

Sydney REIT TAX CONFERENCE

General EU Structuring Issues

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Focus EU REITs

- Definition
- Overview
- Comparison of recent REITs
- Impact of EU law
- Summary
- Final remarks

What makes a fund vehicle a REIT?

- vehicle
- owns income producing real estate
- exempt from corporate income tax
- obligation to distribute profit

And also:

- collective investment?
- listing/shareholders requirements?
- other assets/activities allowed
- Risk diversification?
- limited leverage?

Overview

(REITs and REIT-like vehicles)

- Netherlands (1969): Beleggingsinstelling (BI)
 - no limitation to real estate
 - 0% tax rate
 - market capitalisation: € 15 billion
- Germany (1969): Sondervermögen/Investment Fund
 - no obligation to distribute profits
 - deemed distribution

Overview - continued

- Luxembourg (1988) FCP/SICAV/SICAF
 - no limitation to real estate
 - no distribution obligation
- Spain (1992) SII/FII
 - subject to 1% tax
 - no distribution obligation
 - limited use

Overview – continued

- Italy (1994) FII
 - no distribution obligation
- Belgium (1995) SICAFI
 - REIT
- France (2003) SIIC
 - REIT
 - Incentives
 - Big bang: € 10 - € 25 billion
 - substantial drop in NAV discounts

Overview – continued

The year 2007:

- Netherlands: BI regime to be amended
- Netherlands: BI Plus regime to be introduced. Not for real estate!
- UK: UK-REIT introduced
- Germany: G-REIT to be introduced
- Luxembourg: SIF
- Italy: SIIQ to be introduced
- Spain: contemplating introduction of a REIT regime

Comparison of main features

- Dutch BI
- French SIIC
- UK-REIT
- G-REIT

(Comparison)

Dutch BI

- Legal form: Dutch N.V., B.V. or mutual fund
- Tax residence: In the Netherlands
- Assets: Only passive; no real estate development
- Shareholders: Extensive requirements to ensure widely held
- Listing: Not necessary, but more lenient shareholder requirements for Amsterdam-listed BI's
- Tax exemption? 0% tax rate
- Distribution: Obligation to distribute 100% taxable profit (not including capital gains)
- Leverage: maximum 60% leverage of tax book value of the real estate
- DWT: 15%

(Comparison - continued)

Dutch BI-amended (plan 2007)

- Legal form: EU companies and Tax Treaty companies can qualify. Latter only if non-discrimination clause in treaty. Not Australia!
- Tax residence: requirement dropped
- Activities: real estate development allowed in taxable subsidiary
- Shareholders: simplified and discrimination against foreign shareholders and non-Amsterdam listing removed

(Comparison - continued)

French SIIC

- Legal form: SA or SCA or any foreign equivalent
- Tax residence: No requirement
- Assets/activities: Main object must be real estate rental. Other assets not to exceed 20% of gross assets. Property development for own portfolio allowed
- Shareholder requirements: No
- Listing requirement: Yes, on French stock exchange
- Tax exemption: On property rental income/gains. Other activities subject to tax
- Distribution: 85% of rental income (12 months) plus 50% of capital gains (24 months)
- Leverage: No specific limitation
- DWT: 25%

(Comparison - continued)

UK REIT

- Legal form: Several requirements.
- Tax residence: UK resident only
- Assets/activities: Main object must be property rental. 75% of business (measured by assets and by income) must be property rental. Property development for own portfolio tax exempt
- Shareholder: No corporate shareholder to hold 10% or more directly
- Listing requirement: Listing on a recognized stock exchange
- Tax exemption: Property rental business exempt. Other activities taxable
- Leverage: $\frac{\text{profit} + \text{financing costs}}{\text{financing costs}} < 1,25$
- DWT: 30%?

(Comparison - continued)

G-REIT

- Legal form: REIT-AG or SE
- Tax residence: German tax resident only
- Assets/activities: Main object must be property rental. 75% of business (measured by assets and by income) must be property rental. Property development for own portfolio allowed.
- Shareholders: < 10% participations
- Listing: On a recognized EU stock exchange. Free float of at least 15% (at listing at least 25%)
- Tax exemption: Full tax exemption
- Distribution: 90% (12 months) of distributable profits. Distribution of 50% of capital gains can be delayed
- Leverage: < 60% of fmv of assets
- DWT: 26.375%

REITs compared

- More uniformity
- Property rental profits exempt
- Distribution obligation
- Taxation shifted to shareholder level
- Foreign shareholders subject to source tax

REITs compared

- Harmonization?
- One EU REIT for all EU investors for all EU property investments?
- Discrimination of foreign REITs
- Discrimination of foreign shareholders – source taxes

Impact of EU law

- Direct taxes: Member State sovereignty
- EC Treaty: six fundamental freedoms
- “Negative integration”: ECJ decisions
- Potent example: 2002 case Lankhorst-Hohorst

EU law impact on REIT requirements

- Legal form
- Tax residence
- Listing
- Shareholders

EU law impact - continued

Legal form:

- E.g. Belgium, Germany and the Netherlands
- Forbidden discrimination on nationality (article 12 EC Treaty)
- No legal form requirement in France
- Netherlands set to remove legal form requirement
- Germany to introduce it?

EU law impact - continued

Tax residence

- All except France
- Non-French REITs qualified as SIIC
- Indirect discrimination against nationality (“Commerzbank case” and “Avoir fiscal case”)
- Objective difference between resident and non-resident REIT?
- Netherlands to remove residency requirement

EU law impact - continued

Tax residence (continued)

- Recent UK, Germany, Italy: REIT must be tax resident
- Why?
- Foreign investors and fair tax share
- Taxation shifted to shareholders
- Only source tax on resident REIT; Art. 10(5) OECD Model
- Compare:
 - no direct participation $\geq 10\%$
 - full exemption Germany

EU law impact - continued

Shareholders

- Dutch BI has more stringent requirements for foreign shareholders
- Indirect discrimination
- To be amended

EU law impact - continued

Listing:

- Local listing requirements in France and Italy
- Belgium removed local listing requirement
- Netherlands has more lenient BI-requirements for Amsterdam listed BI's
- Probably an indirect discrimination
- Netherlands to remove discrimination in 2007

Summary

- 2007: big year for EU REITs
- Several attractive regimes
- More to be expected
- More or less uniform underlying principles
- However: no pan-European investment REIT in sight
 - discrimination of foreign REITs
 - discrimination of foreign shareholders
- Impact of ECJ?

Final remarks for Australian investors

- Advice remains: country-by-country approach
- Direct investment attractive, unless:
 - Investor qualification issues
 - Tax on gross rental income
 - High RETT/VAT
- Investment through local partnership to be considered
 - save RETT?
 - limited liability
 - but: entity qualification issue in Australia

Final remarks for Australian investors - continued

- If investment via local corporation
 - avoid source taxes
 - appropriate European holding structure required
 - challenge: substance
 - maximise leverage
 - if share deal: debt push down
 - challenge: local thin cap rules
- Favourite holding flavour: Luxembourg