in Medina or Makkah

REITs in Saudi Arabia are allowed to invest up to 25% of the fund's total assets value abroad.

At least 75% of the fund's total asset value according to the last audited financial statements must be invested in constructed developed real estate qualified to generate periodic and rental income. The fund manager is allowed to invest up to a maximum of 25% of the fund's total assets value in:

- real estate development, whether the real estate is owned by the fund manager or not, and
- renovation and redevelopment of real estate;
- real estate repurchase agreements;
- cash and such units of investment funds licensed by the CMA and real estate companies; and
- usufruct rights.

The fund manager is prohibited from investing in vacant, undeveloped (so-called 'white') lands.

REITs with foreign owners cannot hold assets in Medina or Makkah.

## e. Leverage

Leverage
Limited to 50% of the total assets value of the fund

The borrowing of the fund must not exceed 50% of the total assets value of the fund.

## f. Profit distribution obligations

Operative income	Capital gains	Timing
90% of the fund's annual net profits	Included in net profits	Annually; Distribution dates may be set out in the Terms and Conditions of the REIT

REITs are required to distribute a minimum of 90% of the fund's net profits annually to its unitholders in the form of dividends. Therefore, dividend growth will be a key indicator of long-term success for investors.

### Operative income

REITs in Dubai are required to distribute an amount not less than 80% of audited annual net income to the unitholders.

### Capital gains

Capital gains are included in the annual net income of the REIT. For profit distribution purposes, the inclusion of capital gains is at the sole discretion of the overseeing body of the fund.

## g. Sanctions

Penalties/loss of status rules
Under certain circumstances, CMA may consider a trading halt or cancellation of listing

The CMA may at any time suspend the trading of REIT units or cancel its listing as it deems fit, under certain circumstances, which are set out in the REITs Instructions.

### 3 Tax treatment at the level of REIT

#### a. Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
N/A	N/A	N/A

##### Current income

Currently CMA regulated funds cannot be registered for tax and as a result in practice REITs are not taxed.

##### Capital gains

Capital gains realised from sale of securities listed on the Tadawul are not subject to Zakat or tax.

##### Withholding tax

Not applicable.

##### Accounting rules

IFRS Standards are required for all listed companies in Saudi Arabia, which are in accordance to the accounting and auditing standards adopted by Saudi Organization for Certified Public Accountants (SOCPA).

#### b. Transition regulations

Conversion into REIT status
No stamp or transfer taxes

#### c. Registration duties

Registration duties
<ul style="list-style-type: none"> <li>- Land Registration Fees</li> <li>- Real Estate Transfer Fees</li> </ul>

Tax for transferor on seeding of assets into the REIT:

- Gains subject to 2.5% Zakat (for KSA or GCC residents) or CIT at 20% (for foreign investors);
- There is currently no property or transfer tax levied on acquisition of freehold property in the KSA.

#### d. Other Taxes

##### Registration duties

Not applicable

#### VAT

From 2018, KSA levied a 5% value-added tax (VAT) on most of its products and services. The recently introduced VAT in Saudi Arabia is applied to any real estate transaction in the Kingdom. The 5% rate is implemented on the sale of a house, apartment, or other residential real estates, the sale of any commercial real estate, transfer of ownership of bare or undeveloped land, and the sale of partly completed construction works. The tax excludes selling to relatives to the fourth degree and residential rentals.

#### Title Deed Fee

A fee of SAR 500 is required for the transfer of ownership for a residential unit or land, Moreover a fee of SAR 5,000 is required for the transfer of ownership for a commercial building or land.

#### Stamp Tax

Not applicable.

#### Property Tax

Not applicable as the fund manager is prohibited from investing in vacant (so-called 'white') lands.

From 2017, KSA levied a White Land tax to help making good use of the idle residential and commercial lands across the Kingdom's largest cities – which constitutes as much as 40% of all land in the capital city, Riyadh. The new law requires the owners of lands that are 10,000 square meters or more to pay 2.5% of the land's value as a tax or to start building on it within 12 months.

#### Environmental Tax

Not applicable.

## 4 Tax treatment at the shareholder's level

#### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
N/A for KSA residents	N/A for KSA residents	N/A for KSA residents

**Capital gains received by resident corporations**

Not applicable.

**Dividends received by resident corporations**

Not applicable.

**Capital gains received by resident individuals**

Not applicable.

**Dividends received by resident individuals**

Not applicable.

**b. Foreign shareholder**

Corporate shareholder	Individual shareholder	Withholding Tax
No Corporate Income Tax	Currently generally exempt from tax	5% withholding tax to other GCC and foreign resident unit holders

**Capital gains received by non-resident corporations**

No Zakat or CIT for foreign shareholders, as no practical basis to currently register the fund in order to tax the disposal by the foreign unitholders.

**Dividends received by non-resident corporations**

5% withholding tax.

**Capital gains received by non-resident individuals**

No Zakat or CIT for foreign shareholders, as no practical basis to currently register the fund in order to tax the disposal by the foreign unitholders.

**Dividends received by non-resident individuals**

5% withholding tax. ■



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AFRICA & MIDDLE EAST

# South Africa

REIT

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIT	REITs were introduced in the market in 2013	<ul style="list-style-type: none"> <li>- Part V of the Collective Investment Schemes Control Act No. 45 of 2002 ('the CISA')</li> <li>- Companies Act No. 71 of 2008 ('the Companies Act').</li> <li>- Income Tax Act No. 58 of 1962 ('the Income Tax Act').</li> <li>- JSE Limited ('JSE') Listing Requirements</li> <li>- The Securities Transfer Tax 25 of 2007 ('the STT Act')</li> </ul>	<ul style="list-style-type: none"> <li>- Legally a company or trust</li> <li>- Listed company for income tax purposes</li> </ul>
	Trust REIT		
	Company REIT		

In the South African context, REITs did not exist until April 1, 2013.; however, comparable investment vehicles included Property Unit Trust (PUT) or a Property Loan Stock Company (PLS company)<sup>1</sup>. A PUT holds immovable property and shares in property companies and is managed by a management company. The management company trades participation units in the market as a market maker. A South African PUT is legally regulated by the CISA. The conduit principle (flow-through) applies to distributions made by a PUT, i.e. income flows through to beneficiaries in its original form and the PUT is exempt from capital gain). The main difference between a PUT and a PLS company is that a PLS company is a company regulated by the Companies Act and is not required to comply with the CISA. Unlike a unitholder in a PUT, an investor in a linked unit in a PLS company holds both equity and debentures. Interest distributions flow through to investors. The interest is deductible by the PLS whilst it is treated as ordinary revenue in the hands of the investor.

The National Treasury has long debated the introduction of a REIT regime in South African. The long-awaited dispensation was introduced through the amendment of the tax legislation and the JSE listing requirements. In light of the recent introduction of special taxation rules<sup>2</sup> in respect of the taxation of REITs versus PUT and PLS, the JSE was requested to facilitate the introduction of the REIT structure and regulations. With effect from May 1, 2013, a REIT is regulated in terms of the JSE listing requirements and rules<sup>3</sup>.

## Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
South Africa	33	13	EUR 20,636	1.08%

<sup>1</sup> South Africa (2007) The Department of National Treasury. Reforming the Listed Property Investment Sector in South Africa – Discussion paper: 'Introduction', December 3.

<sup>2</sup> Section 25BB of the Income Tax Act No. 58 of 1962 (ITA) applicable in respect of years of assessment commencing on or after April 1, 2013.

<sup>3</sup> Bulletin 3 of 2013, The JSE Limited Listing Requirements read with section 25BB of the ITA. These rules were introduced to align the legislation with international standards and to streamline the tax treatment of PUT and PLS

## Top five REITs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Growthpoint Prop Ltd	EUR 4,492	-0.50%	8.78%	0.38%
Redefine Properties	EUR 3,246	-4.28%	10.95%	0.28%
Vukile Property Fund	EUR 1,143	8.17%	9.46%	0.09%
Hyprop Investments Ltd	EUR 1,113	-25.09%	10.96%	0.10%
Investec Property Fund Ltd	EUR 702	9.87%	9.30%	0.04%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.

## 2 Requirements

### a. REIT: Formalities/procedure

#### Key requirements

- Qualify for listing under the JSE rules
- Distribute at least 75% of its taxable earnings available for distribution to its investors each year
- Earn 75% of its income from rental or from indirect property owned or investment income from indirect property ownership
- Owns at least ZAR 300 million worth of property
- Maintain its debt below 60% of its gross asset value
- Have a committee to monitor risk
- Not enter into derivative instruments that are not in the ordinary course of business

A REIT is a listed property investment vehicle which is primarily engaged, directly or indirectly, in property activities and is listed on the JSE under the REIT sector. A REIT that is resident for South African income tax purposes qualifies for the REIT tax dispensation. A REIT can be a listed Company REIT or a Trust REIT.

No prescribed management model is enforced as to how a Company REIT is to be managed both internally and externally. Company REITs may have external or internal management and/or property administration function. The company's directors are responsible for the ongoing compliance with the JSE listing requirements and the Companies Act.

### b. Legal form/minimum initial capital

#### Legal form

A Company REIT is a company regulated by the Companies Act and is a legal person for the purposes of South African law.

A Trust REIT is a unit trust, regulated by the CISA.

### Minimum initial capital

A Company REIT is required to own at least R300 million worth of property and must keep its debt below 60% of its gross asset value.

### c. Unit holder requirements/listing requirements

	Unitholder requirements	Listing mandatory
REIT	No requirements	Yes

### Unitholder requirements

The sale and acquisition of units in a REIT must comply with the JSE regulatory requirements for securities exchange. Such requirements include compliance with the Financial Intelligence Centre Act (No 38 of 2001) (FICA) and the Securities Services Act (No 36 of 2004).

The purchase and sale of units in a REIT can only be done through a securities account (online or using a stockbroker), collective investment scheme (Unit Trust) or a Retirement Annuity that invests in South African REITs. The SA REIT index can also be used to obtain exposure to the whole sector. A minimum investment of one share is required to invest in a REIT.

### d. Asset level/activity test

Rental Income includes amounts received from:

- use of immovable property including penalty interest;
- dividends from other REITs;
- qualifying distributions from a company that is a controlled company; and
- local dividends or foreign dividends from a property company.

Rental income excludes amounts received from:

- the total investment exposure to assets included in a portfolio may not exceed 25% of the market value of all assets comprised in a portfolio;
- all assets issued by a single concern may not exceed 10% of the market value of all assets comprised in a portfolio; and
- a manager must obtain the prior consent of the trustee for the inclusion of any asset in a portfolio.

The following limits and conditions are imposed on the above investments:

- The total investment exposure to assets included in a portfolio may not exceed 25% of the market value of all assets in a portfolio;
- All assets issued by a single concern may not exceed 10% of the market value of all assets comprised in a portfolio; and
- A manager must obtain the prior consent of the trustee for the inclusion of any asset in a portfolio.

The above limits may only be exceeded by virtue of the appreciation or depreciation of the market value of the underlying assets comprised in the portfolio, or as a result of any corporate action by the REIT. A manager may not make any further investment in the asset in question as long as any limit determined above is exceeded.

A REIT may only invest in property in a foreign country and property shares or participatory interests in a collective investment scheme in property in a foreign country if that foreign country has a foreign currency sovereign rating by a rating agency. The rating and rating agency must be determined by the Registrar. Currently, the requirement is a rating of 'Baa2' or higher by Moody's Investors Service Limited, or 'BBB' or higher by Standard and Poor's, or by Fitch Ratings Limited<sup>4</sup>, or by Fitch Southern Africa (Pty) Limited. Where the country has been rated by more than one agency, the lower of the ratings applies.

#### e. Leverage

	Leverage
REIT	Debt financing is limited to 60% of the gross value of the underlying asset value

The debt financing of a Company REIT is limited in terms of the company's memorandum of incorporation and the Companies Act, and a Trust REIT is limited in terms of its Trust Deed and the CISA. Furthermore, the JSE requirements only permit a REIT to be geared up to levels of 60% of the gross value of the underlying assets.

#### f. Profit distribution obligations

	Operative income	Capital gains	Timing
REIT	Earn 75% of its income from rental, property owned or investment income from indirect property ownership	No requirement	Distribute at least 75% of its taxable earnings available for distribution to its investors each year

#### Operative income

A REIT is required to distribute at least 75% of its taxable earnings available for distribution to its investors annually. Qualifying distributions by the REIT to unitholders will be treated as deductible expenditure for income tax purposes.

#### Sanctions

	Penalties/loss of status rules
REIT	<ul style="list-style-type: none"> <li>- Non-compliance with the CISA</li> <li>- Non-compliance with the JSE requirements</li> <li>- Non-compliance with the Companies Act</li> </ul>

There are specific sanctions for non-compliance with the CISA, the Companies Act and the JSE requirements, which may result in the renunciation of the REIT status and therefore loss of the tax benefit

<sup>4</sup> Foreign Countries in Which Collective Investment Scheme in Securities Or In Property May Invest' Published under General Notice 2073 in Government Gazette 25283 of August 1, 2003

under the new dispensation.

### 3 Tax treatment at the level of REIT and PLS

#### a. REIT: Corporate tax/withholding tax

Current income	Capital gains	Withholding tax
<ul style="list-style-type: none"> <li>- Subject to tax on dividend income from financial instruments</li> <li>- Allowed to deduct qualifying distributions made</li> <li>- Undistributed income is subject to a tax rate of 28%</li> </ul>	A REIT is generally not subject to capital gains tax	A South African tax resident REIT will not be subject to withholding taxes

#### General

Section 25BB of the Income Tax Act is the primary taxing section applicable to REITs and controlled companies. The basic paradigm underpinning section 25BB is to treat REITs and controlled companies as flow-through entities by granting a deduction for qualifying distributions made to shareholders. Such distributions are then taxed as normal income in the hands of the shareholder.

To qualify for the specific tax regime, a REIT is required to meet the following requirements:

- it must be a company resident in South Africa;
- its shares must be listed on an exchange as defined in section 1(1); and
- its shares must be listed as shares in a REIT as defined in the JSE Listings Requirements.

A controlled company for section 25BB purposes is a subsidiary, as defined in the International Financial Reporting Standard (IFRS), of a REIT.

A property company is a company where at least 20% of the equity shares or linked units are held by a REIT or a controlled company jointly or severally with other relevant companies in the same group of companies. In addition, and with regards to the property company, 80% of the value of the assets is directly or indirectly attributable to immovable property. The concept of a property company is important for the purposes of determining the amounts to be included when calculating the gross income of the REIT and for capital gains tax purposes.

#### Current income

A REIT will be subject to ordinary tax on rental income received at a rate of 28%. A REIT or controlled company may claim a deduction in respect of dividends paid or payable to its shareholders, except in the case of a share repurchase. A REIT may also claim a deduction for interest incurred in respect of a debenture forming part of a linked unit in that company. The deduction may be allowed to the extent that gross rentals received or accrued by the REIT, controlled company or an associated property company exceeds 75% of the gross receipts or accruals of the REIT. The deduction will also be limited to the REIT's taxable income before taking into account any taxable capital gain and the deduction for the amount distributed.

A REIT or a controlled company is precluded from claiming any building tax allowances. However, a wear and tear/depreciation allowance on assets, other than immovable property may be claimed by a REIT or a controlled company, assuming that all relevant requirements are met.

Where a REIT or controlled company is the beneficiary of a non-resident (vesting) trust and this trust was liable/subject to tax on income in the country where it was established, the amount of tax proved to be payable (to a government other than South Africa) by the trust, as is attributable to the interest of the REIT or controlled company in that trust, will be allowed as a deduction from taxable income of the REIT or controlled company. In order for the foreign tax incurred to be deductible, there must be no right to recovery. This deduction is allowed prior to taking into account any deduction of a qualifying distribution.

Similarly, any tax paid by a REIT or controlled company to a government other than South Africa is deductible for income tax purposes if, the amount has been proved to be payable and there is no right to recovery (other than the entitlement to carry back losses). This deduction is allowed before taking into account any deduction of a qualifying distribution.

The amount of any donation made by a REIT or controlled company is allowed as a deduction from taxable income. This deduction is limited to 10% of taxable income, after taking into account both foreign tax deductions (mentioned above) and before any deduction of a qualifying distribution.

## Capital gain

A REIT or a controlled company does not pay tax on capital gains arising from the disposal of immovable property, a share/linked unit in a REIT or a share/linked unit in a property company. In order for the capital gains tax on these disposals to be disregarded, it is vital that the company is a REIT, controlled company or property company at the time of the disposal. A REIT or controlled company may have to account for capital gains tax on the disposal of other assets, not listed above.

## Withholding tax

South Africa imposes withholding taxes on royalties, interest, dividends, payments made to foreign entertainers and sportspersons, and payments from the sale of immovable property or an interest in immovable property situated in South Africa by a non-resident seller. It is unlikely that withholding tax on royalties or similar payments could be applicable to a REIT, given its principal business purpose.

Withholding tax on interest payments at a rate of 15% is only applicable to the extent that such payments are made to non-residents and are subject to the application of the relevant Double Tax Agreement. Therefore, interest paid by a REIT to a non-resident may be subject to withholding taxes. To the extent that a REIT receives any interest income, such amount will form part of its gross income calculation.

Dividends withholding tax, by contrast, is applicable to both resident and non-residents at a rate of 20%. However, dividends paid to South African resident companies are exempt from the withholding tax. Therefore, dividends declared to REITs will not be subjected to the dividends withholding tax, provided the relevant administrative requirements are adhered to.

Foreign dividends received by a REIT will be exempt from tax to the extent that the REIT holds at least 10% of the equity shares in the company declaring the dividend. A REIT may claim a tax credit/deduction for any foreign taxes suffered provided the requirements in section 6 of the Income Tax Act are met.

The REIT is required to withhold dividends tax on distributions made to investors who are not South African tax residents. The current withholding rate is 20%, subject to the applicable Double Tax Agreement.



## Securities transfer tax

In terms of the STT Act, securities transfer tax is levied at a rate of 0.25% on a transfer of a security issued. Securities transfer tax is not payable on the transfer of a security that constitutes a share in a REIT. However, the transfer of a security in a controlled company may be subject to securities transfer tax.

### b. Transition regulations

#### Conversion into PLS to REIT status

A PLS can be converted to a REIT

In accordance with the JSE listing rules, a PLS can be converted to a REIT. The deadline to convert a PLS to a REIT was July 1, 2013. It had until July 2015 to meet the gearing requirements.

### c. Registration duties

#### Registration duties

No specific rules

There are no specific registration duties applicable to a REIT. These vehicles will need to comply with general initial set-up requirements for trusts, companies and JSE listing requirements. Annual fees may be required in respect of the specific vehicle, i.e. JSE annual listing fees, etc.

## 4 Tax treatment at the unit holder's level

### a. REIT: Domestic unitholder

	Corporate unitholder	Individual unitholder	Withholding tax
REIT	<ul style="list-style-type: none"> <li>- Distributions are taxed at 28%</li> <li>- Taxation of capital gains on disposal (if not dealer) at 80% of the gain is included in taxable income (resulting in an effective rate of 22.4%)</li> </ul>	<ul style="list-style-type: none"> <li>- Distributions are taxed at an individual's margin tax rate (between 18% and 45%) as if income was directly received; Note that Trusts are taxed at a different rate</li> <li>- Taxation of capital gains on disposal (if not dealer) 40% of the gain is included in taxable income (resulting in an effective rate of between 7.2% and 18%)</li> </ul>	There are no withholding taxes

### Corporate unitholder

A shareholder holds a property linked unit in the REIT. Any distributions made by the REIT in relation to the property linked unit including the interest paid in respect of the debenture portion will be deemed to be a dividend (excluding in the case of a share repurchase). The property linked unit can also be converted to an equity share.

## Capital gains

A shareholder will be subject to capital gains tax at an effective rate of 22.4% (28% x 80%) on the disposal of a unit in a REIT.

## Withholding taxes

South Africa imposes withholding taxes on royalties, interest, dividends, interest and payments made to foreign entertainers and sportspersons, and the sale of immovable property located in South Africa by a non-resident. It is unlikely that withholding tax on royalties or similar payments could be applicable to a REIT given its principal business purpose.

Withholding tax on interest payments is only applicable to the extent that such payments are made to non-residents at a rate of 15% subject to the application of the relevant Double Tax Agreement.

Dividends withholding tax, by contrast, is applicable to both resident and non-residents at a rate of 20%. However, dividends paid to South African resident companies are exempt from the withholding tax, provided the relevant administrative requirements are adhered to.

Dividends paid by the REIT to non-resident shareholders will be subject to dividends withholding tax at a rate of 20%, subject to the application of a Double Tax Agreement.

## Individual unitholder

The taxation is the same as for corporate unitholders except that capital gains tax is imposed at a rate of 40% of the gains included on taxable income. The resultant tax effective rate is between 7.2% and 18%. Post January 1, 2014, the distributions will still be exempt from dividends withholding tax and will remain taxable as ordinary revenue.

### b. Foreign unitholder

	Corporate unit holder	Individual unit holder	Withholding tax
REIT	<ul style="list-style-type: none"> <li>- Distributions are subject to dividends withholding tax, at 20%, unless reduced by an applicable double tax agreement</li> <li>- Taxation of capital gains on disposal (if not dealer) at 80% of the gain is included in taxable income (resulting in an effective rate of 22.4%), to the extent that the unitholder holds more than 20% of the shares in the REIT</li> </ul>	<ul style="list-style-type: none"> <li>- Distributions are subject to an individual's tax margin rate (between 18% and 45%) as if income was directly received; note that trusts are taxed at a different rate</li> <li>- Taxation of capital gains on disposal (if not dealer) at 40% of the gain is included in taxable income (resulting in an effective rate of between 7.2% and 18%), only to the extent that unitholder holds more than 20% of the shares in the REIT</li> </ul>	Dividends are subject to withholding tax at 20%, subject to the application of a double tax agreement

## Corporate unitholder

As stated above, a shareholder holds a property linked unit in the REIT. Any distributions made by the REIT in relation to the property linked unit including the interest paid in respect of the debenture portion will be deemed to be a dividend (excluding in the case of a share repurchase). The property linked unit can also be converted to an equity share.

## Capital gains

Capital gains tax is levied on a right of whatever nature of a person to or in immovable property situated in South Africa. Such interest in immovable property situated in South Africa includes an interest of at least 20% held by a non-resident in the equity shares of a company or any other entity. In addition, 80% or more of the value of the abovementioned company or other entity at the time of disposal of the shares or interest, must be attributable directly or indirectly to immovable property situated in South Africa other than immovable property.

## Withholding tax

South Africa imposes withholding taxes on royalties, interest, dividends, interest and payments made to foreign entertainers and sportspersons, and the sale of immovable property located in South Africa by a non-resident. It is unlikely that withholding tax on royalties or similar payments could be applicable to a REIT given its principal business purpose.

Dividends and deemed dividends paid by a REIT or a controlled company and received or accrued to a foreign shareholder are subject to dividends withholding tax at a rate of 20%, subject to the application of a relevant Double Tax Agreement. The application of the Double Tax Agreement is subject to the unitholder providing the REIT with certain declarations.

Withholding tax on interest will generally not apply since the distribution made by the REIT is deemed to be a dividend which is subject to dividends withholding tax.

## Individual unit holder

The taxation is the same as for corporate unitholders save for the capital gains tax rates that may be applied.

# 5 Treatment of foreign REITs and its domestic unitholder

Foreign REIT	Corporate unitholder	Individual unitholder
Subject to tax on income from a source in South Africa or which is attributable to a South African permanent establishment or immovable property	Subject to tax on income from REIT based on South African tax residence status, subject to certain exceptions	Subject to tax on income from REIT based on South African tax residence status, subject to certain exceptions

## Foreign REIT

A Foreign REIT will generally be subject to tax on income from a source in South Africa.

## Corporate unitholder

A Foreign REIT will generally be subject to tax on income from a source in South Africa.

## Individual unit holder

A Foreign REIT will generally be subject to tax on income from a source in South Africa if not of a capital nature. Profits of a capital nature are subject to tax if attributable to a permanent establishment or immovable property in South Africa. ■

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GLOBAL  
REIT SURVEY

AFRICA & MIDDLE EAST

# Turkey

REIC

2019

A comparison of the  
major REIT regimes  
around the world.



# 1 General introduction

	Enacted year	Citation	REIT type
REIC	1995	- Capital Markets Law no. 6362 ('CML')	Corporate type National Stock Exchange Commission
		- Communiqué on Principles Regarding Real Estate Investment Companies, Serial III No. 48.1 ('Communique')	
	2014	- The Communiqué Revising the Communiqué on Principles of Real Estate Investment Companies, Serial III number 48.1.a ('Communique number 48.1.a')	
	2017	- The Communiqué Revising the Communiqué on Principles of Real Estate Investment Companies Serial III number 48.1.b ('Communique number 48.1.b')	
	2018	- The Communiqué Revising the Communiqué on Principles of Real Estate Investment Companies Serial III number 48.1.c ('Communique number 48.1.c')	
	2019	- The Communiqué Revising the Communiqué on Principles of Real Estate Investment Companies Serial III number 48.1.ç ('Communique number 48.1.ç')	

The concept of a 'trust' does not exist in Turkey, so REITs are structured as Real Estate Investment Companies (REICs).

REIC is a capital market institution that can invest in real estate, capital market instruments based on real estate, real estate projects and rights based on real estate.

REICs were introduced in 1995 after the completion of the necessary legal arrangements by the Capital Markets Board (CMB). Turkish REICs are corporate income tax-exempt stock companies that must be listed on an organised stock market in Istanbul.

The Turkish real estate market has grown very rapidly and has demonstrated remarkable performance during the past couple of years. In parallel to the increase in demand and high-quality office and retail space, the brand new mortgage system and decreasing interest rates have been the main catalysts for the noteworthy pick up of the real estate market.

REICs have entered the Turkish real estate market as an advantageous vehicle that offers easy access to the profits of huge real estate portfolios. Thus REICs have attracted the attention of both local and foreign investors. The listed REICs' total asset value reached a level of approximately EUR 11,679 million as of December 31, 2018.

From a legal aspect regarding the issues on REICs, the first separate and significant regulation was the Communiqué on Principles of Real Estate Investment Companies Serial III number 48.1 published by Capital Markets Board of Turkey (CMB) on May 28, 2013. This communiqué sets forth the general and fundamental principles such as incorporation, legal form, capital, management structure and other requirements on the REICs.

The first amendment, namely Communiqué number 48.1-a, was published by CMB on 23 January 2014. It consists of provisions pertain to Infrastructure Real Estate Investment Companies (IREICs) which were published at the beginning of 2009 and which were integrated to the Communiqué 48.1 as a type of REIC. Therefore, REICs which are incorporated to manage portfolios composed of infrastructure investment and services and other infrastructure-related market instruments under the provisions of Communiqué number 48.1-a can operate as IREIC. Please note that, in accordance with the Corporate Income Tax Communiqué number 13, IREICs cannot benefit from the Corporate Income Tax exemption.

The latest major amendments on the Communiqué was published in the Official Gazette on January 17,

2017, as the Communiqué number 48.1-b. The provisions on the Communiqué number 48.1-b mainly focus on activities, structure and portfolios of IREICs. In addition to these provisions, there are a number of amendments regarding the management structure of REICs, principals on investments and activities, prohibited activities, principals on valuation and distributions which are elaborated in the following sections. Furthermore, an amendment to extend the period of the temporary clause was published on May 10, 2018.

On January 2, 2019, the Communiqué numbered 48.1-ç was published in the Official Gazette, amending many provisions. One of the major amendments is that portfolio limitations of IREICs are expanded and new exemptions regarding IREICs that have not yet made an initial public offering or been sold to qualified investors are introduced. Also, obtaining services from portfolio management companies for REICs that have more than 10% of their portfolio invested in money and capital market instruments has been introduced as a requirement. The scope of the purposes enabling a REIC to become a subsidiary to other companies expanded. The provision regarding the determination of real estate appraisal companies has been amended.

### Sector summary\*

Listing Country	Number of REITs	Number in EPRA REIT Index	Sector Mkt Cap (EUR m)	% of Global REIT Index
Turkey	33	4	EUR 2,582	0.04%

### Top REICs\*

Company name	Mkt Cap (EUR m)	1 yr return (EUR) %	Div Yield	% of Global REIT Index
Emlak Konut Gayrimenkul Yatirim Ortakligi AS	EUR 631	-52.02%	2.86%	0.028%
Torunlar Gayrimenkul Yatirim Ortakligi	EUR 293	-42.45%	2.59%	0.004%
AKIS Gayrimenkul Yatirimi AS	EUR 154	-5.21%	11.97%	0.004%
Is Gayrimenkul Yatirim Ortak	EUR 147	-16.96%	7.08%	0.006%

\* All market caps and returns are rebased in EUR and are correct as at June 28, 2019. The Global REIT Index is the FTSE EPRA Nareit Global REITs Index. EPRA, July 2019.



## 2 Requirements

### a. Formalities/procedure

#### Key requirements

- Regulated and closely monitored by the Capital Markets Board (CMB)
- Statutes must be in accordance with the law and the procedures of the Communiqué
- Founders must have no records of legal prosecution due to bankruptcy or other offences
- Unless otherwise stated in particular, rules applying to the REICs are also applicable for the IREICs

According to article 6 of the Communiqué, REICs may be constituted by way of establishing new joint-stock companies, or existing joint-stock companies can be converted into REICs by amending their articles of association in accordance with the procedures of the Communiqué and CML.

For the purpose of establishing a REIC, the founders are required to apply to the CMB in order to obtain its approval for the establishment with an application for establishment form, the format and procedures of which are determined by the CMB, and the documents specified in this form.

For either the establishment or the conversion of a company into a REIC, CMB approval must be obtained. In order to obtain the approval for the establishment from the CMB, the applicant companies are required to hold the qualifications specified below:

- Prospective REICs have to be established in the form of joint-stock companies with registered capital;
- Prospective REICs have to be established in order to offer the shares representing at least 25% of the issued capital to the public within three months after the establishment and principles determined by the Communiqué;
- The initial capital should not be less than TRY 36 million for the year 2019 and if a company manages a portfolio consisting of exclusive infrastructure investment and services, the initial capital of this company is required to be at least TRY 120 million. CMB is authorised to amend the mentioned amounts indicating initial capital annually;
- If the initial capital is less than TRY 72 million, at least 10% of the shares representing the initial capital should be issued for cash; if the initial capital is TRY 72 million or more, at least TRY 7.2 million of the shares representing the initial capital should be issued for cash and in the case a company manages a portfolio consisting of exclusive infrastructure investment and services, at least TRY 12 million of the shares representing the initial capital have to be issued for cash. The shares can only be issued in registered or bearer form;
- The phrase ‘Real Estate Investment Company’ must be included in the commercial title;
- Real person founders indirectly and ultimately holding at least 20% or more of the concerned company’s shares and real person founders indirectly holding privileged shares providing management control in the concerned company’s shares must meet the conditions mentioned in the Communiqué;
- Directors and the members of the board of directors of the company must meet the conditions mentioned in the Communiqué.



The articles of association of the prospective REIC have to be in conformity with the provisions of CML, and the Communiqué and affirmative opinion of the CMB needs to be obtained.

- Applicant companies are required to be in the registered capital system or should have applied to the CMB for this purpose;
- Applicant companies are required to declare their commitment to the CMB that at least 25% of the issued capital of that company shall be offered to the public within three months after the conversion and principles determined in the Communiqué;
- The present paid-in capital or issued capital and its equity should not be less than TRY 36 million whereas this amount for IREICs should not be less than TRY 120 million;
- If the present paid-in capital or issued capital is less than TRY 72 million, at least 10% of the shares representing present paid-in capital or issued capital should be issued for cash;
- If the present paid-in capital or issued capital is TRY 72 million or more, at least TRY 7.2 million of the shares representing present paid-in capital or issued capital should be issued for cash;
- An application needs to be filed with the CMB in order to change its commercial title so that the phrase ‘Real Estate Investment Company’ is included;
- Real person shareholders indirectly and ultimately holding at least 20% or more of the concerned company’s shares and real person shareholders indirectly holding privileged shares providing management control in the concerned company’s shares must meet the conditions mentioned in the relevant legislation;
- Directors and the members of the board of directors of the companies must meet the conditions mentioned in the Communiqué.

An application needs to be filed to amend the articles of association to comply with the provisions of the relevant legislation and obtain the affirmative opinion of the CMB.

The CMB evaluates the application in terms of conformity to with the provisions of CML and the Communiqué. Upon obtaining the relevant approval from the CMB, an additional application shall be filed with the Ministry of Trade requesting for the approval of the amendments in the articles of association in the case of conversion or the approval for establishment in the case of establishment.

Companies to be established shall acquire a legal identity upon registration of the company with the Trade Registry in accordance with the related provisions of the Turkish Commercial Code no 6102 (‘Turkish Commercial Code’).

Corporations to be converted shall call the shareholders and, if necessary, the preferred stockholders of the company to a meeting in accordance with article 421 and 454 of the Turkish Commercial Code so that the changes in the articles of association of the concerned company can be approved. With the approval of the amendments and registration with the Trade Registry, the conversion transactions shall be completed.

Further requirements other than those explained above may be imposed by the CMB during the approval process.

## b. Legal form/minimum share capital

Legal form	Minimum share capital
Joint-stock company	TRY 36 million (for REICs) and TRY 120 million (for IREICs)

## Legal form

The general guidelines of joint-stock companies are regulated with the Turkish Commercial Code. REIC specifics shall be determined by the CML and the Communiqué. The company's name must include 'real estate investment company'.

## Share capital

The minimum capital requirement for a REIC is TRY 36 million for the year 2019 and TRY 120 million for IREICs. These amounts may be amended annually by the CMB.

If the initial capital is:

- less than TRY 72 million, at least 10% of the shares; and
- TRY 72 million or more, shares representing at least TRY 7.2 million of the initial capital should be issued for cash, and companies which will exclusively manage a portfolio consisting of infrastructure investment and services have to issue shares representing at least TRY 12 million of the initial capital for cash.

### c. Shareholder requirements/listing requirements

Shareholder requirements	Listing mandatory
Only for company founders	Yes

## Shareholder requirements

It is required in the real estate investment companies that:

- Real or legal person founders must not have any payable tax;
- Real or legal person founders must not be bankrupt, go bankrupt, or have any postponement of bankruptcy;
- Real or legal person founders must not have any responsibility for actions that cause cancellation of an enterprise's activity permits by CMB;
- Real or legal person founders must not be condemned;
- Real or legal person founders, or the corporations that they are shareholders of, must not be subject of a liquidation decision;
- Real or legal persons must have obtained the resources needed for foundation from their own commercial, industrial and other legal activities free from any kind of collusion, and must have the financial power to fund the subscribed capital amount\*;
- Real or legal persons must have the honesty and the reputation required for the business
- Real or legal persons must not have been convicted of crimes under the Law on Prevention of Financing of Terrorism no. 6415; and
- Real or legal persons must not have been banned on trading pursuant to the investigations of insider trading and manipulation under CML.

\*This requirement is not applied in the conversion applications.

In terms of CMB regulations, there are no restrictions on foreign shareholders.

## Listing requirements

At least 25% of the REIC's shares should be offered to the public. REICs are obligated to apply to CMB for offering share certificates representing 25% of their capital to the public within three months as of their establishment or registration of their articles of association's amendment before the trade registry.

### d. Asset level/activity test

#### Restrictions on activities/investments

- Only transactions permitted by the Communiqué are allowed
- Must primarily deal with portfolio management
- The portfolio of a general-purpose REIC is required to be diversified
- If a REIC is established to display activity in a specific area or invest in a specific project, 75% of its portfolio must consist of assets mentioned in its title and/or articles of association
- Cannot be involved in the construction of real estate
- Cannot commercially operate any hotel, hospital, shopping centre, etc
- Cannot provide services by its personnel to individuals or institutions in project development, project control, financial feasibility and follow-up of legal permission except for the projects related or to be related with the portfolio
- Cannot make any expense or commission payment that is not documented or that materially differs from the market value
- Cannot sell or purchase real estate for short-term consistently

The portfolio of a general-purpose REIC is required to be diversified based on industry, region and real estate and to be managed with a long-term investment purpose.

In the case a REIC is established with the purpose of operating in certain areas or investing in certain projects, at least 75% of the REIC's portfolio must consist of assets mentioned in its title and/or articles of association.

REIC's are required to invest in real estates, rights supported by real estates and real estate projects at a minimum rate of 51% of their portfolio values. They can invest in time deposit and demand deposits in TRY or any foreign currency for investment purposes at a maximum rate of 10% of their portfolio values. The rate of vacant lands and registered lands that are in the portfolio for a period of five years that have not been subject to any project development should not exceed 20% of the portfolio value. In addition to these, the minimum 75% rate of the portfolio of the companies which will exclusively manage a portfolio consisting of infrastructure investment and services should consist of these corresponding infrastructure investment and services.

REIC's cannot:

- engage in capital market activities other than portfolio management for its own portfolio limited to the investment areas;
- be involved in the construction of real estate as a constructor;
- commercially operate any hotel, hospital, shopping centre, business centre commercial parks, commercial warehouses, residential sites, supermarkets and similar type of real estates and employ any personnel for this purpose;

- engage in deposit business, conduct business and operations resulting in deposit collection;
- engage in commercial, industrial or agricultural activities other than the transactions permitted;
- grant loans or commit in any debit/credit transaction which is not related to good/services purchase and sale with their participations;
- make any expense or commission payment which is not documented or which materially differs from the market value; or
- sell or purchase real estate for short-term consistently.

REICs can invest in foreign real estate and capital market instruments backed by real estate at a maximum rate of 49% of the portfolio value.

#### e. Leverage

Leverage
Short-term credits limited to five-times the shareholders' equity

In order to meet the short-term fund demands or costs related to the portfolio, a REIC can obtain credits at a rate of five times its shareholders' equity. In order to calculate the maximum limit of such credits, the obligations of the company arising from financial leasing transactions and non-cash credits shall be taken into account.

A REIC can issue debt instruments within the restrictions of the capital market legislation. As for the issued debt securities, the aforementioned credits shall be deducted from the issue limit calculated according to the capital market legislation.

Companies can issue asset-backed securities-based on sales contracts, or on the promise to sell, real estate from the portfolio.

#### f. Profit distribution obligations

Operative income	Capital gains	Timing
REICs determine their own profit distribution politics	Will be regarded within the distributable profit	Annually or quarterly

The CMB sets out specific rules with respect to the timing, procedures and limits of profit distributions. As REICs are public companies, profit distributions of REICs are subject to the general regulations of the CMB regulating the profit distribution of public companies. According to the communiqués regarding dividend distributions, public companies are free to determine their own profit distribution politics. The distributable profit is calculated in line with both CMB and Turkish Commercial Code regulations.

In order to secure the capital position of the REIC, the lesser of the net distributable profit calculated in line with the statutory accounts or in line with CMB regulations should be distributed.

The public companies may freely determine their dividend distribution policy under the CMB's new Dividend Distribution Communiqué through their general assemblies. General assemblies should determine their policy on whether to distribute any dividend, the rate and type (i.e. in cash) of the dividend, the time of the dividend payment and whether to pay an advance dividend. The general

assembly of the company must determine the time of the dividend payment provided that the distribution payment process is initiated no later than by the end of the relevant financial year of that general assembly meeting.

Moreover, based on the CMB communiqué, public companies may freely decide to:

- distribute dividends entirely in cash;
- distribute dividends entirely as shares;
- distribute dividends partially in cash and partially as shares and keep the remaining as reserves; or
- keep all the profits as reserves.

However, the public companies whose shares are not traded in the exchange have to distribute the dividend fully and in cash. Also, the rate of the dividend for those companies cannot be less than 20% of the net distributable profit calculated under the Communiqué.

REICs are entitled to make advance dividend distributions quarterly. Such advance dividend distributions are subject to CMB regulations as well. Advance dividend distributions can only be realised in cash. Advance dividend distributions shall not exceed half of the net interim profit remaining after subtracting the legal reserves and accumulated losses.

Besides, the advance dividend distribution amount shall not exceed the lower one of the following amounts;

- a. half of the previous year's net profit amount, or
- a. the total amount of other distributable sources, except the net profit amount stated in the financials of the corresponding interim period.

In addition to above-mentioned provisions, a temporary clause concerning profit -distribution is stipulated for the IREICs under the Communiqué number 48.1-b and amended by Communiqué number 48.1-c to extend the period. Article 45 of the Communiqué regulating prohibition of the cash profit distribution before the public offering of shares or sales to the qualified investors will not be applicable for the IREICs until December 31, 2019.

## g. Sanctions

### Penalties/loss of status rules

Modification of the articles of association to exclude real estate investment company operations

If REICs do not apply to the CMB by completing the public offering application form and the documents mentioned in this form within the time periods, or if the application is found inappropriate due to the failure to fulfil the necessary conditions, the REIC shall lose the right to operate as an REIC. The CMB will inform the Ministry of Finance, and the company loses its tax-exempt REIC status.

As the company will lose its REIC and tax-exempt status, unpaid taxes, late payment interest and tax penalty may be levied retrospectively on the REIC from the incorporation date of the company.

In addition to judicial fines, the CMB may impose administrative fines for breaches of the CMB regulations or decisions made by the CMB or take relevant measures or bring the case to court or the public prosecutor's office where relevant.

### 3 Tax treatment at the REIC level

#### a. Corporate tax

Current income	Capital gains	Withholding tax
Tax-exempt	Tax-exempt	Credit/refund may be possible

#### Current income

Generally, corporations in Turkey are subject to 20% corporate tax (22% for the years 2018, 2019 and 2020) which is payable over the fiscal profit after adjusting for deductible/non-deductible items and exemptions. Annual corporate tax is declared and paid in April of the following year (assuming that a normal calendar year is applied).

The determination of the taxable income of REICs is no different from ordinary companies in Turkey. On the other hand, REICs are exempt from corporate tax, and whilst they are obliged to submit an annual corporate tax return in April of the following year, they do not pay any corporate tax.

The dividend income of Turkish resident companies obtained from its taxable Turkish resident subsidiaries is exempt from corporate income tax.

Dividends received from non-taxable subsidiaries are taxable in Turkey. However, dividends received by REICs, in general, are tax-exempt due to REIC exemption status.

The foreign corporate income of REICs is also exempt from corporate tax.

#### Dividends

A dividend withholding tax rate of 15% is applicable to dividends distributed to individual and foreign corporate shareholders. However, for REICs, the Council of Ministers has determined a withholding tax rate of 0%. Therefore, dividend distributions to individual and non-resident shareholders of REICs create no dividend withholding tax burden.

#### Capital gains

Capital gains are, in principle, deemed the commercial income of an REIC and are thus regarded as corporate tax-exempt.

#### Withholding tax

REICs may have income subject to withholding taxes to be taxed at source. A credit/refund may be possible.

#### Accounting rules

Turkish REICs are required to prepare audited financial statements in accordance with the standards of the CMB, which are very similar to IFRS standards.

There is no separate tax accounting system in Turkey. The provisions of the tax laws are applied to the determination of taxable income by making adjustments to the fiscal profit determined in accordance with the CMB financial standards.

## b. Transition regulations

### Conversion into REIC status

In principle, no tax privilege

There is no exit tax or any other major tax to be applied upon transformation from a regular company into a REIC.

There is no privileged exit taxation rule for capital gains realised on real estate if sold to a REIC. However, there is a specific limited exemption rule stipulated in the Corporate Income Tax Code and applicable only for resident companies. According to this rule, under some certain conditions, 50% of the gains derived from the disposal of real estate may be exempted from corporate taxes. This is not a special rule for real estate disposals to REICs. However, according to Corporate Tax Code, the earnings that a company, which is engaged in the trading of real estate property or their rental, obtained from the sale of such assets, are not eligible to the exception.

## c. Other taxes

### Registration duties

- Title deed fee of 3% until December 31, 2019 (after this date 4% will be applied)
- Stamp tax exemption
- A transfer may be subject to VAT

## VAT

Since no specific VAT exemption is applicable for the transactions carried out by REICs, transactions of REICs are subject to value-added tax (VAT). All transactions carried out by REICs, including the purchase and sale of land or any other real estate by an REIC from/to a Turkish resident company will be subject to 18% VAT which is accounted as input VAT.

On the other hand, there are some exemptions to the above-mentioned principle:

- If the seller of the real estate is an individual who is not constantly engaging in real estate trading, the sale of real estate is not subject to VAT;
- Acquisitions of real estate from banks and insurance companies are not subject to VAT but are subject to banking and insurance transaction tax (BITT) at the rate of 5%. Please note that this BITT is taken as a cost; and
- Acquisitions of real estate from companies whose main activity is not real estate trading is exempt from VAT if the seller company has held that real estate for at least two years at the time of sale.

However, the input VAT that has been accumulated can be offset against the output VAT calculated over the sales or rental income of the REIC. Please note that the input VAT, that has been accumulated which could not be offset against the output VAT, cannot be considered as a deductible expense in the determination of the corporate tax base.

Effective VAT rate to be applied on the sale of residential units which are holding their building license as from January 1, 2013 with a net area of less than 150 sq.m. will be 1%/8%/18% based on some certain conditions stated in the corresponding legislation.

Within the scope of the latest updates in the legislation, VAT implementation for the houses and commercial units, which are subject to 18% VAT, is updated and decreased to 8% until 31 December 2019. For the transactions of other types of real estates other than houses and commercial units, the reduced VAT rate will not be applied.

### Title deed fee

The acquisition of the legal title of Turkish property is subject to a 2% title deed charge over the higher of the sales price or the real estate tax base, which is determined by the related municipality by taking into consideration the fair market value of the real estate. This title deed fee is applicable to both the buyer and the seller separately. Therefore, the total title deed charge burden is 4%. Additional title deed fees may also apply depending on the type of the title deed transaction.

With the latest amendment, a reduced title deed fee of 3% for residential and commercial units will be available until 31 December 2019. For other types of real estates, total title deed fee will remain at 4%.

### Stamp tax

Stamp tax applies to a wide range of documents, including but not limited to agreements, financial statements and payrolls. Stamp tax is levied as a percentage of the monetary value stated on the agreements at rates ranging from 0.189% to 0.948%.

On the other hand, promise to sell agreements and agreements signed by REICs regarding the acquisition and the disposals of real estate are exempt from stamp tax. Please note that apart from these agreements REICs are also subject to all stamp tax liability mentioned above. The new amendments under Stamp Tax Law on reducing stamp tax rate on preliminary sales agreements to 0% were published on February 2017. Stamp tax rate is reduced to 0% on contracts specific to the construction sector such as flat for land and revenue sharing contracts.

Agreements that have a monetary value stated on it is separately subject to stamp tax at a general rate of 0.948% (9.48 per thousand) with a ceiling of TRY 2,135,949.30 (approximately EUR 392,000 under the current foreign exchange rate, subject to annual revaluation) for the year 2018.

Lease contracts are also subject to stamp tax. The rate applicable per original copy of a lease agreement is 0.189% (1.89 per thousand) with the cap amount mentioned above. In the case the period of the rental contract is longer than a year, the taxable base for the stamp tax is the total rent amount calculated over the full rental income and the total period of the contract.

### Property tax

An annual property tax (real estate tax) is levied on the owner of real estate.

Buildings and land owned in Turkey are subject to property tax at the following rates:

- Residences: 0.1%
- Other buildings: 0.2%
- Vacant land (allocated for construction purposes): 0.3%
- Land: 0.1%

Furthermore, the effective property tax rates double for property located within the borders of metropolitan areas.

### Environmental tax

Annual environmental tax will become due based on a tariff that does not have a material value.



## 4 Tax treatment at the shareholder's level

### a. Domestic shareholder

Corporate shareholder	Individual shareholder	Withholding tax
Dividends and capital gains from share disposal subject to the standard corporate income tax rate	5 Dividends and capital gains from share disposal subject to the standard corporate income tax rate	General view: N/A

#### Capital gains received by resident corporations

The capital gains derived from the sale of REIC shares by resident legal entities are to be included in the corporate income and will be subject to corporate income tax at 20% (22% for the years 2018, 2019 and 2020). However, there is a special partial exemption method that can be used to minimise the tax burden which is available for 75% of the gains derived from the sale of shares that are held for at least two years, with certain further conditions.

#### Dividends received by resident corporations

Since REICs are exempt from corporate tax, 'participation exemption' is not applicable for the dividends received from REICs. So, dividends received by corporations in Turkey from REICs are subject to a 20% corporate income tax (22% for the years 2018, 2019 and 2020). And then, if distributed to non-resident companies or individuals, those distributions are also subject to dividend withholding tax in line with local regulations.

#### Capital gains received by resident individuals

Since REICs are public companies, capital gains derived from the sale of shares in the Borsa Istanbul by resident individuals will be subject to taxation via withholding tax. The current rate of 0% withholding tax is applicable for the capital gains received by resident individuals, and that tax will be the final tax for those individuals.

#### Dividends received by resident individuals

Resident individual shareholders of REICs are obliged to declare half of the dividends received from REICs if half of the dividends received exceed the declaration limit (approx. EUR 5,000 for the year 2019). Declared income will be subject to Income tax at the progressive rate between 15%-35%.

### b. Foreign shareholder

Corporate shareholder	Individual shareholder	Withholding tax
0% withholding tax	0% withholding tax	0% withholding tax

## Capital gains received by non-resident corporations

Since REICs are public companies, capital gains derived from the sale of shares in the Borsa Istanbul by non-resident legal entities that do not have a permanent establishment in Turkey will be subject to taxation via withholding tax. The current rate of 0% withholding tax is applicable for the capital gains received by non-resident corporations, and that tax will be the final tax for those companies.

Please note that capital gains derived from the sale of non-listed Turkish company shares by non-resident corporations that do not have a permanent establishment in Turkey is to be declared after the application of cost adjustment (adjustment of the original cost with Whole Sale Price Index (WPI) except for the month the shares are disposed if the total increase in WPI is more than 10%), within 15 days following the sale of shares, through a special corporate tax return and be taxed at standard corporation tax rate. Additionally, dividend withholding tax will be applied on the net gains. But, since most of the Double Tax Treaties prohibits Turkey's taxation right on these capital gains depending on the holding period (one year in most cases) of the Turkish company shares, we strongly suggest examining double tax treaties before these transactions.

## Dividends received by non-resident corporations

Dividends that are distributed by REIC will be subject to a 0% dividend withholding tax in Turkey. On the other hand, taxation of dividends in the hands of non-resident corporations depends on the tax treatment of the country of residence.

## Capital gains received by non-resident individuals

Since REICs are public companies capital gains derived from the sale of shares in the Borsa Istanbul (BIST) by non-resident individuals, will be subject to taxation via withholding tax. The current rate of 0% withholding tax is applicable for the capital gains received by non-resident individuals, and that tax will be the final tax for those individuals.

## Dividends received by non-resident individuals

Dividends that are distributed by REIC will be subject to a 0% dividend withholding tax in Turkey. On the other hand, taxation of dividends in the hands of non-resident individuals depends on the tax treatment of the country of residence. ■

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