



SOCIEDADE DE ADVOGADOS, SP,RL
ROGÉRIO FERNANDES FERREIRA
& ASSOCIADOS



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NEWSLETTER

THE NEW REAL ESTATE INVESTMENT TRUSTS (“REITs”) IN PORTUGAL

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SUMMARY

The revitalization of the real estate market and the Portuguese capital markets led the Government to approve the first real estate investment trusts regime. These companies are a new type of vehicle, incorporated to promote real estate, converting real estate investment in financial investment, with its regime being specifically directed to the leasing market.



www.rfflawyers.com
Praça Marquês de Pombal, 16 – 5th (Reception)/6th
1250-163 Lisboa • Portugal
T: +351 215 915 220 • F: +351 215 915 244
contact@rfflawyers.com



FRAMEWORK

The revitalization of the real estate market and the national capitals’ market led the Government to approve a regulatory framework for the new Real Estate Investment Trusts. (“REITs”). These companies are new vehicles incorporated to promote real estate investment, converting the real estate investment into financial investment, with the legal framework also directed to the enhancement of the leasing market in general. It will be necessary to analyze the reaction of markets and international players, bearing in mind the restrictive rules of the new legislation, notably on what concerns indebtedness, investment and results distribution policies. The Portuguese experience will probably be different from the Spanish case, where no companies of this type have been incorporated in the first 4 years of the implementation of the Spanish regime, which was also caused by the absence of a specific tax regime, contrary to the Portuguese case, where the Collective Investment Vehicles (“CIVs”) tax regime will be applicable.

THE NEW REITs

On the 28th of January of 2019, Decree-Law n.º 19/2019 was published, setting

up the regulatory framework for the new REITs.

REITs are real estate investment companies, regulated by the Companies’ Code (“CSC”) and by the rules applicable to private limited companies, also being regulated by the Portuguese Securities Code (“PSC”).

The fact that the legislation qualifies these companies as real estate investment companies is particularly important, especially on what concerns the applicable tax regime, i.e. the application of article 22 of the Tax Benefits Code. (“EBF”)

REQUIREMENTS APPLICABLE TO COMPANIES

In order to be qualified as a REIT, companies need to fulfill the following requirements:

- i) Adopt the form of a public limited company and have the supervisory bodies set forth on article 413.º, n.º 1, al. b) of the CSC, i.e., having a Supervisory Board and an Official Auditor;
- ii) Have as corporate purpose the following activities:

- The acquisition of property rights, building rights or other property rights of equal content, as well as leasing and other forms of property exploitation. In the case of leasing, it includes not only the development of projects of construction and rehabilitation, but also leasing for commercial purposes, at shopping centers or offices;
 - The acquisition of shares on other REITs or shares on companies with statutory office located in the EU (i) with the same corporate purpose of REITs; (ii) whose assets abide by the limits set forth on the Portuguese legislation (iii) whose share capital is composed of nominal share (iv) whose profit distribution policy is similar to the one set forth on the Portuguese legislation;
 - The acquisition of share units or shares of (i) companies with profit distribution policies like the Portuguese regime or (ii) CIVs (Investment Funds) or Real Estate Leasing Investment Funds or Companies;
- iii) Have a minimum subscribed and fully paid up share capital amounting to € 5.000.000, represented by common shares, not being allowed the issuing of categories of shares;
- iv) Comply with the portfolio and indebtedness limits set forth in the Portuguese legislation;
 - v) Include in the company’s name “Sociedade de Investimento e Gestão Imobiliária, S.A.” or “SIGI, S.A.”;
 - vi) The shares are listed and traded in the stock exchange market or in a system of multilateral negotiation (Euronext Access or Alternext, in Portugal).
- REITs may be incorporated with or without invitation for public subscription, which means that in the latter case articles 279.º to 283.º of the CSC will be applicable. As mentioned beforehand, it is not allowed to create categories of shares, which means that promoters cannot be granted special advantages. The shares of the promoters are immediately sellable, and they integrate the same category of shares of other subscribers. Contrarily to the general regime of public limited companies, in REITs deferment of the obligation to pay-up the share capital is not allowed.
- The corporate registry regarding the incorporation of REITs is deemed

temporary, until all shares are subscribed.

In the case of incorporation with invitation for public subscription, the incomplete subscription of shares does not prevent the conversion of the incorporation registry from temporary to definitive, if, at least 3/4 of the shares designated for public subscription are effectively subscribed and provided:

- i) All the promoters’ shares have been subscribed;
- ii) The subscribed shares are enough to comply with the minimum amount of share capital of € 5.000.000;
- iii) Express mentioning to the incomplete subscription was included on the documents concerning the offer to subscribe.

CONVERSION OF COMPANIES INTO REITs

Public limited companies, as well as CIVs adopting a company form, may be converted into REITs.

Regarding public limited companies, these may be transformed into REITs by resolution of the General Meeting of Shareholders, adopted by the majority required to modify the articles of

association – in principle, 2/3 of the votes. The General Meeting of Shareholders which resolves the conversion, also needs to approve the modifications in the articles of association, so as to guarantee that the REIT legal requirements are complied with. In this case, the conversion comes into effect on the first day of the taxation period following the registration of the modifications of the articles of association. If there is the need to demerge several activities of the public limited company, each split activity is considered one economic unit.

In the case of conversion of CIVs into a REIT, the resolution approving the conversion must be approved by, at least, 90% of the share capital. The shareholders who voted against the conversion have the right to abandon the CIV via redemption of the units, or, otherwise, by acquisition of the shares by the CIV’s Managing Entity or by any third-party. The shareholder who intends to redeem his units must communicate it to the CIV’s Managing Entity, within 15 days after the conversion resolution.

A resolution of conversion of the company and the articles of the association need to be immediately submitted to the CMVM, as the

resolution is published in the informational system, with the conversion producing effects as of the date of the resolution, which will also determine the cancelation of the license to act as a CIV (granted by CMVM).

THE COMPOSITION OF THE ASSETS AND THE LIMITS TO INDEBTEDNESS

One of the features of the REITs regime is the existence of legal limits, both for the type of asset and for the indebtedness of the REIT.

REITs need to comply with a double limit (which can be verified at all time, as of the second year of incorporation of the REIT), concerning the portfolio composition:

- i. Rights over real estate properties and equity invested on REITs, which can be part of the REIT’s corporate purpose have to represent at least 80% of the total amount of assets;
- ii. The amount of the real estate rights designated for leasing must represent at least 75% of the total amount of assets.

When calculating the limits specified above, it is only considered the value of

the real estate property which is free of charges, burdens and encumbrances which may impair the sale, except for collaterals established in order to finance the acquisition, construction or rehabilitation of the real estate units.

If the REIT is the parent-company of a group of companies, the limits specified above must be assessed considering the consolidated accounts of the group.

In relation to real estate property owned in co-ownership, these can only be considered and included in the calculations if:

- i. the property is functionally attached to the exploitation of units owned by the REIT and there is a written agreement about the allocation of profits and costs;
- ii. the property is owned in co-ownership with other REITs, provided there is an agreement of allocation of profits and costs or, in alternative, there is an agreement about a future implementation of the strata title.

On the other hand, any asset acquired by the REIT must be held for, at least, 3 years following the acquisition. This limitation is intended to avoid the incorporation of REITs for speculation purposes only.

Regarding the indebtedness capacity of REITs, these cannot have a debt ratio exceeding 60%. The justification for this limit is based on the necessity of preserving the stability of the financial system.

REITs may acquire plots of lands, but these need to be qualified as buildings or being established under the strata title, in the 3 years following the acquisition.

STOCK MARKET TRADING

Within the first year of incorporation of the REIT, the shares must be admitted for stock exchange trading in the regulated exchange market or selected for trading in multilateral systems, located in Portugal or in the other EU Member States.

When the shares are admitted or selected for stock exchange trading, at least 20% of the shares must be diffused between the investors with less than 2% of the shares and voting rights.

INCOME DISTRIBUTION

The income distribution policies of REIT are one of the milestones of its legal framework, aimed at attracting smaller

investors, and ensuring a mandatory income distribution, if applicable.

The new regulatory framework establishes that, within 9 months following the closing of the financial year, REITs need to distribute, under the form of dividends:

- i. 90% of the profits of that period resulting from the payment of dividends and profits of units in investment funds;
- ii. 75% of the remainder profits (the ones arising out of the real estate activity *per se*).

On the other hand, the legal framework imposes the reinvestment of the product of sale of the assets: at least 75% of the net proceedings which result from the sale of assets of the REIT must be reinvested in other assets within 3 years following said sales.

On what concerns legal reserves, these cannot exceed 20% of the share capital.

SANCTIONATORY FRAMEWORK

Although there is not an express misdemeanor regime, it is clarified that the violations of requirements regarding corporate purpose, share capital, assets and indebtedness limitations and stock exchange trading and dispersion rules,

determine the loss of the REIT character and qualification.

The loss of the REIT qualification does not impair the nature of a publicly traded company. In that case, the company will be regulated under the rules for stock companies.

The loss of the REIT qualification also means that the company cannot reapply for this status for a period of 3 years.

TAX REGIME

The tax regime applicable to the REIT companies is the one provided on articles n.º 22 and following of EBF, applicable to all real estate investment companies.

REITs are subject to the general tax regime of Corporate Income Tax and, to the general 21% rate, applicable to the net income of the period.

According to this regime, when determining the net profit of the period, one excludes capital income (interests, dividends), real estate income and capital gains income, except when this income is paid by entities whose residence or domicile is located at offshore jurisdictions or tax havens.

Costs related with the exempt income, cannot be deducted and are not accepted as tax expenditure.

Income and expenditure related with commissions is also excluded of the profits' base.

The taxation of investors is made at the exit.

If the investor is a private individual, dividends have a 28% flat rate withheld at source. This tax is the final tax, except if the income arises out of a commercial, industrial or agricultural activity.

When the investor sells the shares, the capital gain originated with this transaction is subject to withholding tax at a flat rate of 28%.

If the investor is a company, the capital gain will be subject to a 25% withholding flat tax rate, which is deemed as a payment on account (not a final tax), except when the investor benefits from a capital gains exemption. In this case, the withholding tax will be considered as a final payment. If applicable, and in case all conditions are met, Participation Exemption may be applicable on the distribution of dividends or on the capital gain obtained with the sale.



In case of non-resident investors (private individuals or companies), withholding tax is made at a flat rate of 10%.

ENTRY IN FORCE

The new REIT regime enters in force on the 1st of February of 2019.

Lisbon, February 5th, 2019

Rogério Fernandes Ferreira

Tomás Calejo Abecasis

Pedro Miguel Callapez

Frederico Ferreira da Silva