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Key Tax Issues at Year End for Real Estate Investors 2019/2020

An overview of year-end to-dos and important issues in real estate taxation in 37 tax systems worldwide

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Introduction

International tax regimes are diverse, complex and variant, and are usually full of fixed dates, terms and deadlines. These dates, terms and deadlines need to be observed carefully in order to avoid penalties and to receive certain tax reliefs or exemptions. At year end these obligations become even more difficult to understand and fulfil, particularly for real estate investors with investments in numerous countries.

This publication gives investors and fund managers an overview of year-end to-dos and important issues in real estate taxation in 37 tax systems worldwide.

Furthermore, it highlights what needs to be considered in international tax planning and the structuring of real estate investments.

Please note that the list of year-end to-dos is not exhaustive. Further matters may be relevant.

We hope that you will find Key Tax Issues at Year End for Real Estate Investors 2019/2020 a useful reference and source of information. We would be pleased to assist you with any further requests.

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List of abbreviations

ACE	Allowance for Corporate Equity
AE	Associated Enterprise
AIMI	Portuguese Additional Real Estate Municipal Tax
ATAD	Anti-Tax Avoidance Directive
ATED	Annual Tax on Enveloped Dwellings
BCRA	Banco Central de la República Argentina (Argentine Central Bank)
BEPS	Base Erosion and Profit Shifting
BGC	Business as a Going Concern
BIST	Borsa Istanbul
BITA	Business Income Tax Act
CbCR	Country-by-Country Reporting
CCA	Capital Cost Allowance
CFC	Controlled Foreign Company
CGT	Capital Gains Tax
CIT	Corporate Income Tax
CITA	Corporate Income Tax Act
CIV	Collective Investment Vehicle
COFINS	Contribuição para o Financiamento da Seguridade Social (Contribuition for Social Security Financing)
CMN	Conselho Monetário Nacional (National Monetary Council)
CRA	Canada Revenue Agency
CSLL	Contribuição Social sobre o Lucro Líquido
CVAE	Cotisation sur la valeur ajoutée des entreprises
DDD	Deemed Dividend Distribution

DTT	Double Tax Treaty
EBITD	Earnings before Interest, Tax and Depreciation
EBITDA	Earnings before Interest, Tax, Depreciation and Amortisation
ECJ	European Court of Justice
EEA	European Economic Area
FAIA	Fichier Audit Informatisé Administration de l'enregistrement et des domaines (Computerised VAT audit file in Luxembourg)
FII	Fundo de Investimento Imobiliário (Brazilian REIT)
FIIS	Fonds d'Investissement Immobilier Spécialisé (Belgian Real Estate Investment Fund)
FIFO	First In, First Out
FMV	Fair Market Value
FONDCE	Fondo Fiduciario para el Desarrollo de Capital Emprendedor (Trust Fund for the Development of New Businesses/Entrepreneurial Capital)
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAAR	General Anti-Abuse Rule
GDP	Gross Domestic Product
GST	Goods and Services Tax
GVBF	Gespecialiseerd Vastgoedbeleggingsfonds (Dutch for FIIS)
GVV	Gereglementeerde Vastgoed Vennootschap (Dutch for SIR)
HUF	Hindu Undivided Family
IRES	Imposta sul Reddito delle Società (Italian Corporate Income Tax)
IFI	Impôt sur la Fortune Immobilière
IFRS	International Financial Reporting Standards
IMI	Imposto Municipal sobre Imóveis (Portuguese Real Estate Municipal Tax)
IMU	Imposta Municipale Unica (Italian Local Property Tax)
IOF	Imposto Sobre Operações Financeiras (Financial Transaction Tax)
IPO	Initial Public Offering

IRAP	Imposta Regionale sulle Attività Produttive (Italian Regional Production Tax)
ISF	Impôts de la Solidarité sur la Fortune
ITA	Income Tax Act
ITBI	Imposto sobre Transmissão Intervivos de Bens Imóveis (Real Estate Transfer Tax)
ITC	Input Tax Credit
JDA	Joint Development Agreement
MAT	Minimum Alternative Tax
MLI	Multilateral Instrument
MNE	Multi National Enterprise
MREC	Mutual Real Estate Company
NATO	North Atlantic Treaty Organization
NCST	List of Non-Cooperative States and or Territories
NFE	Net Financial Expenses
NID	Notional Interest Deduction
NOL	Net Operating Loss
NRCGT	Non-Resident Capital Gains Tax
NWT	Net Wealth Tax
OECD	Organisation for Economic Co-operation and Development
OPCI	Organisme de Placement Collectif en Immobilier (open-end fund)
PCM	Project Completion Method
PE	Permanent Establishment
PIS	Programa de Integração Social (Employees' Profit Participation Program)
PIT	Personal Income Tax
POCM	Percentage-Of-Completion Method
PPT	Principle in Principal

RE	Real Estate
REAT	Real Estate Acquisition Tax
REIT	Real Estate Investment Trust
REF	Real Estate Fund
RET	Real Estate Tax
RETT	Real Estate Transfer Tax
RMA	Resource Management Act
RRR	Renovation, Reconstruction and Restoration
RUSF	Resource Utilisation Support Fund
SAF-T	Standard Audit File for Tax Purposes
SDC	Special Defence Contribution
SEBI	Securities and Exchange Board of India
SEZ	Special Economic Zones
SIR	Société Immobilière Réglementée
SOCIMI	Sociedades Anónimas Cotizadas de Inversión en el Mercado Inmobiliario (Spanish Real Estate Investment Trusts)
STT	Securities Transaction Tax
TCP	Taxable Canadian Property
TIVUL	Tax on the Increase in Value of Urban Land
TP	Transfer Pricing
VAT	Value Added Tax
WHT	Withholding Tax

Europe

1 Austria

Tax group

In order to form a tax group between companies, a written application has to be signed by each of the group members prior to the end of the fiscal year of the respective group member for which the application should become effective.

Consequently, the taxable income of the group members is integrated into the parent's income. Profits and losses can be compensated between group members.

Make sure the written application has been filed before the end of the fiscal year.

Losses carried forward

Tax losses may be carried forward for an unlimited period of time and may be offset in the amount of 75% of the total amount of the annual taxable income. However, any transfer of shares or reorganisations may lead to a partial/total forfeiture of losses carried forward.

In order to avoid negative tax consequences regarding tax losses carried forward, any transfer of shares or reorganisations should be reviewed in detail.

Substance requirements

Please note that anti-abuse provisions apply to the application of double tax treaties (DTTs) as well as to the Parent Subsidiary Directive. Relief-at-source is available only if the direct parent company issues a written declaration confirming that
- it is an "active" company carrying out an active business that goes beyond the level of pure asset management (holding activities, group financing, etc.),
- has own employees and
- office space at its disposal (substance requirements).

Provided the requirements are not met, Austrian Withholding Tax (WHT) has to be deducted and the refund method applies. In that procedure the foreign company has to prove that its interposition in the structure is not abusive. Further, the lack of substance can result in the non-deductibility of certain expenses (e.g. if the company which receives interest payments has no substance and the actual beneficial owner is an affiliated company which is located in a low-tax jurisdiction). Finally, it should be mentioned that there is also a general substance-over-form provision in the Austrian Fiscal Code, which shall avoid tax abuse.

Substance requirements are more and more challenged by the Austrian tax authority. Therefore, it should be ensured that these requirements are met.

Controlled Foreign Corporation (CFC)

For financial years beginning after December 31st 2018 CFC rules apply if
- a (directly or indirectly) controlled foreign company (i.e., voting rights of more than 50%) without significant business activities;
- earns mainly (i.e., more than one third) passive income (e.g., interest, royalties, dividends, etc.) and
- is subject to low taxation (i.e., effective income tax rate of 12.5% or lower) in an EU member state or a third country.

Consequently, the passive income items of the CFC company will be (proportionately) added to the Austrian taxable base of the controlling Austrian company.

To mitigate any negative consequences due to the new CFC rules we recommend to review the structure of existing groups and to evaluate whether there are any possibilities for tax optimisations.

Transfer pricing

Generally, all business transactions between affiliated companies must be carried out under consideration of the arm's length principle. In case that a legal transaction is deemed not to correspond with the arm's length principle, or if the appropriate documentation cannot be provided, the transaction price would be adjusted for tax purposes. Additionally, the adjustment may trigger interest payments and fines.

Further, Austria implemented mandatory transfer pricing documentation requirements as defined in Action 13 of the OECD's Action Plan on Base Erosion and Profit Shifting.

The mandatory transfer pricing documentation requirements follow a three-tiered documentation approach, requiring the preparation of a Master File, a Local File, and a Country-by-Country Report (CbCR). The entire documentation is to be prepared in either German or English.

Austrian companies with a turnover above €50m in the two preceding fiscal years are subject to transfer pricing documentation requirements under the Master File/Local File concept. In case the consolidated group revenue of a multinational enterprise (MNE) group amounted to at least €750m in the preceding fiscal year, the ultimate parent entity, if resident in Austria, is obligated to file a CbCR with the Austrian tax authorities.

An Austrian business unit (i.e., basically legal entities or Permanent Establishments [PEs] preparing financial statements) of a qualifying foreign MNE may take over its parent's duty to report in case the ultimate parent entity is not obligated to file a CbCR in its jurisdiction of tax residence or in case no (functioning) qualifying competent authority agreement is in place with the tax jurisdiction of the ultimate parent entity that provides a basis for the exchange of the CbCR.

The arm's length principle should be duly followed and documented in order to avoid negative tax consequences. Further, the mandatory transfer pricing documentation requirements have to be considered.

Thin capitalisation rules

Under Austrian law, interest payments on senior and shareholder loans are generally tax deductible. There are no explicit thin capitalisation rules. Generally, group financing has to comply with the general arm's length requirements. A debt/equity ratio of 3/1 is usually accepted by Austrian tax auditors.

Payments made to related parties located in low-tax jurisdictions are no longer tax deductible. The restriction applies in case the respective interest income is not taxed or subject to a nominal or effective tax rate of less than 10%. The low-taxation test has to be passed at the level of the beneficial owner of the income.

An Austrian group entity being financed by an affiliated entity must be able to document that the financing structure is in line with the arm's length principle. The affiliated financing entity must not be situated in low-tax jurisdictions.

Real estate transfer tax (RETT)

Austrian RETT of 3.5% on the compensation is generally payable upon the transfer of Austrian real estate.

Also, the transfer of shares in a company owning Austrian real estate may trigger RETT in case 95% or more of the shares in the asset-owning company are transferred or finally held by the buyer. In that case, RETT amounts to 0.5% of a so-called "property value", whereby this "property value" is comparable to the market value of the property.

Furthermore, the transfer of at least 95% of the shares in a real estate owning partnership to new shareholders within a period of five years is subject to Austrian RETT.

Shares held by a trustee for tax purposes will be attributed to the trustor and are therefore part of the calculation of the shareholding limit.

RETT is generally triggered on transactions that cause a change in the ownership of Austrian real estate or in the person empowered to dispose of such property. RETT in the amount of 0.5% of the property value is also triggered in situations where the shares of corporations or interest in partnerships owning Austrian real estate are transferred.

Land registration fee

The fee for the registration of real estate and transactions within the land register has to be calculated on the basis of the purchase price of the real estate. The fee amounts to 1.1%.

Real estate transactions within the family or due to reorganisations enjoy tax privileges. The registration fee is calculated based on three times of a special tax assessed value. The tax base is limited to 30% of the market value of the real estate.

Capital gains on the sale of property

Capital gains deriving from the disposal of privately owned real estate properties and business properties of individuals, which were acquired after March 31st 2002 are taxed at a rate of 30%. The tax assessment base is the profit calculated by sales price less acquisition costs.

Real estate property acquired before March 31st 2002 is effectively taxed at
- 18% of the sales price, if the real estate property was rededicated from green area to building area after December 31st 1987 and
- 4.2% of the sales price without rededication after this date.

Losses arising from the sale of private real estate can be compensated with gains from other private real estate sales upon application. Further, 60% of the remaining losses can be offset with income from letting private property over a period of 15 years or in the same year (application necessary).

Basically, the above-mentioned tax regime for the sale of private property is also applicable for business property held by individuals. However, the transition rules are only applicable for land (and not for buildings).

Losses arising from the sale of business real estate can be compensated with gains from other business real estate sales. With regard to business property, 60% of the losses can be offset against other income and an overhang is added to the loss carry forwards.

The special tax regime is not applicable for corporations since all their profits (including capital gains resulting from the sale of real estate) are taxed with the standard CIT rate of 25%.

Gains from the sale of private property are subject to income tax with a special tax rate of 30%.

Transfer of hidden reserves realised from capital gains on the sale of property

Capital gains realised from the sale of real estate property that was held for at least seven years (in certain circumstances 15 years) as business property by individuals (not corporate investors) are not taxed under the condition, that such gains are used to reduce the book value of fixed assets purchased or manufactured within the financial year of the sale.

The transfer of the hidden reserves is only available in cases where the replacement asset is used within a domestic permanent establishment.

The valuation basis of land may only be reduced by hidden reserves from the sale of land. The valuation basis of buildings may be reduced by hidden reserves from the sale of buildings or land. In case the hidden reserves are not transferred within the financial year of the sale, they can be used to form a tax-free reserve. If this tax-free reserve is not used within a 12-month period (or 24 months under certain circumstances), it is assigned to taxable income.

A potential transfer of hidden reserves should be reviewed to avoid immediate taxation.

Interest limitation rule

Article 4 of the Anti-Tax Avoidance Directive (ATAD) requires the EU member states to introduce interest limitation rules into national tax law. The ATAD interest cap allows deduction of interest expenses only to the amount of interest income and, in addition, only up to 30% of the EBITDA. The rule is subject to a number of optional provisions.

The EU required implementation into national law until December 31st 2018. Only member states with national targeted rules that are equally effective to the ATAD rule may delay the implementation until January 1st 2024. The Austrian Ministry of Finance assumed that the existing national targeted rules fulfill this requirement. However, the European Commission did not agree on this assumption and explained in December 2018 that Austria has to apply the rules until year end 2018.

Since Austria did not implement the required interest limitation rule up to now the EC has started an infringement procedure against Austria in July 2019. Currently it is not foreseeable when and to which extent the rule is implemented in Austrian tax law.

Further developments regarding the implementation of the interest limitation rule should be observed.

2 Belgium

Corporate tax rate

As of January 1st 2018, the corporate tax rate has been decreased to 29.58% (nominal rate of 29%, increased by a 2%-crisis tax). As of financial year 2020, the nominal rate will be decreased to 25% and the crisis tax will be abolished. Small and medium-sized enterprises (SMEs) will see a decrease in the rate to 20% as from 2018 for the first bracket of €100,000 in profit.

Advance tax payments

Unless a company pays its Belgian corporate income taxes by means of timely tax prepayments (key dates April 10th; July 10th; October 10th; December 20th [dates applicable for assessment year 2020 if accounting year equals calendar year]), a surcharge on the final corporate tax amount will be due (6.75% for assessment year 2019 and 2020).

If tax prepayments are made, a credit ('bonification') will be granted which can be deducted from the global surcharge. The credit depends on the period in which the prepayment was made.

The company should verify whether any tax prepayments should be performed in order to avoid a possible tax surcharge.

Provisions for risks and charges

Provisions for risks and charges are in principle to be considered as taxable. Provisions for risks and charges can however be tax-exempt under certain conditions. The most important conditions are summarised as follows:
- The provisions are recorded in order to cover a loss that is considered likely due to the course of events;
- The charges for which a provision is established must be deductible as business charges;
- The provision must be included in one or more separate accounts on the balance sheet.

Specific attention should be paid to provisions for major repairs. These provisions can only be tax-exempt to the extent that the following conditions are met:
- The repairs must be manifestly necessary at least every ten years;
- The repairs must be major;
- Any renewal is excluded.

As of assessment year 2019, the following additional conditions need to be met to consider provisions for risks and charges as tax deductible:
- They correspond to an existing and known obligation at year-end closing;
- They result from any contractual, legal or regulatory obligation (other than those resulting merely from the application of the law on accounting rules and annual accounts). This change does not apply to existing provisions created before assessment year 2019.

By the year end, the company should book all necessary provisions for risks and charges relating to the assessment year.

Pre-paid costs

Pre-paid costs have to be deducted in the year of payment in the proportion of the part of the charge that relates to this accounting year (application of the accounting matching principle). It is then no longer possible to shift costs that will only be made in the future to the current year in order to reduce the tax charge on the current-year profits.

The fiscal regime for pre-paid costs now follows the accounting regime (i.e. matching principle).

Notional interest deduction (NID)

Deduction of interest expenses

Belgian companies are allowed to claim a tax deduction for their cost of capital by deducting a notional (deemed) interest on equity and retained earnings. As from 2018, the equity is calculated based on the incremental equity (over a period of five years) and no longer on the total amount of the company's qualifying equity. Simplified, the incremental equity equals one-fifth of the positive difference between the equity as at the beginning of the taxable period and that as at the beginning of the fifth preceding taxable period.

Thin cap rule: 5/1 ratio

Before January 1st 2019, a debt/equity ratio of 5/1 had to be considered in relation to interest payments. Interest expenses relating to intercompany loans and/or loans granted by a company subject to low tax on interest revenue exceeding five times the sum of the taxed reserves at the beginning and the paid-up capital at the end of the assessment year (i.e. debt/equity ratio of 5/1) were considered as non-deductible for tax purposes (i.e. to be added to the disallowed expenses).

As per January 1st 2019, this ratio rule of 5/1 is replaced by the 30% EBITDA rule, as explained hereafter. However, for all loans concluded prior to June 17th 2016 the ratio of 5/1 still applies instead of the 30% EBITDA rule (grandfathering rule).

30% EBITDA rule

The new interest deductibility limitation rule applies not only to intragroup loans but also to bank loans. Indeed, the exceeding borrowing costs are computed on a net basis and they take into account payments economically equivalent to interest. Three types of loans are outside the scope of the exceeding borrowing cost computation: loans granted before June 17th 2016 without "fundamental modification" (grandfathering rule – still subject to old thin cap rule of 5/1 – see above), loans in relation to public-private co-operation projects, and loans granted between Belgian entities that are part of the same group.

Exceeding borrowing costs will be deductible up to the highest amount of 30% tax EBITDA or €3m (= de minimis/safe harbour rule – €3m to be allocated across Belgian group entities – exact guidance still to be communicated). Disallowed exceeding borrowing costs can be carried forward without time limit. The new law provides for a transfer of “deduction capacity” to another Belgian group entity (while the current law provides for a transfer of exceeding borrowing costs). This must be analysed in conjunction with the new consolidation regime (see below, under consolidation).

Companies of which the tax basis is determined by means of article 185bis Belgian Income Tax Code (BITC) (i.e. regulated real estate companies [SIR/GVV] and real estate investment funds [FIIS/GVBF]) do not fall into the scope of the 30% EBITDA rule.

Since January 1st 2019, the 30% EBITDA limitation rule is applicable in Belgium. This will need to be monitored in detail and should be kept in mind for the calculation of the financial year 2019 corporate income tax provision. Its impact should be carefully analysed together with the potential applicability of the consolidation regime (see below).

Tax consolidation

Tax consolidation was also introduced as from assessment year 2020 (i.e. years starting January 1st 2019 or later). This rule implies that Belgian companies can offset their (new) profits against tax losses of another Belgian affiliated company. Only the consolidated tax base is then subject to corporate income tax.

The scope of the consolidation regime is limited to certain qualifying companies:
- a 90% direct shareholding between the companies (or via the EEA parent company) during the entire assessment year is required, limiting the scope to the parent, subsidiary and sister companies and their Belgian permanent establishments;
- the measure is limited to group companies that have been affiliated for at least the last five successive calendar years;
- some companies such as investment companies, regulated real estate companies (SIRs/GVVs) as well as real estate investment funds (FIIS/GVBF) are excluded.

In order to benefit from this new system of tax consolidation, the group companies concerned have to conclude a “group contribution agreement” that meets certain conditions.

Tax losses carried forward

Based on current Belgian tax law, tax losses can be carried forward indefinitely as long as the company is not formally liquidated or dissolved. Under certain circumstances (e.g. change of the control not meeting legitimate or economic needs), the tax authorities are entitled to forfeit the carried-forward tax losses of the company.

As general rule, the tax authorities are entitled to challenge the carried-forward tax losses for three years as of their utilisation by the company.

As from 2018, a new order of deduction applies. Non-taxable elements, dividends received deduction of the year, patent income deduction and investment deduction (the last one, as from 2019) are fully deductible. Other tax attributes (as listed hereafter) can only be claimed on 70% of profits exceeding the €1m threshold. The remaining 30% of profits are fully taxable at the above new rate. The tax attributes concerned are the deduction of carry-forward tax losses (CF losses), carry-forward dividends-received deduction (CF DRD), carry-forward innovation income deduction (CF IID) and carry-forward notional interest deduction (CF NID) as well as the new incremental NID. The new rules do not apply to losses incurred by SMEs starters.

In the case of a change of control (including in case of an internal group restructuring), the application of the Belgian change of control rules should be carefully analysed and the need of requesting a ruling on the availability of the losses should be assessed.

Deferred taxation

The deferred taxation regime allows (provided certain conditions are met) capital gains to be taxed in proportion with the depreciation booked on the qualifying asset(s) (located in EEA member states) in which the realisation proceeds have been reinvested in due time (period of five years for buildings).

In the event that the commitment has been made to reinvest the total sale proceeds but no (full) reinvestment has taken place within the required period, the capital gain (which has not yet been taxed) will be added to the taxable income of the financial year in which the reinvestment period expires and a late payment interest (currently at a rate of 4% per year – may vary between 4% and 10% in the next financial years) will be due.

A capital gain that benefits from the deferred taxation regime and which becomes taxable after the tax reform (and thus after the application of the lower corporate tax rates, see above point 1) because of the absence of reinvestment will be taxed at the highest corporate tax rate that was applicable for the financial year during which the capital gain was realised.

When selling real estate and applying the deferred taxation regime it is important to properly monitor the time frame for reinvestment and tax formalities.

Transfer pricing

Generally, all intercompany payments have to comply with the arm's length principle. Failure to do so (incl. failure to have appropriate underlying documentation) might result in the non-deductibility of (some part of) intragroup payments.

In 2016, specific transfer pricing documentation requirements were introduced in Belgian tax law by means of the following three layers:
- Country-by-country reporting (CbCR)
- Masterfile: A global Masterfile covering information relevant to the entire group of companies;
- Local file.

The obligations for filing the Masterfile and the Local File are only applicable if at least one of the following thresholds is exceeded:
- Operational and financial revenue (excluding non-recurring revenue) of at least €50m;
- Balance sheet total of €1 billion at least;
- Annual average full-time equivalents of at least €100m.

Only Belgian ultimate parent entities of a multinational group with a gross consolidated group revenue of at least €750m should file a country-by-country report.

As from 2018, part B of the Local File – which aims at obtaining detailed information on each operating unit – must also be completed if the total amount of the cross-border intra-group transactions (part of the same unit) exceed a €1m threshold during the last (closed) accounting year.

The master file and country-by-country report should be filed no later than 12 months after the last day of the reporting period concerned of the multinational group. The local file, however, should be filed with the tax return concerned.

The arm's length principle should be duly followed and the necessary transfer pricing documentation should be complied with.

Withholding tax

Since 2017, a uniform withholding tax (WHT) rate of 30% on interest, dividends and royalties is applicable.

Some WHT reductions/exemptions are still provided for under Belgian domestic tax law, such as for dividends from the Belgian specialised real estate investment fund or Belgian regulated investment companies to non-resident investors (WHT of 0%) to the extent the income originates from foreign real estate income, interests paid to credit institutions located in the EEA or in a country with which Belgium has concluded a double taxation treaty (0%).

In the light of the corporate tax reform and as from 2018, the reimbursement of capital is deemed to derive proportionally from paid-up capital and from taxed reserves (incorporated and non-incorporated into capital) and exempted reserves incorporated into capital. The reduction of capital will be allocated to paid-up capital in the proportion of the paid-up capital in the total capital increased with certain reserves. The portion allocated to reserves is deemed to be a dividend and becomes subject to withholding tax (if applicable). Share premium distributions are submitted to the same system. Exempt reserves not incorporated into capital continue to be outside the scope of the rule. Some elements, such as (but not limited to) revaluation surpluses, provisions for liabilities and charges, and unavailable reserves, have to be withdrawn from the reserves taken into account for the coefficient calculation. A sequence of allocation has been set for situations where the amount of the paid-up capital and sums being treated as capital are insufficient.

It should be carefully analysed whether any withholding tax exemptions might apply and it is important to comply with the required formalities.

In addition and in order to benefit from a WHT exemption on dividend distributions and/or interest payments, it is now more than ever key that the receiving entity qualifies as the beneficial owner of the income. In its recent decisions, the Court of Justice of the European Union concluded that a broad interpretation of this notion should be followed (so-called 'Danish cases'). In this context, particular attention should be paid to the upper-tier structure of a Belgian company (e.g. substance, back-to-back structures, etc.) so as to avoid any successful challenging of Belgian WHT exemption.

Capital gains on shares

As from 2018, the separate 0.412% capital gains tax rate for multinational enterprises on qualifying shares has been abolished, while the conditions to benefit from the full capital gains exemption have been aligned with the conditions to benefit from the dividend received deduction. This implies the application of a minimum participation threshold of at least 10% or an acquisition value of at least €2.5m in the capital of the distributing company.

In a nutshell, in 2018 and 2019, capital gains on shares are:
- exempt provided that all the conditions are met;
- taxed at 25.5% if the one-year holding period requirement is not met;
- taxed at 29.58% if the participation condition or taxation condition is not met.

As from 2020, capital gains on shares are:
- taxed at the standard rate (25%) if one condition is not met.
- also exempted when all the conditions are met

It will be key to monitor whether all conditions to benefit from the exemption for capital gains on shares are complied with.

Anti-abuse regulation

Belgian tax law provides a general anti-abuse measure. Under this measure, a legal deed is not opposable towards the tax authorities if the tax authorities could demonstrate that there is tax abuse. For the purposes of the anti-abuse rule, "tax abuse" is defined as a transaction in which the taxpayer places himself out of the scope of this provision of Belgian tax law or a transaction that gives rise to a tax advantage provided by a provision of Belgian tax law whereby getting this tax advantage would be in violation with the purposes of this provision of Belgian tax law and whereby getting the tax advantage is the essential goal of the transaction.

In case the tax authorities uphold that a legal deed can be considered as tax abuse, it is up to the taxpayer to prove that the choice for the legal deed or the whole of legal deeds is motivated by other reasons than tax avoidance (reversal of burden of proof). In case the taxpayer could not prove this, the transaction will be subject to taxation in line with the purposes of Belgian tax law, as if the tax abuse did not take place.

The impact of the anti-abuse measure on real estate transactions (e.g. share deals, split sale structures) should be analysed on a case by case basis.

Payments to tax havens

Belgian tax-residents have to declare their direct or indirect payments made to tax havens when these payments amount to at least €100,000. This declaration is made through a specific form F275 to be annexed to the tax return. Since assessment year 2016, it is no longer required to report payments to Cyprus or Luxembourg (which were up to then also considered as tax havens).

To avoid any negative tax consequences, this reporting obligation should be carefully monitored.

Recent changes

In addition to the changes already mentioned above, the following modifications in Belgian tax law should be noted:

VAT on rent

Since January 1st 2019, the new legislation allowing VAT to be applied to rent is applicable. This regime provides the following new possibilities:
- Option to apply VAT (in a B2B context) to the rental of newly constructed or newly renovated buildings after October 1st 2018;
- Application of VAT for short-term leases (maximum six months) in a B2B context;
- Simplification of the conditions to apply VAT to the rental of (old or new) warehouses (only 50% of the building must be used for warehousing purposes).

With the new regime, the cost of investing in real estate should decrease significantly as input VAT paid on construction and operating costs would become recoverable.

Specific modalities regarding the refund of the historic input VAT have been put in place for 2019.

Multilateral Instrument (MLI)

On June 26th 2019, Belgium ratified the MLI as adopted by more than 100 jurisdictions to efficiently update their treaties network with some measures to prevent base erosion and profit shifting (e.g. one of the principal purposes of entering into the specific transaction or arrangement was not to obtain the treaty benefit concerned).

It will be implemented on October 1st 2019 while the time it enters into effect will vary depending on the double tax treaty concerned and the other country's ratification of the MLI (reciprocity).

DAC 6

In the light of EU Council Directive 2011/16 in relation to cross-border tax arrangements (known as DAC 6), specific cross-border arrangements (as carried out since June 25th 2018) are now reportable to local tax authorities.

More specifically, these arrangements need to be disclosed to the tax authorities before 31 August 2020 by intermediaries (such as PwC), individual taxpayers or corporate taxpayers. Failure to comply with this reporting obligation could result in penalties.

Ultimate Beneficial Owners (UBO) Register

According to the fourth AML Directive, all Member States need to establish a national register of Ultimate Beneficial Owners before June 26th 2017. In this respect, a centralised UBO register has been created under Belgian tax law. Registration needs to be completed before September 30th 2019 (where applicable). The Belgian tax authorities will however apply a general administrative tolerance until December 31st 2019. During this period, the tax authorities will not impose sanctions.

Anti-Hybrid Mismatch

From financial year 2019, anti-hybrid rules have been introduced within Belgian tax law in line with the Anti Tax Avoidance Directive I and II (ATAD).

These rules cover not only situations where Belgium is immediately involved in a hybrid mismatch but also imported mismatch situations. More particularly, payments made in the context of an imported hybrid mismatch are disallowed for tax purposes to the extent they (in)directly finance expenses that are deductible at the level of certain foreign taxpayers without any income corresponding to that cost being however included in the taxable income of the beneficiary (unless, of course, an equivalent adjustment is made in one of the jurisdictions involved). This measure may very well turn the spotlight on certain financing instruments being used notably in a Luxembourg context.

Belgian controlled foreign company (CFC) regime

In force as from January 1st 2019, the Belgian CFC regime implements the ATAD. It has been transposed into Belgian tax law in article 185/2 BITC. This new regime is an anti-abuse measure aiming to tax the undistributed profits earned in or through low-tax foreign subsidiaries or permanent establishments in the hands of their Belgian controlling shareholders.

To be characterised as a CFC, the BITC requires the foreign entity to fulfil the following three conditions:
- be legally or economically directly or indirectly controlled (not de facto control);
- have undistributed profits arising from artificial arrangement(s) set up with the essential purpose of obtaining a tax advantage;
- pay less than half of the corporate income taxes it would have paid if it was established in Belgium.

The above conditions consist of the transactional approach i.e. it reflects the application of the arm's length principle – and in particular with regards to the Significant People Function concept – when it comes to the assessment of the genuine character of the arrangements.

3 Bulgaria

Transfer pricing

In 2019 Bulgaria adopted rules providing for mandatory preparation of transfer pricing (TP) documentation, justifying the arm's length nature of the related party transactions.

The TP documentation shall comprise a Local file and a Group Master file (if the company is part of a multinational group). Bulgarian entities, as well as foreign entities acting through permanent establishments in Bulgaria, which participate in cross- border related party transactions will be required to prepare TP documentation, if as at December 31st of the preceding year the following thresholds are exceeded:
- balance sheet value of the assets – BGN 38m, and
- net sales – BGN 76m, or
- average number of employees – 250.

The first year for which a Local file should be available is 2020 (i.e. the documentation should be prepared by March 31st 2021). Both, the Local and the Master file would be provided to the tax authorities upon their request.

Companies should consider the new TP rules in their real estate transactions.

Thin capitalisation rules

As at January 1st 2019, Bulgarian tax legislation provides for two regimes of treatment of the interest expenses for the purposes of corporate income taxation – i) thin capitalisation regime and ii) the interest limitation rules.

In broad terms, the company should determine which of the regimes is applicable in any given year (could be none, one or both of them).

Under the Bulgarian **thin capitalisation rules**, interest expenses may not be fully tax deductible if the average between the company's debt-to-equity ratio as at January 1st and December 31st exceeds 3/1. Even if this ratio is not met, the thin capitalisation restrictions would not apply if the company has sufficient profits. Restricted interest expenses may be reversed in the following years (without time limitation), under certain conditions.

Interest costs incurred on bank loans and interest elements of finance lease payments are subject to the thin capitalisation rules, not only when the bank loan agreements and the finance lease agreements are concluded between related parties but also when the finance lease/the loan is guaranteed by a related party.

The **interest limitation regime** is triggered when the net borrowing incurred during the year are above €3m. The excess of the company's borrowing costs over its interest income (i.e., net borrowing costs), is tax deductible in the year when incurred, only up to 30% of its tax-adjusted EBITDA.

Borrowing costs are defined very broadly and cover various costs (i.e. interest under bank loans, interest capitalised in the value of a non-depreciable asset or the amortisation of capitalised interest in a depreciable asset, etc.)

The non-deductible excess of borrowing costs from one year can be carried forward and deducted without time limitation. There is no debt-equity ratio safe harbour rule in respect of the interest limitation rules.

Withholding tax

Bulgarian withholding tax (WHT) applies to certain types of income (e.g., interest, royalties, consultancy services, etc.) accrued in favour of a foreign tax resident.

Beneficial ownership

A special definition of beneficial owner for the purposes of obtaining withholding tax relief exists in the Bulgarian tax legislation. Generally, a foreign entity is considered the beneficial owner of income if it has the right to freely dispose about the income and bears the full or a significant part of the risk related to the activity and is not a conduit company.

In view of the increasing focus by the Bulgarian tax authorities on tax relief entitlement, companies should be in a position to prove, in case of a tax audit, that the income recipients were the beneficial owners of the received income, that they have adequate substance, they are not part of a conduit arrangement or non-genuine/tax-driven structures, etc. This is also in light of some recent tax developments with two judgments of the European Court of Justice from February 2019, that stress on the beneficial ownership concept when applying EU WHT exemptions on interest and dividends (Judgment from February 26th 2019 in Joined Cases C-115/16, C-118/16, C-119/16 and C-299/16, and Judgment from February 26th 2019 in Joined Cases C-116/16 and C-117/16).

Suppliers in offshore jurisdictions

There is a 10% Bulgarian withholding tax on income from services, rights, indemnities and penalties, which is accrued to certain persons in offshore jurisdiction.

Real estate tax

Real estate is subject to annual real estate tax at a rate between 0.01% and 0.45% depending on the municipality where the property is located. The tax base is the higher between the gross book value of the property as per the company’s balance sheet and the tax value as determined by the municipality where the real estate is located. In the case of a change in the circumstances applicable to the tax rate the taxpayer should declare this change in the relevant municipality. The period for declaring the change is two months.

Garbage collection fee

Companies are obliged to pay garbage collection fees with respect to their real estate. Generally, the fees are based on the gross book value of the real estate properties and could be material for expensive real estate.

It is expected that as of January 1st 2022, new rules for the calculation of the garbage collection fees will come into force. Under these rules the amount of the fee due should be determined in accordance with the actual volume of the garbage. However, the exact methodology of fee calculation is still under discussion.

Value added tax

The transfer of ownership over land and the renting out of land is generally VAT-exempt. However, the transfer of regulated land plots in Bulgaria (i.e. land that is eligible to be built upon) is a supply subject to 20% VAT.

The disposal of buildings (and the underlying area plus an adjacent area with three metre width) for which more than five years have passed from the date of issuance of the permit for their use (so-called 'old buildings') is VAT-exempt. The sale of "new" buildings (and the underlying area plus an adjacent area with three metre width) or units in them is always subject to VAT.

The rent of buildings is a VAT-able supply, except when rented out to individuals for residential purposes.

Where the above supplies are VAT-exempt, there is an option for the supplier to treat them as subject to VAT.

The sale of construction rights over land is VAT-exempt until the issuance of construction permit.

If a company uses a building partly for the provision of taxable supplies, and partly for provision of exempt supplies/performance of non-taxable activity, it would be entitled to partly (pro rata) recover the input VAT incurred on the purchase/rent of the building. A change of the use of the building from taxable to exempt activities over a period of 20 years may have an impact on the right of input VAT credit, which is to be adjusted, based on a specific formula.

Real estate related services (such as those performed by consultants, architects, engineers, supervisors, intermediary brokers, etc.) are always considered with place of supply in Bulgaria and attract Bulgarian VAT when the real estate is located in the country. In case the supplier is a taxable person not established in Bulgaria, the Bulgarian VAT should be self-charged by the recipient of the above services (a taxable person) in Bulgaria under the reverse charge mechanism.

Currently, there is a draft law for amendment in the Bulgarian tax legislation, which suggests that the transfer of shares of legal entities owning real estates shall be subject to VAT. However, this draft amendment is still under discussion as neither the exact threshold of real estates ownership required for triggering application of this regime, nor method for determination of the taxable base are regulated by the draft law.

4 Cyprus

Cyprus Income Tax (CIT)

Immovable property trading gains and rental income derived from Cyprus immovable property are subject to CIT.

If the property owner is a company (whether resident or non-resident) the corporate tax rate of 12.5% applies.

If the property owner is an individual, rental income is added to his(er) other Cyprus taxable income and the following personal income tax (PIT) rates apply:

Chargeable Income for the tax year €	Tax rate (currently applying in 2019) %	Accumulated Tax €
0–19,500	0	0
19,501–28,000	20	1,700
28,001–36,300	25	3,775
36,301–60,000	30	10,885
>60,000	35	

Property running expenses incurred in deriving rental income such as insurance, repairs and maintenance, and property management fees as well as any other expenses incurred wholly and exclusively for the production of rental income are deductible if the owner of the Cyprus-situated immovable property is a company.

Individuals are not allowed to deduct such actual expenses (other than interest expenses and capital allowances), but instead can deduct a notional 20% on the gross rental income from buildings (i.e. land not included), independent of whether any actual expenses were incurred in deriving the rental income or not.

In regards to the Cyprus-situated immovable property on which rental income is earned, the deductions could additionally include any interest expense accruing on borrowings that were obtained by an individual or a company to finance the acquisition of the building.

Capital expenditures such as stamp duty and legal costs incurred in acquiring the property are not deductible, but form part of the acquisition for depreciation allowances and for costs deductible against sales proceeds realised upon potential disposal of the property.

Refer also to the *"Special contribution for defense (SDC)"* section.

Special defence contribution (SDC)

In addition to income tax (refer to *'Cyprus Income Tax'* section) SDC is imposed on gross rental income, reduced by 25%, at the rate of 3% (i.e. at an effective rate of 2.25%) earned by Cyprus tax resident companies and Cyprus tax resident-domiciled individuals.

For Cyprus sourced rental income where the tenant is a Cyprus company, partnership, the state or local authority SDC on rental income is withheld at source and is payable at the end of the month following the month in which it was withheld.

In all other cases, the SDC on rental income is payable by the landlord in two six monthly intervals on June 30th and December 31st each year.

Payment of tax

Corporate property owners must pay the Cyprus Tax liability arising on rental income in two equal provisional instalments by self-assessment due by July 31st and December 31st. The first instalment may be revisited upwards until December 31st. A final balancing payment must be made on or before August 1st of the following year by self-assessment to bring the total payments of tax to the total actually due according to the tax return.

Corporate property owners also pay SDC arising on rental income in two equal instalments by self-assessment due by June 30th and December 31st. Corporate property tenants must withhold SDC from rental payments on a monthly basis and pay SDC to the authorities by next month.

Individual property owners that earn rental income must pay personal income tax annually by self-assessment due by June 3oth of the following year. Individual property owners must also pay SDC in two equal instalments by self-assessment due by June 30th and December 31st.

Tax return for 2018

Corporate property owners should be registered online and submit their annual tax returns electronically. The submission deadline of the 2018 corporate tax return is March 31st 2020.

Individuals (without obligation to prepare accounts as per the law) must submit their annual tax return by July 31st of the following year.

Deemed dividend distribution (DDD) for 2017

A Cyprus tax resident company is deemed to distribute 70% of its accounting profits of 2017 two years from the end of the tax year in which the profits were generated (i.e. by December 31st 2019), otherwise it will be subject to the deemed dividend distribution (DDD) provisions of Special Defence Contribution at 17%, and pay the relevant SDC by January 31st 2020.

However, it should also be noted that a Cyprus tax resident entity ultimately held beneficially by 100% non-Cyprus tax resident (or Cyprus tax resident but non-Cyprus domiciled) shareholders will not come under the scope of the DDD provisions.

Capital gains on sale of property

Unless the seller is considered to be a trader in real estate (in which case CIT would apply, refer to ‘Cyprus Income Tax’ section), any gains realised upon disposal of immovable property situated in Cyprus will be subject to Capital Gains Tax (CGT).

Having said that, subject to certain conditions, land as well as land with buildings acquired at market value (excluding exchanges, donations, and foreclosures) from unrelated parties in the period of July 16th 2015 up to December 31st 2016 will be exempted from CGT upon their future disposal.

Disposal for the purposes of CGT specifically includes sale, exchange, lease, gift, abandoning use of right, granting of right to purchase, and any sums received upon cancellation of disposals.

Certain disposals of Cyprus-situated immovable property are not subject to CGT, for example, gifts from parent to child or between husband and wife or between up to third degree relatives, gifts to charities, expropriations, donations to a political party etc. (non-exhaustive list).

CGT at the rate of 20% is imposed (when the disposal is not subject to income tax) on gains arising from the disposal of immovable property situated in Cyprus including gains from the disposal of shares in companies that directly own Cyprus-situated immovable property. CGT is also imposed on disposals of shares in companies that indirectly own immovable property situated in Cyprus where at least 50% of the market value of the said shares derives from Cyprus-situated immovable property.

Disposal of shares listed on any recognised stock exchange are exempted from CGT.

In the case of disposal of non-listed company shares, the gain is calculated exclusively on the basis of the gain relating to Cyprus-situated immovable property. The value of the immovable property will be its market value at the time the shares were disposed of.

The taxable gain is generally calculated as the difference between both the disposal proceeds and the original cost of the property plus any improvements as adjusted for inflation up to the date of disposal on the basis of the consumer price index in Cyprus. In the case of property acquired before January 1st 1980, the original cost is deemed to be the value of the property as at January 1st 1980 on the basis of the general valuation conducted by the Land Registry Office under the Immovable Property Law.

Other expenses that relate to the acquisition and disposal of immovable property are also deducted from the gain, subject to certain conditions (e.g. interest expenses on related loans, transfer fees, legal costs).

The following lifetime exemptions are available to individuals:

Capital gain arising from:	Deduction €
Disposal of private principal residence (subject to certain conditions)	85,430
Disposal of agricultural land by a famer	25,629
Any other disposal	17,086

The above exemptions are lifetime exemptions subject to an overall lifetime maximum of €85,430.

Depreciation allowances

Annual tax depreciation allowance on capital costs is available both to the individual and the corporate investors at the rate of 3% for commercial buildings, and 4% for industrial, agricultural, and hotel buildings.

In the case of industrial and hotel buildings that are acquired during the tax years 2012 and 2018 (inclusive), an accelerated tax depreciation at the rate of 7% per annum applies.

Buildings for agricultural and livestock production acquired during the tax years 2017–2018 (inclusive) are eligible for accelerated tax depreciation at the rate of 7% per annum.

These rates are amended accordingly in the case of second-hand buildings.

Upon disposal of the Cyprus-situated immovable property, a tax balancing allowance/charge is calculated on the difference between sale proceeds and the tax written down value. However, the maximum taxable profit which may be taxed under income tax resulting from a balancing addition is the total tax depreciation allowances previously claimed during the period of ownership.

Individuals who have been claiming tax depreciation allowances on Cyprus-situated immovable property from which rental income derived are not subject to the balancing allowance/charge provisions upon disposal. Further, balancing statements are not required in cases of tax-qualified company reorganisations.

Finally, land does not attract tax depreciation allowances.

Tax losses carried forward and surrender of losses in the same tax year

Any trading tax loss incurred during a tax year and which cannot be set off against other income, is carried forward subject to conditions and set off against the profits of the next five years. In addition, for corporate owners of the Cyprus-situated immovable property, provisions of group loss relief apply.

Group relief (set-off of the income tax loss of one company with the taxable profit of another) is also allowed between Cyprus tax resident companies of a group. A group is defined as:
- one Cyprus tax resident company holding directly or indirectly at least 75% of the voting shares of another Cyprus tax resident company, or
- both Cyprus tax resident companies are at least 75% (voting shares) held, directly or indirectly, by a third company.

As from January 1st 2015 interposition of a non-Cyprus tax resident company(ies) will not affect the eligibility for group relief as long as such company(ies) is/are tax resident(s) of either an EU country or a country with which Cyprus has a double tax treaty or an exchange of information agreement (bilateral or multilateral). Also as from January 1st 2015, under conditions, an EU group company loss may be surrendered to a Cyprus company, under conditions.

Capital tax losses may also be carried forward and set off against future capital gains tax profits without time restriction (but not group relieved).

Dividends and withholding tax

No withholding tax is imposed on dividend payments to investors – both individuals and companies – who are non-residents of Cyprus in accordance with the Cyprus domestic tax legislation, irrespective of the percentage and period of holding of the participating shares. Additionally, no withholding tax will apply in case the recipient of the dividend is an individual who is Cyprus tax resident but not Cyprus domiciled – applicable as from July 16th 2015.

No double tax treaty protection is needed for payment of dividends from Cyprus to non-residents of Cyprus.

Stamp Duty

The general rule is that Cyprus stamp duty is imposed only on written instruments relating to assets located in Cyprus or relating to matters or things that are done or executed in Cyprus. Unless otherwise stipulated in the sale-purchase agreement, the purchaser is liable for the payment of stamp duty. The applicable rates are based on the value stipulated in each instrument and are nil for values up to €5,000, 0.15% for values from €5,001 up to €170,000, and 0.2% for values above €170,000, subject to an overall maximum amount of stamp duty of €20,000. Exemption from stamp duty applies in the case of a qualifying reorganisation.

Transfer Fees and mortgage fees

The fees charged by the Department of Land and Surveys to the acquirer for transfers of Cyprus-situated immovable property are as follows:

Market Value €	Rate %	Fee €	Accumulated Fee €
<85,000	3	2,550	2,550
85,001–170,000	5	4,250	6,800
>170,000	8		

It is important to note that, no transfer fees will be payable if VAT is applicable upon purchasing the immovable property, and the above transfer fees are reduced by 50% in case the purchase of immovable property is not subject to VAT.

Mortgage registration fees are 1% of the current market value.

In the case of companies' qualifying reorganisations, transfers of immovable property are not subject to transfer fees and mortgage registration fees.

Municipality levy

Subject to certain exemptions property owners are liable to pay Municipality Levy on immovable property which is set at a rate 1.5‰ on the assessed value of the property (this rate applies to all municipalities).

Programmes of Naturalisation and Permanent Residence

Cyprus offers two programmes for foreign investors that are interested in either relocating in Cyprus or in becoming active in Cyprus and the EU. The two programmes are the Cyprus Investment Programme and the programme for obtaining Permanent Residence Category F 6.2 through an expedited process.

Cyprus Investment Programme

Under the Cyprus Investment Programme, an investor and his(er) family (i.e. spouse, underage children, qualifying adult dependent children, and investor's parents) can apply for Cyprus citizenship under criteria. Investment amount varies depending on the economic criteria minimum €2m–€3m plus VAT. Economic criteria consists of Investment in Real Estate, Cyprus Companies/Business, Alternative Investment Funds and combination of the above. Upon approval of the application, the applicant must contribute €75,000 to Cyprus Land Development Corporation and €75,000 to the Cyprus Research and Innovation Foundation (certain exemptions apply).

A residential property of €500,000 must be kept for life and the investment as per the economic criteria above must be held for minimum five years from the date of Naturalisation. Adult applicants must hold a Permanent Residence Permit for six months prior of naturalisation and meet certain other terms and conditions.

Permanent Residence Category F 6.2

Non-EU citizens, who purchase new property in Cyprus of a cost exceeding €300,000 plus VAT, are entitled to apply and receive an Immigration Permit (Permanent Residence) through an expedited process. The investment in property/ies could be in two residential units, or one residential and one commercial property, subject to certain conditions.

This Permit grants its holders the right to travel to and reside in Cyprus for life. The Permit is extended to the applicant's spouse, under age children, adult dependent children up to 25 years and parents/in-laws of the investor. The holders need a Schengen visa to travel to EU.

Value Added Tax (VAT) on immovable property

The supply of new buildings (before their first use as well as the land on which they are built) is subject to VAT at the standard rate of 19%.

The supply of second-hand buildings (after their first use) is exempt from VAT.

VAT is imposed on leasing of immovable property (land and commercial buildings, other than residential buildings) when used by the lessee in making taxable supplies and the lessee engages in taxable activities of at least 90% of its turnover. The lessor has the right to opt not to impose VAT on the specific property. The option is irrevocable. This applies as of November 13th 2017.

VAT is imposed on the sale of non-developed building land, which is defined as land intended for the construction of one or more structures in the course of carrying out a business activity. No VAT is imposed on the purchase or sale of land located in a livestock zone or areas that are not intended for development, such as environmental protection, archaeological, and agricultural zone/areas. This applies as of January 2nd 2018.

Reverse charge provisions apply on transactions relating to transfers of immovable property during the process of loan restructuring and for compulsory transfer to the lender. This applies as of January 2nd 2018.

The long-term leasing of immovable property is regarded as supply of goods for VAT purposes as of January 1st 2019 and is subject to VAT at the standard rate of 19%.

Real Estate investors, landlords and end-users should assess the impact of the above provisions on their existing lease arrangements as well as future plans.

VAT exemptions in respect of letting of immovable property

The letting of immovable property exempt from VAT for residential purposes.

Imposition of the reduced rate of 5% on the acquisition and/or construction of residences (including land purchases) for use as the primary and permanent place of residence

The reduced rate of 5% applies to contracts for acquisition and/or construction of residences to be used as the primary and permanent place of residence for the next 10 years.

The reduced rate of VAT of 5% applies on the first 200 square meters whereas for the remaining square meters as determined based on the building coefficient, the standard VAT rate is imposed.

The reduced rate is imposed, under certain conditions, only after obtaining a certified confirmation from the Commissioner of Taxation.

As from June 22nd 2012, under certain conditions, eligible persons include residents of non EU Member States, provided that the residence will be used as their primary and permanent place of residence in the Republic.

A person who ceases to use the residence as his primary and permanent place of residence before the lapse of the 10 year period must notify the Commissioner of Taxation, within thirty days of ceasing to use the residence, and pay the difference resulting from the application of the reduced and the standard rate of VAT attributable to the remaining period of 10 years for which the property will not be used as the main and primary place of residence.

In addition, under certain conditions, persons who have already acquired a residence on which the reduced VAT rate was imposed, can re-apply and acquire a new residence on which the reduced VAT rate will be imposed, irrespective of whether the 10 year prohibition period for using the residence has lapsed or not.

Moreover, the VAT rate on acquisition of building land for the purpose of constructing the primary and permanent residence can be reduced, under conditions, from 19% to 5% in the form of a refund.

VAT Regulations – Compliance

VAT Registration:

VAT Registration is compulsory for businesses with:

a. turnover subject to VAT in excess of €15,600 during the 12 preceding months, or
b. expected turnover subject to VAT in excess of €15,600 within the next 30 days.

Businesses with turnover of less than €15,600 or with supplies that are outside the scope of VAT but for which the right to claim the amount of the related input VAT is granted, have the option to register on a voluntary basis.

Furthermore an obligation for VAT registration arises for businesses carrying out economic activities from the receipt of services from abroad for which an obligation to account for Cyprus VAT under the reverse charge provision exists subject to the registration threshold of €15,600 per any consecutive 12 month period.

No registration threshold exists for the provision of intra-community supplies of services and/or goods.

Exempted products and services, and disposals of items of capital nature are not taken into account for determining annual turnover for registration purposes. Registration is effected by completing the appropriate application form.

VAT declaration – payment/refund of VAT:

- VAT returns must be submitted quarterly and the payment of the VAT must be made by the 10th day of the second month that follows the month in which the tax period ends.
- VAT registered persons have the right to request for a different filing period. The approval of the Commissioner of Taxation is required.
- The Commissioner of Taxation also has the right to request from a taxable person to file his VAT returns for a different period.
- Where in a quarter input tax is higher than output tax, the difference is refunded or is transferred to the next VAT quarters.
- As from February 19th 2013 taxpayers who make a claim for VAT refund are entitled to repayment of the principal amounts together with interest in the event that the repayment is delayed for a period exceeding four months from the date of the submission of the claim.
- The grace period for the Tax Department to repay the refundable amounts is extended by four months (i.e. eight months in total) in the event that the Commissioner of Taxation is carrying out an investigation in relation to the submitted claim.

5 Czech Republic

Thin capitalisation rules

All related-party loans are subject to thin capitalisation rules. Any interest-free loans, or loans from which interest is capitalised in the acquisition costs of fixed assets, are excluded from the thin capitalisation rules.

The debt-to-equity ratio of 4/1 applies for thin capitalisation purposes thus any interest from loans granted by related parties exceeding the debt-to-equity ratio represents tax non-deductible costs. For thin capitalisation calculation purposes equity is calculated as the annual daily weighted average. The current year's profit is not included in equity for thin capitalisation calculations.

Thin capitalisation rules are also applicable for any back-to-back financing arrangements in which the provision of a loan by a third party is conditioned by a corresponding loan by a related party to the third party lender.

In April 2019 a new amendment to the Income Tax Law became effective. The amendment transposes the general rules set out in the EU Anti-Tax Avoidance Directive (ATAD) including interest stripping rule.

The new interest stripping rule was introduced on top of the currently applicable deductibility rules and apply to both related and unrelated loans. The ATAD test applies only to the interest expenses that successfully passed all other interest tax deductibility tests, such as already effective thin capitalisation rules as explained above.

Any net borrowing costs, defined as the excess of tax deductible borrowing costs over related taxable borrowing income will only be tax deductible up to 30% of a taxpayer's earnings before interest, tax depreciation and amortisation (EBITDA) as defined for tax purposes, or up to CZK80m. per year (safe harbour), whichever is higher. However, any interest costs treated as tax non-deductible due to the interest stripping rule may be carried forward for an indefinite period of time and used as a deduction in the years where the threshold has not been reached. However, any interest carried forward under the ATAD rules cannot be utilised by a legal successor.

Please note that the borrowing costs subject to the ATAD limitation rules comprise not just expensed interest costs but, among others, also capitalised interest and foreign exchange differences arising from financing.

Reserve on repairs of fixed assets

Reserves for repairs of fixed assets are tax-deductible only if created in accordance with the Czech Act on Reserves and the corresponding cash amount is deposited in a special escrow bank account.

A company should ensure that the value of the reserve is deposited in the special bank account at latest by the deadline for filing of its corporate income tax return.

Tax losses carried forward

Tax losses can be carried forward for utilisation up to five years after they were incurred.

Where a company is not able to effectively utilise tax losses, it is generally possible to suspend tax depreciation of certain tangible fixed assets in order to increase the tax base of the company for the corporate income tax purposes and utilise the tax losses carried forward that would otherwise expire.

Tax basis of a new real estate built in place of a building that was demolished in the course of construction

As of January 1st 2017, the tax residual value of a demolished building enters the tax basis of the new real estate, if demolished as part of the construction works. So far, it was the accounting residual value that entered the tax basis.

Companies should be aware of the above mentioned potential change to the ITA that is in force from January 1st 2017.

Hedge accounting

The use of hedge accounting is based on natural hedges which exist between euro-denominated (or other foreign currency) rental income and financing to defer recognition of any unrealised foreign exchange differences for Czech tax purposes until their actual realisation. Hedge accounting requires that a hedge accounting policy and model is implemented which complies with the requirement of the Czech GAAP.

The company should review the effectiveness of its hedge accounting model.

New notification obligation

The amendment to the ITA includes introduction of the new notification obligation applies on tax remitter payments from the Czech source income that is generally subject to withholding tax (WHT) but is WHT exempt or not subject to taxation in the Czech Republic based on the applicable Double Tax Treaty, and when this income is being paid to a Czech tax non-resident, the tax remitter is obliged to announce this payment to the Czech Tax Authority.

The tax remitter is not obliged to report payment provided that the aggregate amount of the same kind of income paid out from the Czech Republic to the Czech tax non-resident does not exceed CZK100,000 in the respective calendar month. This does not apply for payments which are subject to WHT in the Czech Republic and for payments in the form of e.g. remuneration/salary of board members, statutory representatives etc. These payments have to be announced regardless the amount of income paid out to a Czech tax non-resident.

The extended notification duty applies to any income paid since April 1st 2019. Notifications should by made until the end of the month following the one in which the WHT was withheld or would be withheld if such income was WHT exempt or would not subject to WHT in the Czech Republic.

Potential VAT claw – back

If a VAT registered company purchases a building for entrepreneurial activities then, in principle, the input VAT charged on the purchase should be fully recoverable.

However, if the building is used solely for activities generating VAT exempt supplies, then the company is not entitled to recover the input VAT at all.

If the building is used for activities generating both VAT-able and VAT exempt supplies, the company is entitled to partially recover the input VAT, in line with the proportion of i) VAT-able and ii) VAT-able and VAT exempt supplies.

A change in the use of the building (e.g. from VAT-able to exempt activities, or vice-versa) within the period of ten years following the purchase of the building may have an impact on the input VAT claimed. In certain situations this may imply that part of the claimed input VAT has to be paid back.

The above VAT refund adjustment applies also to repair/maintenance costs associated with real estate assets exceeding CZK200,000.

At year-end the company should evaluate whether the use of its buildings have changed, in terms of what supplies (VAT-able or VAT exempt) the buildings generate and in this regard, assess a potential claw-back of input VAT already refunded on the purchase of the buildings.

Liability of the recipient of the supply for VAT unpaid by the supplier

As a way of fighting tax evasion, the Czech VAT Act has introduced a concept of a so called “unreliable VAT payer”. Unreliable VAT payers are considered payers that, according to the tax authorities, do not comply with their tax related obligations.

Among other cases, the recipient of the supply is liable for any VAT unpaid by the supplier where:
- The supplier is known to be an unreliable VAT payer, or
- The recipient makes a payment to a bank account other than one which is publicly disclosed. This applies only in cases where the consideration for the supply exceeds the amount of CZK540,000, or
- The payment is made on bank account held by a bank not seated in the Czech Republic.

The database of unreliable VAT payers is publicly accessible. Bank account numbers of VAT payers are publicly disclosed in the VAT payers register.

6 Denmark

Corporate income tax (CIT)

Standard Corporate Income Tax rate (CIT) is 22% for corporate entities, which are either 1) incorporated in Denmark, or 2) has their effective place of management in Denmark. The actual place of management is typically the place where the management decisions concerning the company's day-to-day operations are made.

The corporate income tax applies to all types of income, including rental income.

Furthermore, foreign companies are subject to Danish corporate tax on certain types of income, e.g. rental income and profit from sale of real estate, if the income originates from Danish real estate. If the foreign company has a Danish permanent establishment, all income which is attributable to the permanent establishment will be subject to Danish corporate tax.

Generally, the taxable period for corporate income tax is the calendar year. The tax return has to be filed before June 30th of the next taxable period. Please be advised, that if the company has a staggered income year, i.e. an income year which ends/begins on different dates, the filing deadlines differs. Ordinary tax on account is payable twice a year in equally large amounts. The company may increase or decrease the instalments (optional third tax on account installment). The instalments are calculated to be 50% of the company's average corporation tax of the past three years. Payment deadlines for optional tax on account are March 20th for the first instalment, November 20th for the second and February 1st the following year for the third.

Permanent establishment

Non-resident companies are liable to tax in Denmark on business profits derived through a PE in Denmark. The existence of a PE is determined according to Danish case law, which makes either a reference to a specific DTT or to text similar to Article 5 of the Organisation for Economic Co-operation and Development (OECD) Model Convention.

Danish real estate may constitute a permanent establishment for the foreign company, if the company has other significant activity in Denmark. However, as mentioned above, foreign companies are subject to limited tax liability on income from Danish real estate, including rental income and profits from the sale of the Danish real estate, even though the company in question does not have a permanent establishment in Denmark.

Danish tax consolidation

Mandatory Danish tax consolidation

A mandatory tax consolidation regime obligates all Danish resident companies, branches and permanent establishments (including Danish real estate) that are members of the same Danish or international group to file a joint group tax return. The definition of a group generally corresponds with the definition of a group for accounting purposes, i.e. controlling interest. The tax consolidated income is equal to the sum of the taxable income of each individual Danish company, Danish branches and Danish permanent establishments (including Danish real estate) of foreign companies that are a member of the consolidated group.

The top parent company participating in the Danish tax consolidation group will be appointed the role of a so-called “management company”; this company is responsible for settling tax on account and final corporate tax payments of all group members.

Companies included in a mandatory tax consolidation are jointly and severally liable for payment of corporate taxes. Withholding taxes on dividends, interest, and royalty payments are also covered by the joint and several liability. For companies with external minority shareholders, the company has a reduced liability and is merely liable if none of the other jointly taxed companies are able to pay the taxes.

Repatriation of dividend

Dividends distributed from a Danish company to a foreign group company are as a main rule subject to Danish withholding tax. However, the foreign group company should be tax exempt on dividends from the Danish company if the foreign group company 1) is a tax resident in an EU-member state or a state with which Denmark has a double tax treaty, 2) holds at least 10% of the share capital and 3) is considered the beneficial owner of the dividends.

Lack of beneficial ownership in the foreign group company could result in the company not being recognised for tax purposes with regards to dividends resulting in a withholding tax obligation for the Danish company on dividends of 27% (refund of withholding tax can be claimed down to 22%).

Beneficial ownership is decided on a transaction-based assessment and the legal presence of beneficial ownership in agreements, etc. is not enough as focus is more on the cash flow.

Payment of interest

Payments/accrual of interest are subject to Danish withholding tax, but only on controlled debt. Debt is considered “controlled” if the lender owns, directly or indirectly, more than 50% of the share capital of the Danish borrower or controls more than 50% of the voting rights. Transparent entities may also be considered to have controlling influence.

If the affiliated recipient benefits from the EU Interest and Royalty Directive or a double tax treaty no withholding tax should be levied but it is a requirement that the recipient is considered beneficial owner of the interest.

Lack of beneficial ownership in the foreign corporate shareholder could result in the receiving company not being recognised for tax purposes with regards to interests resulting in a withholding tax obligation for the Danish companies on interests (22%).

See also our previous comments on the Danish general anti avoidance rule (GAAR).

Danish general anti-avoidance provision (the GAAR)

The Danish tax Agency have since 2009 raised claims in a number of tax cases related to withholding tax on dividends paid to foreign group companies. The Danish tax Agency claims that the receiving group company is not the beneficial owners of the dividend and/or that they lack substance. However, the beneficial ownership and substance requirements are not yet fully described in Danish legislation.

Danish tax law contains a general anti-avoidance provision (a GAAR), which is based on the EU anti-avoidance directives (ATAD). The GAAR was introduced in Danish tax law with effect from January 1st 2019.

According to this provision, taxpayers should in connection with the preparation of the Danish tax return and the calculation of Danish taxes disregard arrangements or series of arrangements that have been carried out with the main aim or with one of the main aims being to gain a tax advantage, which is not in line with the purpose of the Danish tax law, and which does not reflect the reality, taking all circumstances into consideration.

If on the other hand there are business reasons for the “arrangement” and the “arrangement” reflects the economic reality, the GAAR should not be applicable.

According to the preparatory work, it is for the Danish Tax Agency to make an objective analysis of all relevant facts and circumstances when assessing whether an event or a series of events may constitute an avoidance, i.e. works against the contents or purpose of the relevant Danish tax rules. It will be up to the Danish Tax Agency to determine whether there is an arrangement with the main purpose or one of the purposes to obtain a tax advantage that acts against the contents or the purpose of the Danish tax rules.

The preparatory works do only give very little guidance regarding the exact context of the new provision.

Recent Danish cases regarding beneficial ownership

On February 26th 2019, the Court of Justice of the European Union (CJEU) issued its judgments in a number of cases regarding beneficial ownership both with regards to dividend and interest payments. Beneficial ownership is a condition for obtaining the withholding tax exemption on both interest and dividend according to the EU Parent-/Subsidiary Directive and the EU Interest/Royalty Directive.

The underlying question of the cases was whether dividend and interest payments were exempt from withholding tax, when the payments were made from a Danish company to a company resident within the EU if the payments were fully or partially passed on to an ultimate parent company resident in a third country.

The Danish companies were all owned by a parent company resident in another EU Member State (Luxembourg, Cyprus or Sweden). The EU parent companies were all directly or indirectly owned by companies resident in third countries (e.g. Bermuda or the Cayman Islands) or by private equity funds with unknown residency of the investors.

The Danish companies paid out either dividends or interest to their EU resident parent companies and claimed that such payments of dividend or interest was free of withholding tax in accordance with the EU Parent-/Subsidiary Directive or the EU Interest/Royalty Directive.

In the CJEU judgments, The CJEU provided guidance on when an arrangement constitutes abuse of rights. If the funds are passed on wholly or partially shortly after they are received, this may serve as an indication that the entity is a flow-through or conduit and this could be an indicator of abuse. It is not a requirement that there is a contractual obligation to pass on the payment. Further, an indication for abuse may be if the recipient lacks substance or has been interposed in a structure that otherwise wouldn’t be covered by the EU Interest/Royalty Directive or the EU Parent-/Subsidiary Directive.

The fact that the ultimate parent is resident in a third country, with which a tax treaty has been concluded, can neither prove nor disprove an abuse of rights.

Regarding the burden of proof, the CJEU stated that an EU Member State is obliged to prove that an arrangement is abusive, but if the authorities conclude that the recipient of the income is not the beneficial owner, they are not obliged to determine which entity is the actual beneficial owner.

It is now up to the Danish High Court to decide the final outcome of each case based on the guidance from the CJEU whether in fact the recipients are the beneficial owners and/or whether there is an abuse of rights. In the meantime, however, these judgments will be extremely important for the application of the EU Interest/Royalty Directive and the EU Parent-/Subsidiary Directive going forward and also more generally for the interpretation of terms such as "beneficial owner" or "abuse of rights".

The cases have a significant impact on most international group structures and the flow of funds from EU subsidiaries to parent companies when the ultimate parent is resident in a third country.

Sale of shares

Profit from sale of shares in Danish companies is as a general rule exempt from Danish withholding tax. This also applies to shares in companies, whose assets either exclusively or primarily consists of real estate.

Stamp duty

A real estate transfer tax of 0.6% of the sales price or the public evaluation (whichever is the highest) is liable on the transfer of title to real property situated in Denmark. The amount is rounded up to the nearest DKK100. A registration duty of DKK1,660 is charged for registration of ownership.

New mortgage loans registered in the Danish Land Register will be subject to a registration fee of 1.5% of the mortgage debt. It may be possible to reduce the 1.5% payment by replacing existing mortgages with the new mortgage loan.

Danish interest deduction limitation scheme

The Danish interest deduction limitation regime consists of three different rules; thin capitalisation limitation, an interest ceiling limitation and an EBITDA-limitation.

Thin capitalisation

If the Danish company is thinly capitalised, it will not be allowed to deduct interest payments or capital losses for tax purposes to the related lender.
But the limitation of deductions for tax purposes is only applicable if:

- The controlled debt (including secured external debt) exceeds a threshold of DKK10m, and
- The loan could not have been obtained from an independent lender without security on similar terms (the company has the burden of proof), and
- The debt/equity ratio exceeds 4/1.

Danish thin capitalisation rules apply when a Danish resident entity has a loan from a related legal entity, or a loan from an independent lender where security for the loan is given by a related legal entity (controlled debt). Debt is seen as "controlled" if the loan is given (or secured) by a legal entity that owns, directly or indirectly, more than 50% of the share capital of the Danish borrower or controls more than 50% of the voting rights. Transparent entities, like private equity funds, might be considered to have controlling influence.

Please be advised, that the thin capitalisation rule also applies to Danish permanent establishments of foreign companies. As such, if Danish real estate is owned by a Danish permanent establishment, which is subject to Danish corporate tax to all income which can be attributed to it, the thin capitalisation rule will apply to the permanent establishment. However, if the Danish real estate is owned directly by a foreign company, and as such subject to limited Danish tax liability on income from the Danish real estate, the thin capitalisation-rule does not apply.

The thin capitalisation rules do not apply to interest expenses that are subject to Danish withholding tax.

"Equity" is calculated at year-end as the fair market value of the assets (including non-booked assets, e.g. goodwill) minus debt at fair market value at year end. If the 4/1 ratio is exceeded, only interest deductions and capital losses allocated to that part of controlled debt, which should have been converted into equity to meet the 4/1 ratio are limited for tax purposes.

The interest payments are not reclassified as dividend payments.

If several Danish companies are "controlled" (i.e. more than 50% of the notional share capital or more than 50% of the voting rights are in the hands of the same group of shareholders), the 4/1 ratio might apply to these companies on a consolidated basis. Shareholdings, debt, and claims between the consolidated companies should then be eliminated.

Capital contributed to a Danish company to avoid a thin capitalisation position must be maintained in the company for at least two years.

The interest ceiling rule

Any limitation to interest deduction according to the thin capitalisation rules will be calculated first.

The interest ceiling and the EBITDA rules apply regardless of whether the interest payments are subject to Danish withholding tax or not.

It is only possible to deduct net financial expenses in a Danish jointly taxed group equal to a pre-determined percentage of the tax value of qualifying assets at year-end (interest ceiling). A base amount will always be deductible. The allowed percentage is now 2.7% (2019), which will be adjusted once a year and the base amount is DKK21.3m.

Net financial expenses consist of any negative sum of:
- interest income and interest expenses;
- taxable gains and losses on receivables, payables, loans, debt, bonds, and certain financial instruments (forwards, swaps, etc.) – not including interest and gains/losses on trade receivables; and
- Calculated interest income and expenses with regard to financially leased assets;
- taxable dividends and capital gains on shares.

Qualifying assets are:
- tax value of depreciable assets (written-down value);
- acquisition cost of non-depreciable assets;
- work in progress, stock, and net trade debtors/creditors including group trade debtor/creditors;
- tax losses carried forward;
- book value of financially leased assets;
- tax value of financially leased assets leased from a member of the jointly taxed group; and
- Assets contributed to the Danish jointly taxed group from a foreign group company only qualify if the assets stay in the Danish jointly taxed group for more than two years.

Qualifying assets specifically do not include:
- shares, receivables, payables, bonds and financial instruments (forwards, swaps, etc.);
- cash; and
- financially leased assets at lessor

Net financial expenses limited for deductibility by the interest ceiling rule can in general not be carried forward. However, restricted net capital losses can be carried forward for three years for utilisation against future gross capital gains, if any.

The EBITDA-rule

Under the EBITDA rule, the taxable income before net financing costs and depreciation and amortisation may not be reduced by more than 30% when reduced by net financing costs.

Compared with the previous EBIT rule, this means that the income to be used for the calculation of the maximum deductible net financing costs is changed so that tax depreciation and amortisation are not deducted from this income (EBITDA as compared to EBIT). There is a special provision for groups of companies, whereby it may be possible to obtain more than 30% deductibility under the EBITDA rule, provided that the net finances does not exceed DKK22,313,400 on a consolidated basis.

Transfer pricing

Danish transfer pricing rules apply to transactions between related parties (e.g. inter-group transactions), whether the transactions are made between residents or non-residents. The rules apply when a company or person directly or indirectly controls more than 50% ownership of the share capital or more than 50% of the voting power of an entity. Transactions with PEs are also considered subject to the rules, whether domestic or foreign.

A group must prepare detailed and extensive transfer pricing documentation to substantiate that intra-group transactions are conducted in accordance with the arm's-length principle if it employs 250 or more employees (calculated as the average number of full-time employees during the income year).

If the group employs less than 250 employees, it will qualify for the small business exemption if it meets either of the following criteria: i) has revenue under DKK250m, or ii) has a balance sheet sum under DKK125m.

However, an enterprise that is generally exempted for preparing transfer pricing documentation based on the above criteria must prepare transfer pricing documentation for transactions with group companies resident in countries outside the EU/European Economic Area (EEA) with which Denmark does not have a DTT.

The Danish tax Agency have in the past interpreted section 3 B of the Danish Tax Control Act to require contemporaneous preparation of documentation, i.e. the final documentation must be in place by the statutory filing date of the tax return. On January 1st 2019, the current provisions in section 3 B of the Danish Tax Control Act will be abolished and replaced by new provisions, which clearly outlines this contemporaneous requirement and is supported by recent case law.

The Danish tax Agency may request a group's transfer pricing documentation to be submitted within 60 days. The Danish tax Agency could request five years of documentation.

Depreciation

Tax depreciation need not be in conformity with book depreciation.

Land cannot be depreciated for Danish tax purposes.

As a main rule, properties used for commercial purposes can be depreciated for Danish tax purposes at a rate of up to 4% annually based on a straight-line basis. The same applies for technical installations. However, certain buildings are not depreciable for Danish tax purposes, including office buildings and o residential buildings (however, technical installations in office building can be depreciated at 4% annual).

Furthermore, if the building or installation is subject to severe deterioration due to the usage of the building or installation, so that the building will have lost its value in 25 years or less, even when calculating for ordinary maintenance, the Danish tax code allows for depreciation on straight-line basis (of the assumed life span of the building) +3%.

Furthermore, if the building or installation is subject to severe deterioration due to usage of the building, even when calculating in ordinary maintenance, so that the building/installation will have lost its value no later than 25 years after construction.

Annual depreciation allowances on properties take effect from the year the properties are constructed and used for commercial purposes.

Professional advisors' fees and loans costs

Professional advisors' fees (financial, legal and tax advisors) are non-deductible for Danish corporate tax purposes and cannot be added to the acquisition price of the Danish real estate.

Costs occurring in close connection with the establishment of a loan can be added to the principal of the loan and be deducted for Danish tax purposes in connection with the repayment of the loan.

Such tax deductible costs will, typically, comprise i) stamp duties (if any); ii) commissions etc., provided that the duration of the loan is two years or more; iii) fees for registrations in the Danish Land Register (mortgage loan); iv) fees paid to legal advisors and accountants, when such fees are directly connected with the establishment of the loan.

Commissions and similar non-recurring payments for establishment of loans can be deducted for tax purposes in the year, where the commission etc. becomes due for payment, provided that the duration of the loan is less than two years. However, such tax deductions cannot amount to more than 2.5% of the principal of the loan, where after tax deductions for exceeding commitment fees etc. are split over the remaining loan period.

Country-by-Country Report (CbCR)

Groups with a consolidated turnover of DKK5.6 billion (approximately €750m or more, based on previous year's turnover, must additionally prepare a country-by-country report. The CbCR must contain a range of information for each country in which the group operates, including revenue, profit, tax, capital structure, assets, and employees. Furthermore, the group has to identify each entity within the group and specify the entities' tax residencies and the activities of each entity.

The deadline for submission of the CbCR is 12 months after the end of the income year (i.e. for the financial year 2018, the deadline is the end of 2019). The rules apply for income years starting on January 1st 2016 or later. A Danish subsidiary, which is part of a multinational group, but is not the ultimate parent entity, will have to file the CbCR if certain requirements are met. However, this is only applicable for income years starting January 1st 2017 or later.

Additionally, Danish taxpayers must notify the Danish tax Agency about which group entity is obligated to file the CbCR. To notify the Danish tax Agency, the taxpayer must submit the notification electronically to the Danish tax Agency through the Danish digital system (TastSelv). The CbCR-notification should be submitted before the year end of the year covering the CbCR (e.g. if the CbCR will include information for the financial year ending December 31st 2019.

New Anti-hybrid legislation

The Danish Corporate Income Tax Act ('CITA') section 2C includes an anti-avoidance rule for hybrid entities. The rule stipulates, that an otherwise tax transparent Danish entity is treated as an opaque entity for Danish tax purposes, if the entity is treated as an opaque entity in another country, where the direct owner of more than 50% of the capital in the Danish entity or more than 50% of the votes is domiciled.

With effect from January 1st 2020, this rule will be amended, entailing that the scope of the rule will be broadened. After the amendment, the tax treatment of the entity by one or more foreign owners with right to more than 50% of the profit from the Danish entity can trigger the anti-hybrid rule as well (even though less than 50% of the shares/votes is held by such foreign tax payer). If the anti-avoidance rule is triggered, distribution of profit will be treated as dividend (triggering withholding tax risk).

Section 2A of CITA stipulates that if it is chosen for foreign (e.g. US) tax purposes to "check the box" with regards to a Danish A/S or ApS for transparency (disregarded entity), the Danish ApS or A/S will for Danish tax purposes also be looked at as a tax transparent entity (branch), if there is no blocker between the US and Denmark.

Section 2B of the CITA concerns hybrid financing instruments, whereby debt in a Danish corporate tax payer can be requalified into equity for Danish tax purposes, if the “debt” is considered equity in the country of the lender (or further up the structure in case of a back to back arrangement). If applicable, this rule will trigger a withholding tax risk on both the “interest” and “capital gains” on the “debt”. In our opinion good arguments support that the repayment of the principal of the loan is not comprised by the rule.

As part of the implementation of the EU anti-tax avoidance directive, “ATAD”, a new Danish hybrid mismatch rule will come into force January 1st 2020, and Sect. 2B will be repealed. This will result in a wider definition of hybrid mismatches compared with the current Danish hybrid rules. The purpose of this new legislation is to counteract double deduction and deduction without inclusion in connection with both hybrid instruments and hybrid entities.

Danish legislation further includes a double tax treaty and EU Directive override rule (not a new rule), which enables the Danish Tax Agency to deny benefits which could not have been achieved without e.g. an intermediary holding company if the relevant “arrangement” is not established for legitimate business reasons or the “arrangement” does not reflect the economic reality.

Additionally, it should be mentioned that a general anti-avoidance provision has been introduced in Danish tax law with effect from January 1st 2019. According to this provision, taxpayers should in connection with the preparation of the Danish tax return and the calculation of Danish taxes disregard arrangements or series of arrangements that have been carried out with the main aim or with one of the main aims being to gain a tax advantage, which is not in line with the purpose of the tax law, and which does not reflect the reality, taking all circumstances into consideration.

Value-added tax

Value-added tax (VAT) in Denmark is 25% on all goods and services. This includes “new” buildings/building sites, i.e. buildings/building sites which 1) has been built after 2011, or 2) has been built prior to 2011, but has undergone significant alteration or renovation after 2011. Such renovation is considered significant, if the costs exceeds 25% of the property value.

A building is considered “new” for Danish VAT purposes until it has been taken into use. However, the first sale of a building within five years after the completion will always be regarded as sale of a “new” building from a Danish VAT perspective, regardless of whether the building has been taken into use or not.

Recent case law has provided clarification on the definition of “building site” in relation to VAT. As such, a building does not constitute a building site for VAT purposes, if the parties intend to demolish the building immediately following the transaction. Instead, the assessment must be made objectively at the time of transfer. However, it is important that the seller is not responsible for the actual demolition as an integral part of the transaction.

7 Estonia

Corporate income tax rate

Estonia is regarded as offering a relatively favourable income tax regime, as all undistributed corporate profits are tax-exempt. Estonia levies a corporate income tax only on profits that are distributed as dividends, share buy-backs, capital reductions, liquidation proceeds, or deemed profit distributions. Distributed profits are generally subject to 20% corporate tax (20/80 on the net amount of the profit distribution).

As of January 1st 2018 the corporate income tax rate for companies paying regular dividends has dropped from 20% to 14% taking into account the period of three years cycle. That means that the payment of dividends in the amount which is below or equal to the amount of taxed dividends paid during the three preceding years (20%), will be taxed with a rate of 14% (the tax rate on the net amount being 14/86 instead of the regular 20/80).

In cases where the recipient of the 14% dividend is either a resident or non-resident individual, a 7% withholding tax (WHT) rate will apply unless a tax treaty provides for a lower WHT rate (5% or 0%).

Estonian companies can choose whether to distribute profits based on the regular regime where 20% corporate income tax is paid or pay out profits regularly, which allows to use reduced rate.

Sale of shares in a real estate company

Capital gains derived by non-residents from the sale of shares in Estonian companies would be subject to 20% income tax in Estonia only if the assets of the company at the time of disposal or at any time during the two-year period prior to disposal consisted directly or indirectly of more than 50% of the immovable property or buildings located in Estonia, and in which the non-resident held at least 10% participation at the time of the sale.

In case of the sale of shares of an Estonian real estate company, budget for potential 20% income tax to be paid on taxable gains.

Transfer pricing

The inter-company transactions must be in accordance with the Estonian transfer pricing regulation, which is generally based on the arm's-length principle that requires the prices charged between related parties to be equivalent to those that would have been charged between independent parties in the same or similar circumstances. Should the transfer prices applied in the inter-company transactions not follow the arm's-length principle, any hidden distribution of profits is subject to Estonian corporate tax (i.e. being subject to monthly 20/80 distribution tax). From 2011 the definition of "related persons" has been broadened and includes also persons who have common economic interests or dominant influence over other persons.

The tax authorities' focus is on transfer pricing transactions; especially on intra-group financing and services arrangements. We recommend reviewing the transfer pricing documentation in the light of that.

Land tax

Land is subject to annual land tax which is calculated on the assessed value of land at rates between 0.1% and 2.5%, depending on the municipality. The land tax is generally paid in two instalments, by March 31st and October 1st. The rate of land tax applicable in Tallinn, the capital of Estonia, is 2.5%.

Significant amendments derived from ATAD

Firstly, a new anti-tax avoidance clause is introduced, which obligates a resident company to pay income tax on a loan issued to a shareholder or a partner if the "circumstances of the transaction indicate that it might be a hidden profit distribution".

If the due date of an outbound loan exceeds 48 months, then the Ministry of Finance assumes that certain loans issued to related parties may constitute hidden profit distributions, and, once the deadline is met, the burden to prove the opposite lies with the taxpayer.

Secondly, exit tax provision comes into force in Estonia. When a resident company transfers assets from Estonia to its permanent establishment(s) in other state(s), then income tax is charged on the amount which equals to the (positive) difference between the fair market value of the transferred asset and the book value at the time of the asset transfer. A number of exceptions are also implemented.

Exemption method on dividend distribution will also be granted to dividends paid on account of assets upon the transfer of which exit tax was paid or dividends received from controlled foreign companies or from sale of shares in such companies to the extent of the amount that was taxed.

Thirdly, the Estonian CFC rules have previously applied to private individuals. These provisions will remain in force, but an additional tax object will be included. Namely, profits of a controlled foreign company will be taxed in the hands of an Estonian resident company (or a permanent establishment) if the specific criteria are met.

A controlled foreign company is defined as any nonresident enterprise in which the resident company alone or together with its related parties holds more than 50% of the voting rights or capital, or is entitled to receive more than 50% of the profits.

Significant VAT amendments

Before October 1st 2018, the sale of land was subject to VAT in case the land is a plot that has an approved zoning plan and construction rights provided there are no buildings located on the plot. Such definition of the tax object depends on the existence of a zoning plan and thus does not allow taxation of all land that are essentially considered as building land.

Thus, instead of a plot a new concept called "building land" was introduced. Building land is defined as immovable property without buildings, which according to its design specifications, zoning plan or a state or local government special spatial plan is designed for construction or for which a building notice has been submitted or for which intended use of cadastral unit is residential or business land.

After the amendment, it can be concluded that:
1. a land without buildings planned for construction works that has a civil engineering work, is subject to mandatory taxation;
2. building land is any type of unimproved building land planned for buildings (with detail plan, special spatial plan, design specifications, submitted building notice);
3. in case a land, with an intended use of commercial or residential land, is sold, this land is considered to be equal to building land and is subject to taxation.

8 Finland

New interest deduction limitation rules

The Finnish Government proposal concerning implementation of EU ATAD I directive (2016/1164) was approved in December 2018. Changes have been applicable from January 1st 2019 onwards.

Interest expenses are always deductible if the total net interest expenses do not exceed €500,000 in a tax year. If net interest expenses exceed this threshold, the limitations would be applied to the total amount and not just to the amount exceeding the threshold.

- The restrictions on interest deductibility have been expanded from interest paid by group companies and permanent establishments to apply to interest paid by "non-independent" companies and interest paid to third parties.
- The definition of related parties has been changed to "group undertakings/ companies", the definition of group undertakings remains at over 50% direct or indirect control.
- Independent companies are completely outside the scope of the restrictions, including in respect of external interest. Independent companies are defined as those where no party has a 25% influence or control stake in another party.
- The restrictions are also applied to general and limited partnerships.
- The restrictions have been extended to the sources of income taxed under the Income Tax Act (TVL) and the Farm Income Tax Act (MVL). As a result, the new restrictions are also applied to real estate companies that have in general been outside the scope of interest capping rules until now.
- The definition of interest has been widened and it includes all expenses related to obtaining financing. Therefore, the type of finance expenses subject to restrictions have been expanded from pure interest expenses.
- The restrictions are to be calculated based on adjusted taxable income and the maximum deduction allowed is 25% of the adjusted taxable income. The adjusted taxable income is described as "taxable EBITD" and is calculated as taxable income including group contributions, adding back interest expenses and tax depreciation (in practice the change in terminology from taxable EBITDA to taxable EBITD does not affect the calculation as all tax depreciation or amortisation is added back to taxable income).
- Annual interest expenses paid to unrelated parties are always deductible up to €3m (if expenses are otherwise at arm's length and related to the company's business).
- As is currently the case, a back-to-back arrangement means that a loan taken from a third party is considered a group loan. Additionally, security for a loan given by another group company in the form of a loan receivable leads to a third party loan to be considered as a group loan.
- Non-deductible financing expenses are carried forward without an expiry date and ownership changes do not effect the carry forward. In practice, the order in which interest expenses carried forward and other interest expenses are deducted will need to be carefully considered.

Exceptions:
- The financial services sector and certain public infrastructure projects (such as social housing projects) are not be in the scope of the restrictions.
- The exemption from the restrictions by comparing the equity ratio (equity divided by gross assets) of the Finnish taxpayer to the group ratio would remain. However, the balance sheet test which provides an exemption to the restrictions has been modified such that the comparable balance sheets must be prepared on the same basis (e.g. company and group balance sheet should both be calculated according to Finnish Accounting Standards or according to IFRS).

Grandfathering rules:
- Interest expenses on third party loans taken before June 17th 2016 are outside the scope of the new legislation, provided that the terms of the loan remain unchanged from June 17th 2016.
- Interest expenses on third party loans, capitalised before January 1st 2019 can be deducted after the change in restrictions.

We recommend that real estate investors analyse the impact of the new interest deduction restrictions on all existing and new investments. The rules may also impact the market practises on purchase price discounts required regarding deferred tax liabilities on share deals.

Abolishment of income sources

As of January 1st 2020, most limited liability companies, cooperatives and certain other corporations are taxed in accordance with Business Income Tax Act (BITA) (except for income derived from agriculture), regardless of whether it arises from business activities or other activities. In this respect, BITA would be applied to all corporations, excluding public bodies, religious organisations, housing companies, mutual real estate companies (MREC) and non-profit organisation, even when their activities do not meet the conditions of business activities.

A new class of asset i.e. deemed investment asset is intended to be created within the basket of business income. These deemed investment assets would be more loosely connected to the business activity than other business assets e.g. assets currently belonging to other income basket. Treatment of capital losses would depend on classification of the asset.

Coverage of group contribution regime broadens as a result of extending the scope of entities taxed in accordance with BITA. Companies within the same group taxed in accordance with the BITA can level their income by giving and receiving group contributions. The group contribution is considered deductible cost for income tax purposes of the distributing company and taxable income for income tax purposes of the recipient company.

The Finnish Tax Administration has released new guidance in July 2019, and is still in the process of updating other guidelines (for example, those regarding group contributions and corporate restructurings) as a result of the new rules.

Real estate tax rates

A real estate, which is located in Finland, is subject to real estate tax. Minimum and maximum tax rates are set by tax legislation. The owner of the real estate at the beginning of the calendar year is liable for the real estate tax.

Currently the minimum tax rate set by tax legislation is 0.93% and the maximum tax rate is 2.0%. Higher real estate tax rates are applied e.g. to power plants (maximum tax rate 3.10%) and vacant construction sites (maximum tax rate 6.0%).

The Finnish Ministry of Finance is also planning a reform to the determination of tax values for land for real estate tax purposes. One aim is to promote transparency in the tax valuation of the real estates with better publicly available information of the tax valuation basis such as information on prices in different areas and construction expenses. It is expected that the reform would be introduced as of 2022.

The tax law changes with respect to real estate tax rates should be closely followed. While the intention of the legislator does not seem to increase tax collection, the reform will impact differently on different types of properties.

Transfer pricing

Generally, all related-party payments and transactions have to comply with the arm’s length principle. This should be duly documented. During the past few years, the Finnish tax authorities have increasingly paid attention to financing transactions (e.g. interest payments).

Ensure compliance with transfer pricing rules.

Mutual Real Estate Company (MREC)

Typically, Finnish real estate is owned via mutual real estate companies. In order for the ownership structure to be tax efficient, payments between the MREC and its shareholder(s) need to be carefully planned and documented.

Payments between the MREC and its shareholder(s) need to be carefully planned and documented.

Transfer tax

A transfer tax of 4% of the sales price is payable on the transfer of real estate situated in Finland. The transfer of shares in Finnish companies (other than housing companies and real estate companies) and other domestic securities is subject to a transfer tax of 1.6%. The transfer of shares in Finnish housing companies and real estate companies is subject to a transfer tax of 2%. No transfer tax is payable if both the seller and the transferee are non-residents. Transfer tax is, however, always payable on transfers between non-residents if the transferred shares are shares in a Finnish housing or real estate company.

Transfer tax implications need to be carefully analysed before a transaction takes place. Transfer tax issues are closely investigated by the Finnish tax authorities and there are currently several ongoing disputes.

Input VAT deductions on transaction costs

Based on a new ruling of the Supreme Administrative Court, input VAT on transaction costs related to sales and purchases of real estate and shares of mutual real estate companies can be deducted (as overhead costs) if the real estate has been or will be used for VAT taxable purposes.

It should be verified whether the requirements for VAT deduction have been met.

Change of VAT-able use of premises

In case the VAT-able use of premises has changed compared to the situation when the real estate investment was taken into use, VAT included in the real estate investment might be subject to adjustment.

It should be verified whether there have been changes to the VAT-able use of real estate and determined whether the VAT deductions should be adjusted. The effect can be positive or negative, depending on whether the VAT-able use has increased or decreased.

VAT refunds from the year 2016

The entity registered for VAT in Finland is entitled to apply the input VAT of purchases to its VAT-able business within three years after the end of the calendar year during which the financial year ended.

If there are undeducted VAT in the purchases, it can be investigated whether it is possible to apply the refund before the end of the year. This relates also to any transaction costs relating to which you have not made a deduction or the deduction has been denied.

Own use of real estate management services

According to the Finnish VAT Act, real estate management services are considered to be taken into own use when the real estate owner or holder is performing services in respect of the real estate by using own employees, if the real estate is used for non-deductible purposes.

However, the holder or the owner of the real estate is not liable to pay tax, if he/she uses the real estate as a permanent home or if the wages and salary costs including social benefit costs relating to these services, during a calendar year, do not exceed the set threshold.

The threshold is €50,000. It may be relevant to make sure that the threshold of costs is observed.

Definition of a real estate from VAT point of view

The definition of a real estate, for VAT point of view changed as of January 1st 2017. The definition of a real estate is determined based on the Council Implementing Regulation (EU) No. 1042/2013. The Regulation also includes an example list of transactions identified as services connected with real estate. Services that are considered to relate to real estate are subject to VAT in the country where the real estate is located, i.e. reverse charge rules are not applicable.

The new definition has widened the scope of real estate. Thus, also the scope of investment subject to VAT adjustment right and liability is wider and should be taken into account when making the adjustment liability calculations.

9 France

List of states or territories defined as NCST

As for FY 2017, the list of NCST includes, Botswana, Brunei, Guatemala, Marshall Islands, Nauru, Niue, and, as from January 1st 2018, Panama.

As a reminder, French interest, dividends, capital gains (non real estate companies) realised by tax residents of those countries or paid in a bank account located in those countries are subject to a withholding tax of 75%. Capital gains on French real estate companies' shares realised by those tax residents are computed as follows: (sale price – purchase price – 2% of the acquisition price of the construction per year of holding). These capital gains are subject to withholding tax at the standard CIT rate.

The French list of NCSTs was amended on October 23rd 2018 to include the states and territories, other than those provided by French Government (see above), that are considered as NCSTs by the European Union, listed in Annex I of the revised EU list of NCST published on December 5th 2017 and revised on March 12th 2019. In this respect, French legislation distinguishes between (1) the states and territories included in the EU list on the ground that they facilitate the creation of extraterritorial structures or devices intended to attract benefits that do not represent real economic activity, and (2) the states and territories included in the EU list because they do not meet at least one of the other EU criteria defined by Annex V of the list, namely tax transparency, the absence of preferential tax measures that are potentially harmful or the implementation of the BEPS (Base Erosion and Profit Shifting) project.

France-Luxembourg double tax treaty

On July 2nd 2019, the Luxembourg Parliament voted to approve Bill n° 7390, ratifying four double tax treaties or protocols amending treaties. Included in this package was the ratification of the entirely new double tax treaty and accompanying protocol between Luxembourg and France (the 'DTT'), signed in March 2018.

As a reminder, on March 20th, the Luxembourg and French Governments have signed, amongst other, a new double tax treaty (DTT), together with an accompanying Protocol.

The new DTT seeks to modernise the rules applying. The new DTT is fully "post-BEPS". It implements the new approaches developed at international level during the OECD/G20 BEPS Project, now reflected in the 2017 version of the OECD Model Tax Convention, and in the Multilateral Convention to Implement Tax Treaty Related Measures (the 'MLI'), signed by both Luxembourg and France in June 2017.

More particularly, several provisions of the DTT are likely to affect many French real estate investments held from Luxembourg, notably those involving French OPCIs. Indeed, the French OPCIs should no longer benefit from the reduced WHT on dividends when more than 10% of the share capital such OPCIs is held by the Luxembourg beneficiary entity. Thus the domestic WHT of 30% (to be progressively reduced until 25% in 2022) will apply to such distributions.

In addition, the new DTT includes a general anti-abuse provision taking the form of a principal purpose test (PPT).

Hence, assuming that the exchange of the instruments of ratification between Luxembourg and France takes place during 2019 (as is now highly likely), this new DTT will largely enter into effect on January 1st 2020.

CVAE

CVAE is payable by the landlord of the property that is let and the landlord will be taxable, based on the value added derived from the rental activity. CVAE will be payable by the landlord of the property if their turnover exceeds €500,000.

The CVAE rate has a progressive rate, which will go from 0.5% for turnover of €500,000 up to 1.5% for turnover exceeding €50m.

The French Constitutional Court on May 19th 2017, ruled that the method used to determine the CVAE tax rate applicable to a French tax consolidated group of companies was unconstitutional because it created an unjustified difference in treatment between entities that were part of a French tax consolidation and those that were not.

Pursuant to the 2018 Act, the CVAE tax rate applicable to a French group of companies complying with the conditions to set up a French tax group (i.e. 95% ownership) is now based on the consolidated gross revenue recognised by the group of companies for a given year, whether or not they are effectively part of a French tax group.

The new regime applies to the CVAE due in 2018.

Decrease of the standard corporate income tax (CIT) rate

As a reminder, the standard corporate income tax rate is 31%, with a reduced rate of 28% applying, on the first €500,000 of taxable income.

The application of the standard rate of 31% for 2019 is limited to companies whose turnover is below €250m, with a 33.33% standard rate for companies with turnover of €250m or more. The rate will be progressively reduced to 25% by 2022.

The 2020 draft budget proposes to postpone, with respect to large companies only, the French corporate income tax rate reduction originally enacted as part of the 2018 French budget.

The corporate income tax reduction path for companies with an annual turnover of €250m or higher is proposed as follows:

- for fiscal years starting from January 1st 2020 to December 31st 2020, profits up to €500,000 will be subject to a corporate income tax rate of 28%. The standard corporate tax rate of 31% will be applicable on the excess;
- for fiscal years starting from January 1st 2021 to December 31st 2021, the rate on all profits will be 27.5%; and
- for fiscal years starting on or after January 1st 2022, the standard rate of corporate income tax will be 25% for all companies and all taxable income (article 11 of the Bill).

For companies with revenues not exceeding €250m, the scheduled corporate tax rate reductions would remain unchanged.

Decrease of the domestic withholding (WHT) rate on dividends

Dividends paid by a French corporation to a non-resident shareholder are subject to a 30% withholding tax, unless a tax treaty provides for a lower rate or the EU parent-subsidiary directive applies.

Under the directive, dividends paid by a French corporation to qualifying EU parent company are exempt from withholding tax.

The 30% domestic withholding tax rate will be progressively reduced to 25% in 2022, in line with the reduction in the standard corporate tax rate.

Net Wealth tax

Article 31 of the 2018 finance bill removed the wealth tax (ISF) in place in France since 1982 and replaces it with a tax on real estate property (IFI) as from January 1st 2018.

The IFI will be based on real estate property which is not attributed to the professional activity of the owner.

The relevant date (January 1st), the threshold for taxation (€1,3m), the tax brackets and the definition of taxpayers subject to the tax remain unchanged compared to the rules applicable to the ISF. Similarly, the flat 30% reduction applicable to the value of a principal residence is maintained.

The five-year exclusion of assets located outside of France from the taxable base for new French tax residents called “impatriates” is maintained; similarly to individual taxpayers with a tax domicile outside of France, individual taxpayers who have not been domiciled in France during the five years preceding the transfer of their domicile to France are only taxed on the property located in France, until December 31st of the fifth year following the year of arrival in France.

The applicable range and the taxable base for the IFI are significantly reduced; only non-professional real estate property is taxable, leading to the exemption of financial assets (notably cash, stock and equity) and moveable assets. In parallel, the rules regarding the exemption of professional assets are redefined and focussed on real estate.

Regarding the debt which may be deducted for French wealth tax purposes, debts granted to an intermediary entity should be deducted from the basis for determination of the portion of the shares of the intermediary entity subject to French wealth tax. However, loan granted by the taxpayer, a member of his family or an entity controlled by the taxpayer to the intermediary entity holding the property may not be deducted from the computation of the portion of the shares subject to French wealth tax except if the taxpayer may demonstrate that the financing by debt is not mainly tax driven.

Regarding the loans that are deductible for French wealth tax purposes, there is a limit of deduction when the taxable asset (the value of French real estate) exceeds €5m. Indeed, in such a case, when 60% of the value of the real estate is financed by debt, only 50% of the portion of the debt in excess of such threshold is deductible for French.

MLI

The Multilateral Instrument (MLI), signed June 7th 2017, and its article 9 (4) provides a new land rich clause for double tax treaties: “gains derived by a resident of a Contracting Jurisdiction from the alienation of shares or other rights of participation in an entity may be taxed in the other Contracting Jurisdiction provided that these shares or rights derived more than a certain part of their value from immovable property (real property) situated in that other Contracting Jurisdiction, or provided that more than a certain part of the property of the entity consists of such immovable property (real property).”

France noticed its intention to apply the provisions of article 9 (4) to its double tax treaties in force. In order for such article to apply to a double tax treaty signed by France, the Contracting Jurisdiction should not make any reserve for application of article 9 of the MLI and notice its intention to apply paragraph 4 of article 9 of the MLI.

On July 12th 2018, France ratified the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI), by way of Law No 2018–604, as published in Official Journal No. 0160 of July 13th 2018.

DAC 6

On October 21st 2019, the French government adopted a Ministerial Order (hereafter ‘the Order’) transposing into French law the EU Council Directive 2018/822/EU on cross-border tax arrangements (also known as ‘DAC6’ or ‘EU MDR’) in force since June 25th 2018.

The Ministerial Order was published in the French Legal Gazette on October 22nd 2019.

The provisions of the Order will take effect as from July 1st 2020 with specific transitional measures applicable to arrangements implemented between June 25th 2018 and June 30th 2020.

Pursuant to the EU Council Directive 2018/822/EU regarding mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements, intermediaries and taxpayers fall in the scope of new reporting obligations with respect to cross-border tax planning arrangements that meet certain hallmarks.

France had until December 31st 2019 to implement DAC6.

The Order closely follows the scope, the hallmarks and the reporting requirements set by the EU Directive.

The Order introduces six new articles in the French Tax Code (Articles 1649 AD to 1649 AH and 1729 C ter).

ATAD II, including hybrid mismatches with third countries

ATAD II, including hybrid mismatches with third countries ATAD I and II Directives were introduced as part of the 2015 OECD Base Erosion and Profit Shifting (BEPS) report, Action 2, on neutralising the effects of hybrid mismatch arrangements.

The French Government has recently published its draft Finance Bill for 2020. The draft Finance Bill is now under discussion in the French Parliament.

Article 13 of the draft Finance Bill for 2020 removes the current anti-hybrid rules set forth by Article 212, I – b of the FTC. For reminder, under this rules, interest paid to a related party is only tax deductible if it is taxed at the level of the beneficiary at a rate exceeding 25% of the standard French CIT rate (i.e., 7.75% for FY2019).

Article 13 would also introduce in French tax law the dispositions of the Anti-Tax Avoidance Directive as updated by the Directive 2017/952 dated May 29th 2017 ('ATAD 2'). In its draft, the French Government has duplicated the definitions and rules set forth by ATAD 2.

The new rules aim to neutralise hybrid mismatches related to differences coming from i) qualification of financial instruments, ii) qualification of entities and iii) rules regarding assignment of payments.

Four categories of hybrid mismatches are identified in the draft Finance Bill:

- hybrid mismatches coming from payments in relation with a financial instrument;
- hybrid mismatches coming from differences in the assignment rules of payments made to a hybrid entity or establishment;
- hybrid mismatches coming from payments made by a hybrid entity to its owner or payments made between the seat and the establishment (or between two establishments or more);
- double deductions effects.

Interest paid in the context of a hybrid mismatch would not be tax deductible in France if not included in the taxable basis of the beneficiary of the interest.

Please note that these new rules are a moving target in France as the draft Finance Bill is under discussion in the French Parliament until end of December 2019 so that our comments are thus not final. However, if the proposed provisions are maintained, the new rules seem to be less strict that the current rules as the FTA focus first on the nature of the paying entity and/or the nature of instruments (hybrid v. not hybrid entity) to analyse then the taxation of interest at the level of the beneficiary to disallow the deduction of interest at the level of the paying entity.

The explanatory statement of the draft Finance Bill for 2019 states that the current anti-hybrid rules could potentially be seen as non-compliant with EU rules (i.e. mechanism which could be viewed as disproportionate to achieve the purpose of the Directive ATAD 2). This could provide some arguments to challenge the application of the current anti-hybrid rules as applied for previous FYs.

Entry into force

All of these new provisions would apply to financial years beginning on or after January 1st 2020, with the exception of the new Article 205 C relating to reverse hybrid mechanisms, which would apply to financial years beginning on or after January 1st 2022.

Office tax

Annual Tax on Office in Ile-de-France (‘TABIF’) applies to owners of office and commercial spaces, business and commercial premises, storage facilities or parking spaces located in Ile de France at January 1st of each year.

As part of the draft finance bill for 2020, MEPs adopted an amendment creating a new “premium” zone in the most attractive municipalities and districts of Paris, where a 20% increase in the office tax will be applied. Four municipalities in the Hauts-de-Seine (Boulogne-Billancourt, Courbevoie, Issy-les-Moulineaux and Levallois-Perret) and nine Parisian districts (1st, 2nd, 7th, 8th, 9th, 10th, 15th, 16th and 17th) are concerned.

Amendments in compliance with EU Free Movement of Capital

Following an ECJ decision dated November 22nd 2018 (C-575/17 Sofina SA, Rebelco SA and Sidro SA) regarding French dividend withholding tax application to loss-making Belgian companies, the draft budget proposes the following main changes to French legislation:

For loss-making foreign companies under a compulsory liquidation procedure (or comparable) or in a dire financial situation with impossibility to recover, a withholding tax exemption would be granted not only to dividends, but also to withholding tax and levies on certain interest, payments, services, real estate gains, and non-resident capital gains (articles 119 bis, 182 A&B, 224 bis, bis A, and bis B of the French Tax Code).

Only a temporary refund will be granted for loss-making foreign companies in a situation to recover financially, until the foreign company becomes profitable and subject to filing and compliance obligations with the French Tax Authorities by the foreign beneficiary.

With respect to withholding taxes and levies under article 119 bis of the French Tax Code, the above provision would apply to foreign entities that are not located or established in non-cooperative states and territories pursuant to French legislation, and in jurisdictions having concluded both a mutual assistance convention regarding the tackling of fraud and tax evasion as well as a mutual assistance convention regarding tax collection with a similar scope to the EU Directive 2010/24 dated March 16th 2010.

With respect to the other types of levies and withholding taxes, the compliance amendments would only apply to foreign entities in EU Member states, or EEA states having concluded a mutual assistance convention regarding the tackling of fraud and tax evasion as well as a mutual assistance convention regarding tax collection, with a similar scope to the EU Directive 2010/24 dated March 16th 2010.

Please note that these new rules are a moving target in France as the draft Finance Bill is under discussion in the French Parliament until end of December 2019 so that our comments are thus not final. However, if the proposed provisions are maintained, they would apply to tax years beginning on or after January 1st 2020. Situations prior to that date would have to be reviewed and addressed through refund claim procedures.

10 Germany

Dividend and capital gains tax exemption

Dividend distributions between corporations are generally 95% tax exempt. However, the 95% tax exemption is only granted where the recipient of dividends holds at least 10% of the nominal capital of the distributing corporation at the beginning of the calendar year. Furthermore, the 95% tax exemption is limited to dividends that have not resulted in a corresponding deduction at the level of the distributing entity. This restriction particularly targets cross-border hybrid financial instruments in German outbound structures under which Germany classifies the financial instrument as equity but the foreign country treats the instrument as debt.

Capital gains received by corporations upon selling the shares in other corporations are 95% tax exempt. Since January 1st 2019 this generally also includes capital gains derived by selling shares in foreign corporations which assets – directly or indirectly – consists more than 50% of German real estate. If the shareholder is a foreign resident corporation, the capital gains are 100% tax exempt according to recent case law of the German Federal Fiscal Court. Currently, there is no minimum holding requirement. However, there are ongoing discussions to align the capital gain exemption rules with the dividend exemption rules, i.e. the 95% capital gains tax exemption would require a minimum holding of 10%.

Consider restructuring shareholding before distributing dividends (and sales of shares). Foreign corporate shareholders may claim a tax refund if they were taxed upon selling shares in other corporations.

Share capital repayments

Share capital repayments received by a German shareholder from a foreign corporation are generally treated as a taxable dividend in Germany. However, share capital repayments from EU-corporations to its German shareholders may not be qualified as taxable dividends but as repayment of shareholder equity upon application. Such application has to be filed up to the end of the calendar year following the calendar year in which the share capital repayment has been received.

Apply for equity qualification of share capital repayments received in 2018 before December 31st 2019.

Rollover relief

Gains of a German permanent establishment from the sale of land and buildings need not be taken to income immediately but may be deducted from the cost of purchasing replacement premises in the same or in the previous year. Alternatively, the gain may be carried forward and be deducted from the purchase price of land and buildings acquired during the following four years or from the construction costs of a building erected during the following six years.

For gains from the sale of land and buildings which do not belong to a German permanent establishment no rollover relief is available. However, the taxation of capital gains reinvested in another EU-member state may be deferred and spread over five years. The application for tax deferral has to be made up to the end of the financial year in which the land or building has been sold.

Apply for tax deferral on capital gains for EU land and buildings sold in 2019 before December 31st 2019.

Interest capping rules	Where an entity is not able to limit its net interest to below the €3m threshold, other escape clauses (non-group escape clause or group escape clause) might be applicable. According to the group escape clause, interest expenses paid in 2020 may be fully deductible only where the equity ratio of the German business equals or is higher than that of the group (2% tolerance) as at December 31st 2019. **It should be verified whether the equity of the tax paying entity equals that of its group. If it stays below the quota of the group by more than 2%, additional equity may be injected in order to ensure interest deductibility in 2020.**
Net operating losses (NOL) planning	According to tax accounting rules, an impairment to a lower fair market value may be waived. **In a loss situation, impairment may be waived to avoid an increase of net operating losses.**
NOL planning for partnerships	Net operating losses of a partnership are allocated to a limited partner only up to the amount of its equity contribution. **Inject equity before year-end in order to benefit from losses exceeding the current equity contribution.**
Losses carried forward	Any direct or indirect transfer of more than 50% of shares/interests (or similar measures, e.g. in the course of restructurings) may lead to a total forfeiture of losses and interest carried forward at the German entity's level. Exemptions may apply for tax privileged restructurings and where the entity continues to perform the same business as prior to the share transfer (restrictive requirements). Currently a case is pending at the German Supreme Court to determine whether the loss forfeiture rules are unconstitutional. The upcoming decision by the Supreme Court may have retroactive effect. **It is strongly recommended to explore structuring alternatives where you intend to reorganise your investment structure. All tax assessments for years in which a harmful share transfer has occurred should be kept open.**
Trade tax status	Investments relying on no trade tax due to the non-existence of a German trade tax permanent establishment, or a preferential trade tax regime under the extended trade tax deduction, must fulfil strict requirements. The requirements of the extended trade tax deduction must be met for a complete fiscal year. **It should be verified whether the requirements are met from January 1st 2020 onwards (if the fiscal year equals the calendar year) in order to mitigate trade tax on income derived in 2020.**
Tax prepayments	In the case of declining profits, an application can be made to reduce current income and trade tax prepayments. **Cash flow models and profit forecasts should be checked in order to improve liquidity by applying for tax prepayment reductions and/or refunds.**

Substance requirements

General substance requirements need to be met by foreign corporations receiving German income in order to be recognised by the German fiscal authorities. This inter alia may ensure the deductibility of interest expenses borne in connection with German investments. Where (constructive) dividends are distributed by a German corporation to a foreign shareholder, the foreign shareholder must fulfil strict substance requirements in order to benefit from a dividend withholding tax exemption/reduction.

Recently, the ECJ has decided that these substance requirements are not in line with EU law and thus the German fiscal authorities have in practice lowered the substance requirements for withholding tax exemptions/reduction. An amendment of the German tax law is expected in the next few months. According to current information, the new rules could lead to significantly stricter requirements in some areas compared to the current practice.

It should be ensured that German substance requirements are met and amendment of German tax law should be monitored. Where German dividend payments have been subject to dividend withholding tax due to a lack of substance, these cases should be kept open.

Transfer pricing

Generally, all related-party cross-border payments have to comply with the arm's length principle. Failure to present appropriate documentation to the tax administration might result in the non-acceptance of group charges and penalties for tax purposes.

The arm's length principle should be duly followed and documented.

Permanent Establishment (PE) cross-border transactions

The German tax legislation adopts the "Authorised OECD Approach". Cross-border transactions between the head office and a permanent establishment or between PEs are generally recognised for income tax purposes and must comply with arm's length principles.

Review cross-border transactions between head office and PEs.

Tax group

The acceptance of a tax group is subject to strict observation of certain legal requirements. The profit transfer agreement needs to be registered with the commercial register before December 31st 2019 in order to become effective for the fiscal year 2019. If companies do not obey the requirements during the minimum term of five years, the tax group will not be accepted from the beginning.

Special precautions need to be taken regarding tax groups for VAT and RETT purposes as there are different legal requirements.

Where a tax group shall be established in future, the profit transfer agreement needs to be drafted properly and registered in time.

Land tax

For vacant buildings and buildings rented subject to low conditions land tax up to 50% is refunded upon application of the landlord.

Apply for land tax 2019 refund before April 1st 2020.

Real estate transfer tax (RETT)

Federal states have the right to set the real estate transfer tax (RETT) rate themselves instead of applying the uniform federal RETT rate of 3.5%. In Bavaria and Saxony the rate of 3.5% applies. The other federal states have increased their RETT rate: Baden-Wuerttemberg (5%), Berlin (6%), Brandenburg (6,5%), Bremen (5%), Hamburg (4.5%), Hesse (6%), Lower Saxony (5%), Mecklenburg-Hither Pomerania (6%), North-Rhine Westphalia (6,5%), Rhineland-Palatinate (5%), Saarland (6,5%), Saxony-Anhalt (5%), Schleswig-Holstein (6,5%) and Thuringia (6.5%). Further increases are expected.

Monitor potential increase of RETT rates in federal states. Proper timing is necessary to avoid increased RETT rates. SPAs have to be concluded before possible further increase of RETT rates.

DAC6

According to the EU DAC 6 Directive, tax arrangements should be subject to reporting requirements if they are
- cross-border and
- have at least one of the marks listed in an Annex, and
- if a mark is subject to the main benefit test, this is fulfilled.

The parliamentary process to adopt the Directive in German law has just started on October 10th 2019. As DAC 6 must be implemented by the EU Member States by December 31st 2019, the law implementing mandatory disclosures rules shall come into effect by January 1st 2020.

Monitor the legislation process and observe your reporting requirements.

Planned tax changes

German tax law is subject to continuous changes.

Currently, there are a number of tax amendment acts in the legislative process which impact taxation of real estate investments.

Amongst others the land tax should be reformed. According to the draft law, the tax base should be aligned to the fair market value as at January 1st 2023. According to the intention of the legislator this increase in tax base should not lead to an increase in land tax burden. An opening clause is planned for the Federal States so that they can levy land tax according to other valuation methods. In the context of the land tax reform there are discussions to abolish the option of the landlord to charge the land tax as operating costs to the tenants.

Further, the RETT rules for share deals should be tightened. The main planned changes affecting real estate transactions are:
- lowering the 95% threshold to 90%;
- introducing a new rule according to which RETT is triggered if at least 90% of the shares in a corporation have been transferred within ten years;
- extending several RETT holding periods from five to ten years.

The draft law is currently under revision. It is expected that revised RETT rules could come into force in the first half of 2020.

Constantly monitor German tax law changes.

11 Italy

Interest capping rule

Effective from FY 2019, the interest capping rule (based on 30% **accounting** EBITDA) has been updated in order to implement the ATAD provisions (Anti-Tax Avoidance Directive, EU Directive 1164/2016). In particular, for corporate income tax (IRES) purpose, interest expenses are now deductible within the limit of interest revenues, and subsequently within the limit of 30% of the **fiscal** EBITDA (before reference was to the accounting EBITDA), where the latter results from the P/L EBITDA adjusted according to the same provisions used in determining the company's corporate income tax base (i.e., revenues and expenses are included in the same measure they are relevant for IRES purpose).

Interest expenses that exceed such limits can be carried forward and deducted in the following fiscal years without time limitations, however, only up to the amount of the interest revenues and 30% fiscal EBITDA of any following year (the latters net of the interest expenses of the same year). Any "excess" of 30% fiscal EBITDA (i.e. the amount exceeding the net interest expenses of that fiscal year) can be carried forward and used to increase the 30% fiscal EBITDA of the following FYs, but only within a five-year time limit. In addition, in case interest revenues exceed interest expenses in a year, such excess may be now carried forward without any time limitation.

Interest expenses concerning facilities executed before June 17th 2016, whose amount or duration has not varied after that date, should be deductible pursuant to new rules or using the 30% EBITDA excesses not yet used up to 2018. This specific portion of EBITDA can be carried over indefinitely, following the previous regulation, but can be used only to deduct interest expenses on facilities executed before June 17th 2016, whose amount or duration has not varied after that date (contrarily, any excess EBITDA existing at year end 2018 will be definitively lost). Furthermore, interest expenses capitalised on assets (to the extent admitted) are now subject to the interest-capping rule (previously they were excluded).

However, it has been confirmed that interest expenses that have been generated by loans/debts guaranteed by mortgages on real estate up for lease are still not subject to the interest capping rule. Pursuant to law (as amended with effect from the tax period starting after October 7th 2015), the benefit of the exclusion of mortgage loans interest from the EBITDA limitation is applicable only to companies which carry on "actually" and "prevalently" real estate activity. This is met if the following conditions are fulfilled:
- the greater part of the total assets are formed by the fair value of properties up for lease;
- at least 2/3 of the revenues derive from building rentals and leases of business which is made prevalently by buildings.

These rules do not apply to partnerships, which can fully deduct interest expenses.

With regard to intercompany non-interest bearing loans, pursuant to the amortised cost method, provided also by the national accounting standards, a notional interest cost should be booked in the P/L account. This interest cost is however not tax deductible.

Evaluate the impact of the interest capping rule as amended, especially with regard to capitalised interest and carried forward EBITDA. Check if there are any interest expenses from previous years that have been carried forward; if so, check if they can be deducted in the year.

Evaluate the possibility of a tax group so that the non-deductible interest from each company can be used to lower the consolidated income, provided that other consolidated entities have "unused" 30% fiscal EBITDA in the same FY.

Check if the stated asset test and revenues test are fulfilled to take benefit from full deduction of interest on mortgage loans concerning properties up for lease.

Check if the P/L includes notional interest booked with respect to intercompany non-interest bearing loans pursuant to the amortised cost method, to be excluded from tax deductible interest expenses.

Tax losses carried forward

For corporate income tax (IRES) purpose, tax losses can be carried forward without any time limit, as follows:
- tax losses incurred in the first three years of activity (provided that they derive from the launching of a new activity) can be used to entirely offset future taxable income;
- tax losses incurred in subsequent years can be used to offset only 80% of the taxable income of any following year. The remaining 20% must be taxed according to the ordinary rules (IRES rate: 24%), resulting in a kind of a "minimum corporate tax".

It is possible to combine the use of the two kinds of tax losses to reduce/offset the taxable income as much as possible. For this purpose, the taxable income of a year may be firstly reduced by 80% using the ordinary tax losses and secondly entirely offset by using tax losses generated during the first three periods of activity, if any, and up to the amount available.

The loss carried forward may be limited in the case of transfer of shares representing the majority of voting rights in the company's general meetings, if also the change of the business activity from which such tax losses derived intervenes in the year of transfer or in the preceding or following two years (exceptions exist).

These rules do not apply to tax losses pertaining to partnerships, which can be carried forward for five years (in the hands of partners), except for those produced in the first three fiscal years which remain "evergreen" (however, some anti-abuse provisions have to be considered also in this case).

The carry-forward of tax losses (as well as of other tax attributes, namely: interest expense and ACE excesses) can meet limitations in case of tax neutral reorganisations (e.g., mergers, spin-offs), in light of a specific anti-abuse provision.

The regional tax on production (IRAP) provisions do not allow any tax losses carried forward.

Check if there are any tax losses that can be carried forward and define their regime of carry-forward.

Make sure that the combination of different kinds of tax losses is suitable, also to maximise the offsetting of the future taxable income.

Check if the tax losses carried-forward are affected by the “change of control” limitation or by other anti-abuse provisions.

“Passive” company legislation

The “Passive” (or ‘non-operative’) company rule postulates that if an “expected minimum” amount of revenues (calculated as a percentage of the average value of the fixed assets over a three-year period) is not reached (‘operative test’) the company is deemed to be “non-operative”, with the consequence that taxation for both corporate income tax (IRES) and regional production tax (IRAP) will not follow the ordinary rules, but will be based on an “expected minimum” taxable income (that cannot be offset by tax losses carried forward), calculated as a percentage of the value of the fixed assets owned. This rule applies also to partnerships.

Other implications for “non-operative” companies include limitations to the tax losses carried forward and to VAT credit refunds/offsets.

In addition, the tax losses incurred in the years of “non-operative” status are disregarded.

Moreover, from the tax period current on December 31st 2012, a company may be considered “non-operative”, regardless if its actual proceeds are higher than its expected ones, also in case it is in a “systematic tax loss” position. A company is intended to be in a “systematic tax loss” position if it declares a tax loss for five consecutive tax periods (before year 2014 the observation period was three years) or, in a five-year period, it declares a tax loss for four years and in the other year its actual revenues do not reach the “expected minimum” ones. In this case, the company is deemed to be “non-operative” in the year following the five-year observation period.

The law provides a list of circumstances in which the application of this legislation is automatically excluded. Out of these cases, if the “non-operative” status is due to objective circumstances, the non-application of this regulation may be claimed by way of specific ruling. However, from FY 2016, in presence of such valid objective circumstances which did not consent the minimum level of revenues (or lead to a systematic tax loss position), the taxpayer can settle income taxes and fulfil relevant payment and reporting obligations without considering the non operative companies rules. The proper demonstration and related documentation have to be submitted to the Tax Office upon request. However, if this demonstration is deemed not sufficient to objectively justify the deviation from the expected revenues, the taxpayer is exposed to the penalties for untrue tax returns.

For companies which are deemed “non-operative” the IRES rate is increased by 10.5% (therefore from 24% to 34.5%).

Check if the company satisfies one of the cases of exclusion from “passive” company legislation provided by law.

Check if the actual revenues allow to comply with the “operative test”.

If the “operative test” is not passed or if the company is in “systematic tax loss” position due to objective circumstances which prevented to reach the “expected minimum” revenues, ask for the non-application of the “passive” company regime by ruling duly documented or, alternatively, arrange a proper set of supporting documentation to be submitted to the Tax Office upon request.

Consider the implications on direct taxes liabilities, tax losses carry-forward/utilisation, VAT refunds/offsets and on VAT credit carried-forward.

Losses on receivables

In general, losses on receivables are deductible if they can be proved with “certain” and “precise” elements and, in any case, when the debtor is subject to bankruptcy and stated similar proceedings. “Certain” and “precise” elements also exist when the credit right is expired or the credit is written-off from the financial statements in compliance with the correct application of the accounting principles. Moreover, losses on receivables may be fully deducted when the following two conditions are met: i) their amounts do not exceed €5,000 (for companies with revenues higher than €100m) or €2,500 (all the others) and ii) the credit has expired from at least six months.

Check if losses on receivables are supported by “certain” and “precise” elements.

Check if the losses on receivables refer to debtors which entered into a special eligible proceedings.

Consider the amount of the credit and the date of its expiration.

Allowance for Corporate Equity

The Allowance for Corporate Equity (Aiuto alla Crescita Economica, or ACE) was a tax relief (applicable since tax period 2011) aimed to boost business capitalisation. It allowed a yearly deduction for IRES purposes, corresponding to the “notional” interest on net equity increases occurred in respect to the net equity existing at year end 2010 (net of the 2010 profit), computed with rate of 1.5% for FY 2018 (the rate was 3% in FYs 2011–2013, 4% in FY 2014, 4.5% in FY 2015, 4.75% in FY 2016 and 1.6% in FY 2017). However, this measure has been repealed starting from fiscal year 2019.

Although it has been repealed, any unused ACE deduction existing at year end 2018 can still be carried forward without any time limit to offset future IRES tax bases.

Check if there is unused ACE deduction carried forward.

Tax benefit for reinvested earnings ('mini-IRES')

Starting from FY 2019, reinvested net profits (and accounted into available retained profit reserves in the net equity) may benefit from a lower IRES tax rate, applied to the portion of the company's tax base equal to the amount of the reinvested net profits aggregated from FY 2019 onwards.

The new tax regime will be introduced gradually by raising the tax discount every year, leading with a 1.5% IRES reduction (resulting in a 22.5% IRES rate in lieu of the ordinary 24%) for FY 2019, 2.5% (21.5% IRES rate) for FY 2020, 3% (21% IRES rate) for FY 2021, 3.5% (20.5% IRES rate) for FY 2022 and, finally, 4% reduction (20% IRES rate) from FY 2023 onwards.

This benefit applies to tax resident companies, as well as partnerships and individual business undertakings, if they apply ordinary (i.e. not simplified) bookkeeping rules.

Earnings reinvested can benefit from this fairer taxation only up to the effective net equity increase compared to FY 2018 net equity. In addition, in case such earnings exceed the IRES tax base of the year, the excess can be carried forward in order to be computed in the benefit of the following year.

Evaluate the possibility and convenience (if any) to reinvest net profits instead of making distributions, in order to benefit from this new tax benefit.

Capital dotation of Italian branches of foreign entities

Legislative Decree No 147/2015 has updated the provision of the Italian Income Tax Code concerning the permanent establishment in Italy of foreign entities (e.g., branch). In particular, it has been also explicitly stated that an Italian branch must have a "congruous" capital dotation (free capital) for tax purposes (it may be also a notional dotation, made by way of treating as undetectable the relevant portion of interest accrued on the financing by the head office). Such capital dotation has to be determined according to the OECD guidelines, taking into account the specific features of the branch (i.e., business activity and related risks and assets used to perform it).

The quantification capital dotation has direct impact on the calculation of the deductible interest expenses.

The new provision is effective from FY 2016, but it may be used by the Tax Office to carry on assessments on previous fiscal years with regard to the redetermination of the "congruous" capital dotation (however, without penalties for the past).

In case of an Italian branch, check if its capital dotation (also in the form of head office's not bearing interest financing) can be considered congruous, in light of assets and risks owned by/attributed to the branch.

Transfer pricing documentary requirements

The setup of a Transfer Pricing (TP) documentation according to certain parameters allows avoidance of tax penalties in case of assessment on transfer pricing matters carried out by Italian tax authority (penalties range from 90% to 180% of the higher tax). The existence of such documentation has to be declared in the annual income tax return. It is worth to note that the Financial Bill 2014 has expressly extended the application of transfer pricing rules also to IRAP.

Map the intra-group transactions and evaluate the tax penalty profile of TP policies not fully compliant with the arm's length criteria, and act accordingly.

Local property tax (IMU) for builders

With effect from the balance payment of local property tax (IMU) for year 2013 onwards, builders are exempt from IMU with regard to buildings built and addressed to be sold (of any kind: residential or commercial/industrial), as long as they are not leased.

Consider the favourable impact of the provision for builders.

Deductibility of Local Property Tax (IMU) on "instrumental" buildings

Local Property Tax (IMU) paid over "instrumental" buildings (these being non residential buildings, directly used in the company's business – therefore subject to depreciation) will benefit from a progressive increase of the deductible amount for IRES purpose over the next few FYs, reaching the full deductibility in FY 2023. In particular, deductibility will increase for IRES purposes from 20% applicable until FY 2018 to a much higher 50% for FY 2019, 60% for FYs 2020 and 2021, 70% for FY 2022, and 100% from FY 2023.

These provisions are precluded to real estate assets for sale (inventory) and those that do not pertain to the company's business.

Consider the opportunity of these increased deductions for real estate lease companies.

Revaluation of buildings – monitoring of recapture period

In previous years several revaluation laws allowed the tax relevant step-up of the investment assets, among which:
- Financial Bill 2014, for the purpose of the fiscal year in course on December 31st 2013 (year 2013, for calendar-year taxpayers);
- Financial Bill 2016, for the purpose of the fiscal year in course on December 31st 2015 (year 2015, for calendar-year taxpayers);
- Financial Bill 2017, for the purpose of the fiscal year in course on December 31st 2016 (year 2016, for calendar-year taxpayers).

However, the higher value was recognised: i) for tax depreciation purpose, from the third year following the one of step-up (thus, for the three provisions stated above from year, respectively, 2016, 2018 and 2019); ii) for capital gain/loss from disposal, from the fourth year following the option (i.e., from year, respectively, 2017, 2019 and 2020).

Detect sales of revaluated real estate properties before the tax recognition of their step-up.

Consider that once the increased values are recognised for tax purposes they are relevant for depreciation, but also for "passive" company legislation.

Shareholders' debt waivers

With regard to shareholders' debt waivers executed after October 6th 2015, the debt waived is taxable for IRES purposes in the hands of the subsidiary to the extent its accounting value, as booked in the subsidiary's general ledger, exceeds its related tax value in the hands of the shareholder.

For this purpose, the shareholder has to communicate in writing to the subsidiary the tax value of its credit waived. In absence of such communication, the entire accounting value of the waived debt is subject to tax.

In case of shareholders' debt waiver executed in the year, obtain the shareholder's communication in order to prevent (or limit) taxation of the contingent income.

Domestic Tax Group regime extended to "sister" companies

Italy has introduced the so-called "horizontal" tax consolidation for corporate income tax (IRES) purpose: the Domestic Tax Group regime can now include also resident "sister" companies, i.e., companies which are not controlled (even indirectly) by the domestic consolidating entity, provided that all the subjects falling in the Tax Group perimeter are subject to the common control of a EU based company.

The change has been enacted by Legislative Decree No. 147/2015 and is effective from the tax period in course on October 7th 2015.

In case of non-Italian EU group, if the foreign controlling company does not have a permanent establishment in Italy, it can designate the entity in the Tax Group perimeter which will act as consolidating entity.

In case the group has more Italian companies, consider if the tax consolidation regime is feasible and may allow tax efficiencies or other benefits.

New tax ruling for new relevant investments

Enterprises which intend to make investments in Italy for at least €20m and with relevant positive effects on employment with regard to the activity object of the investments, will be entitled to submit a ruling to the Tax Office to address: i) the tax treatment of the investment plan and of any eventual extraordinary operations that may be performed to implement the investment; ii) eventual abuse of law and/or tax avoidance profiles of the intended investments; iii) the request of disapplication of anti-avoidance provisions and/or of access to specific tax regimes. For this purpose, the intended investment and related plan have to be disclosed and detailed in the ruling.

The Tax Office replies within 120 days. This term can be extended in case of request of further information/documentation by further 90 days (starting from their submission). In absence of reply within the stated deadline, the tax treatments/conclusions proposed by the applicant are deemed as accepted and applicable (so-called 'silence-acceptance'). The Tax Office's reply (explicit or implicit) is binding till the terms and conditions of the new investment/business disclosed in the ruling remain unchanged.

Ministerial Decree dated April 29th 2016 and Tax Authorities provision dated May 20th 2016 set forth relevant application guidance.

Statute of limitation regarding tax assessment

Pursuant to Financial Bill 2016, starting from fiscal year in progress at December 31st 2016, tax assessments (for both Income Taxes and VAT purposes) can be notified within December 31st of the fifth year following the one in which the relevant tax return is filed (e.g., tax year 2016; filing of the tax return in 2017; tax assessment expiry term on December 31st 2022).

The statute of limitation can be extended by further two years in case of omitted filing of the tax return.

In case of filing of an amended tax return pursuant to the self-curing procedure, with respect to the amended date the aforesaid expiry terms shall run from the date of the amendment itself (e.g. original filing of the tax return for tax year 2016 in 2017 – tax assessment expiry term on December 31st 2022; filing of the amended tax return in 2018 – tax assessment expiry term for the amended items only on December 31st 2023).

For tax years before the one in progress on December 31st 2016 (for both Income Taxes and VAT):

- tax assessments can be notified within December 31st of the fourth year following the one in which the relevant tax return is filed (e.g., tax year 2015; filing of the tax return in 2016; tax assessment expiry term on December 31st 2020);
- in case of omitted filing of the tax return, the above term is extended by one further year;
- in case of violations relevant for tax criminal law, reported to the Public Prosecutor within the ordinary statute of limitation, the above term is doubled (i.e., in case of timely filed tax return, December 31st of the eight year following the year of filing).

Tax credit for companies without employees

Pursuant to Financial Bill 2015, with effect from fiscal year 2015, labour costs concerning open-ended jobs are fully deductible for IRAP purposes.

In this contest, in order not to disadvantage companies without employees, the latter can benefit from a tax credit, to be used to offset all kind of taxes, equal to 10% of the annual IRAP liability. Such tax credit gives rise to a non-contingent income subject to IRES taxation.

In case of company without employees, check if it may be convenient to take benefit from this rule.

Country-by-Country Reporting (CbCR)

With effect from FY 2016, the Country-by-Country Reporting (CbCR) regulation has been enacted. In particular, multinational groups with global turnover exceeding €750m and mandatorily drawing-up the consolidated financial statements, have to report specific data in each jurisdiction where they are present.

The Italian entities belonging to a multinational group in the scope of this regulation, has to:

- communicate to the Italian Tax Authority, in its income tax return:
  - its CbCR status (e.g., ultimate parent entity, constituent entity);
  - certain information of the ultimate parent entity and of the reporting entity (in principle, apart certain cases, the reporting obligation is in the hands of the ultimate parent entity – i.e., the one that prepares the consolidated financial statements);
- file to the Italian Tax Authority the CbCR related to the whole group, within 12 months from the last day of the year subject to reporting, if:
  - the ultimate parent entity is not required to file the CbCR in its jurisdiction, and/or
  - the jurisdiction where the ultimate parent entity is resident for tax purposes, does not have a Qualifying Competent Authority Agreement in force with Italy for the exchange of the CbCR.

Check if the requirements to file the CbCR are met (i.e., existence of a multinational group with turnover exceeding €750m and obliged to draw-up consolidated financial statements).

If in CbCR scope, check the status of the Italian entity (e.g., parent entity, constituent entity).

Check if the ultimate parent entity is required to file the CbCR in its jurisdiction. If so, check if this jurisdiction has a Qualifying Competent Authority Agreement with Italy for the exchange of CbCR information.

In case the Italian entity has to file the CbCR for the whole multinational group (this should be if the questions in previous paragraph are negative), collection of all the information to be reported pursuant to the CbCR regulation.

12 Latvia

Changes as of January 1st 2019

The CIT Act (in force as of January 1st 2019) prescribes that a Latvian company owning a substantial share in a foreign company (owning more than 50% of a foreign company's shares directly or indirectly or being entitled to more than 50% of its profit) should pay CIT on profit in proportion to that share if the foreign company is a non-genuine (artificial) arrangement established to obtain CIT advantage and no substantial business is carried on by the CFC. If these criteria are met, then any profit made by a CFC that is based or incorporated in a tax haven is taxable in Latvia from the first eurocent, while a CFC registered elsewhere will not attract CIT unless its profits reach €750,000 and passive income exceeds €75,000.

Taxation of dividends

PIT: The rate of PIT on dividends is 20%, subject to tax exemption on dividends already subject to PIT or CIT at source. During a two-year period of transition, dividends paid out of profits arising before 2018 will attract a 10% PIT. From 2020 onwards, also dividends paid from pre-2018 profits will attract a 20% PIT.

CIT: Flow through dividends would be exempt from CIT provided that they are received from corporate income taxpayer or tax has been withheld at source state. In addition some anti-avoidance provisions would apply aimed at offshore entities or artificial structures.

Review your dividend payment policy in order to benefit from the new tax reform (e.g. profits paid out of retained earnings up to December 31st 2017 are not a subject to CIT).

Management fees

Management and consulting fees paid to non-residents are subject to a 20% withholding tax (WHT). However, WHT may be eliminated under provisions of the respective tax treaty. In order to apply for a more favourable tax regime, the non-resident has to provide the payer with a residence certificate.

Given the fact that settlements are often made at year end, the Latvian payer should obtain this certificate from the income recipient to ensure income is not taxed before the submission deadline of the last CIT return (i.e., January 20th of the following year).

Sale of shares and securities

In line with the CIT Act the income arising on the disposal of shares constitutes CIT taxable base. At the same time, CIT Act provides the relief determining the reduction of the taxable base in case of a disposal of direct participation shares held for at least 36 months (i.e., three years). Mentioned relief is not applicable to the shares held in the companies established in black-listed jurisdictions.

Please note there are specific rules for the sale of real estate company shares by non-residents.

If relevant, please take into account that income gained on disposal of shares held for three years or more may be used in order to reduce CIT taxable base.

Sale of real estate/rental income	The sale of property by non-resident directly is subject to 3% WHT. The same applies also to the sale of company shares, if at least 50% of the assets in this company at the beginning of the year of disposal or in the previous year are formed by real estate in Latvia. Non-resident from the EU or tax treaty country can choose whether to pay 3% WHT from the sales proceeds or 20% tax from the profit. The same principle applies to income from consulting services. The change of real estate ownership attracts a stamp duty payable at 2% of the acquisition price. If a real estate is invested in a company's share capital, the stamp duty is 1% of the amount to be invested as share capital. **In case of the sale of real estate EU/tax treaty resident may choose between 3% WHT payment calculated on total income or 20% tax on profit.**
Losses carried forward	The CIT Act does not include the concept of tax losses. Transitional rules stipulate that the tax losses can be utilised by the companies during five financial years (beginning in 2018) by deducting an amount equal to 15% of the total loss brought forward from CIT calculated on dividends for the financial year. However, such deduction is capped at 50% of the amount of CIT charged on dividend for the financial year. **Review the possibilities to utilise tax losses carried forward in next four years (until 2022).**
Deductibility of interest payments	CIT is payable on the increased interest payments. The allowable interest shall be calculated applying following methods: Method 1 anticipates that interest is deductible, if the average liability does not exceed four times shareholders' equity at the beginning of the tax year less any revaluation reserve, excluding, loans from qualifying leasing companies. Method 2 The threshold is applied through calculating the 30% EBITDA of the loan receiver and is applied only if the receiver's annual interest expenses exceed €3m, including, finance lease interest expenses. In this case the annual interest expenses exceeding the threshold are considered as a taxable item for CIT purposes. In case both methods are applicable, the higher of the two amounts calculated which exceed the afore-described threshold should be added to the CIT taxable base. There are number of exemptions from above rules, e.g., qualifying loans from credit institutions do not fall under the mentioned regulation. **If relevant, consider options for improving equity before years end in order to improve deductibility of interest next year.**

Exchange of shares

Where a share exchange takes place (one kind of shares being exchanged for another kind without receiving any other type of consideration), no disposal of shares is considered to take place within the meaning of the PIT Act and hence payment of personal income tax is postponed to a future date when the person will sell the shares acquired through exchange.

Where a share exchange takes place (one kind of shares being exchanged for another kind), payment of PIT is postponed and is due when the individual sells the shares acquired through exchange.

Provision for bad debts

Provisions for bad debts do not become a subject to CIT if debts are repaid during 36 months period.

Opportunities to recover bad debts should be considered to decide how much provision for bad debts is necessary.

Write-offs for bad debts

Bad debts must comply with certain criteria listed in the CIT Act in order not to constitute the CIT taxable base, when written off.

Consider whether the particular debt complies with these criteria.

Transfer pricing

All related-party cross-border payments have to comply with the arm’s length principle. Failure to present appropriate documentation to the tax administration might result in the non-acceptance of group charges and penalties for tax purposes.

The obligation to submit TP documentation, both Master and Local file or only one of them and submission deadlines depend on the amount of the controlled transactions and the respective partners of the transaction. Respectively, if a taxpayer, resident, or PE enters into a transaction with a:

- related foreign company
- related private individual
- company in offshore country, or
- related Latvian-resident company and the transaction is economically linked to transactions with a related foreign entity or with an entity registered in a tax haven under the single supply chain transaction,

then the requirements may apply, and one should look at the amount of the transaction.

The arm’s length principle should be duly followed and documented.

Real estate tax (RET)

Companies have to pay annual real estate tax. Generally, the RET is between 0.2–3% of the cadastral value. The exact rate is determined by each municipality.

In accordance with The National Cadastre of Real Estate Act the cadastral values will change once every two years if the property market or factors affecting the value of an area have changed.

Consider the RET payments taking into account available exemptions and possible changes in cadastral value.

Value Added Tax (VAT) legislation regarding sale of real estate (RE) in Latvia

According to VAT Act sale of unused real estate and development land attracts the standard VAT rate.

Under VAT Act, development land is defined as a piece of land that is covered by a permit issued under construction law for building development, engineering communications or access roads.

Unused RE within the frame of VAT Act means:
- Newly constructed buildings (and an associated land unit or its part) or structures (including any fitted stationary equipment) that are not used after completion;
- Newly constructed buildings (and an associated land unit or its part) or structures (including any fitted stationary equipment) that are used and sold for the first time within a year after completion;
- Buildings (and an associated land unit or its part) or structures that are not used after completion of renovation, reconstruction or restoration (RRR) work;
- Buildings (and an associated land unit or its part) or structures that are used after completion of RRR work and sold for the first time within a year after completion;
- Incomplete construction items (and an associated land unit or its part); and
- Buildings (and an associated land unit or its part) or structures undergoing RRR before completion.

There might be claw-back provision, if a RE previously acquired with VAT has been further sold as used within the meaning of VAT. It means that the seller is liable to repay a proportion of Input tax previously recovered.

Option to tax allows a registered taxable person to charge VAT on supplies of used RE transactions. This option is available only where property is registered with Latvian tax authorities and sold to a registered taxable person.

Make sure that VAT for the sale of RE has been applied correctly.

VAT grouping

The VAT grouping facility helps related companies reduce their administrative burden and improve cash flows, as their mutual transactions no longer attract VAT. A single VAT return can be filed covering all group companies. This especially benefits group companies with both taxable and exempt supplies and companies that have extensive sales outside Latvia.

Consider the option of creating a VAT group.

Reverse-charge VAT on construction services

Reverse-charge VAT is applied to construction contracts signed after December 31st 2011.

Make sure that reverse-charge VAT has been applied correctly.

Permanent establishments

If you have not registered a legal entity or a branch in Latvia, consider if your business operations have created a permanent establishment (PE), which requires a CIT compliance in Latvia.

Consider the requirements for registering a PE in Latvia.

13 Lithuania

Investment in Real Estate and Land

There are no restrictions for foreigners to acquire the immovable property in Lithuania (except for land). Agricultural, non-agricultural and non-forestry land, inland waters and forests can be acquired only by companies or individuals who are established or residing in the EU member states or in countries that are the members of OECD, NATO or EEA and receive relevant permissions from local authorities.

Additional restrictions are applied in respect of acquisition of agricultural and forestry land. Individuals and companies (both local and foreign) are allowed to buy up to 500 hectares of farmland (or more if the buyer is a stockbreeder and some other conditions are met). As of January 1st 2020 individuals and companies (both local and foreign) are allowed to buy up to 1,500 hectares of forestry land as well as other restrictions to acquire forestry land apply.

Real estate related transactions are subject to a notary's approval. The notary fee charged in case of a sale and purchase of real estate amounts to 0.45% of the real estate price but not lower than €28.96 and not higher than €5,792.40. Besides, changes in real estate ownership rights must be registered with the Real Estate Register. The amount of the fee charged for the registration of a title to immovable property depends on the type and value of the property.

In case of a share deal the transfer of shares in a real estate holding entity is subject to the notary fee of 0.4–0.5% on the value of transaction (the fee shall not be less than €14.48 or exceed €5,792.40), when:
- ≥25% of limited liability company's shares are sold;
- the sale price of the limited liability company's shares sale exceeds €14,500 except for certain exemptions.

State duties imposed upon the registration of a transfer of real estate are typically not material and vary depending on the real estate value (up to €1,448.10).

It is advised to monitor Lithuanian land law and forestry law for possible changes.

Group Taxation

Generally, tax grouping is not allowed in Lithuania, thus each company is taxed separately. However, current year operating tax losses can be transferred to another legal entity of the group if certain conditions are met (see section 'Losses Carried Forward' below).

Real Estate Tax (RET)

The real estate tax (RET) is applied both for local and foreign tax residents holding real estate in Lithuania. RET is levied on the value of immovable property owned by legal entities. Local municipalities must set tax rate before July 1st of the previous tax period. RET rate ranges from 0.3% to 3% depending on the local municipality.

In Vilnius, the RET rates established for 2019–2020 are:
- 1% – standard RET rate;
- 0.7% – for cultural, leisure, catering, sport, educational or hotel buildings (with some exceptions);
- 3% – for actually used real estate, that is not 100% completed and for real estate that is not used at all or is abandoned or unattended.

Immovable property owned by individuals and used for commercial purposes is also subject to real estate tax.

Residential and other personal premises owned by individuals are exempt from tax where the total value of €220,000 is not exceeded, whereas the excess value is subject to progressive taxation:
- 0.5% RET rate is applied on taxable value exceeding €220,000 but not exceeding €300,000;
- 1% RET rate is applied on taxable value exceeding €300,000 but not exceeding €500,000;
- 2% RET rate is applied on taxable value exceeding €500,000.

Total non-taxable value is increased by 30% to real estate held by families which meet certain criteria.

RET base is the average market value of the property: depending on the type and purpose of the property it can be assessed either by mass valuation method (performed every five years) or using the replacement value (costs) method. There is a possibility to apply the property value determined during the individual valuation if it differs from the market value by more than 20%.

RET return for residential and other personal premises owned by individuals should be submitted to the Tax Authorities and the tax due should be paid until December 15th of the current tax period. For other RET owned by individuals or legal entities – until February 15th of the next tax period.

Please be informed that draft RET legislation determining changes in RET system as of January 1st 2020 is prepared, however, it is not yet approved and subject to change.

Real estate tax rates as well as other conditions in specific municipality should be followed in case of possible changes.

Procedure of Filing advance Real Estate Tax Return

Legal entities have an obligation to pay advance RET on a quarterly basis. Advance RET return for the first nine months of the current tax period should be submitted together with the annual RET return for the previous tax period.

Value Added Tax (VAT)

The standard VAT rate in Lithuania is 21%. The reduced VAT rates are 5% and 9%. The sale of new buildings is subject to VAT at the standard rate while the sale of buildings used for more than 24 months is VAT-exempt. A sale or any other transfer of land is exempt (except for building land and land transferred together with a new building that has been used for less than two years and land for construction). Rent of real estate is also VAT-exempt (with some exceptions).

However, taxable persons are entitled to opt for taxation of sale of buildings older than 24 months or land and buildings' rental services with VAT if such buildings/land are sold or rented to VAT payers. If option is exercised, it has to be applied consistently for 24 months.

Lithuanian VAT payer can adjust output VAT payable to the Lithuanian budget due to bad debts if certain conditions are met.

VAT treatment of services related to Accommodation Services

The official Commentary of the VAT Law on the application of 9% VAT rate to the supply of accommodation services was supplemented with additional explanations based on the decisions of the European Union Court of Justice.

In cases when together with accommodation services secondary services, which make the accommodation services more appealing are provided (without additional fees, e.g. access to water entertainment area), the secondary services should be considered to be inseparable from the main services, i.e. accommodation services. 9% VAT rate should be applied for such composite supply.

Reverse-charge VAT on construction services

Local reverse-charge VAT mechanism applies for supply of construction services, when such services are supplied to a taxable person Lithuanian VAT payer. If a foreign entity supplies construction services in Lithuania to a taxable person Lithuanian VAT payer, then the foreign entity is required to register with the Lithuanian VAT payers' register and apply local VAT reverse-charge mechanism for construction services.

Reverse-charge VAT mechanism is also applicable to supply of goods installed in immovable property in which construction services are performed and after such installation the goods become an integral part of the property. Such treatment is applicable when goods are supplied under a single agreement (supply of goods and installation services).

Each case should be analysed separately in order to comply with reverse-charge mechanism correctly.

IT-based tax administration system – i.MAS

The Lithuanian Tax Authority has introduced an IT-based tax administration system ('i.MAS'). The Tax Authority is collecting data from taxpayers and is using this data for control purposes.

For the tax period starting from October 2016, all persons registered for VAT purposes in Lithuania are required to submit invoice data to i.SAF subsystem on a monthly basis (with some exceptions).

In addition, following certain turnover thresholds, with effect from 2017 till 2019, companies established in Lithuania are required to prepare their accounting data in a SAF-T file and upon request provide it to the Tax or other Authority.

Corporate Income Tax

Standard Corporate Income Tax (CIT) rate is 15%. Small entities (i.e. entities with fewer than ten employees and less than €300,000 gross annual revenues) can benefit from a reduced corporate income tax rate of 0% for the first tax period and 5% for the consecutive tax periods with certain exceptions.

Generally, the taxable period for corporate income tax is the calendar year. The tax return has to be filed and corporate income tax due has to be paid before June 15th of the next taxable period.

The companies with annual turnover exceeding €300,000 are also subject to advance CIT payment in Lithuania.

Subject to permission from the State Tax Authorities, a taxable period other than the calendar year may also be used by companies. In that case, the payment and declaring terms should be changed accordingly.

Dividends Exemption Rule

Dividends distributed by a Lithuanian company to another Lithuanian company are generally subject to a 15% CIT, which is withheld by a distributing company.

Dividends distributed by a Lithuanian company are exempt from Withholding Tax (WHT) if the recipient company has held not less than 10% of the voting shares in the distributing company for at least a 12-month period and the distributing entity is subject to 5% or 15% Lithuanian CIT rate (except for blacklisted territories).

Dividends distributed by a foreign company are subject to a 15% CIT that is to be paid by the receiving Lithuanian entity.

However, dividends distributed by a foreign company to a Lithuanian company are exempt from CIT in Lithuania if the distributing foreign entity is established in the EEA and related profit is properly taxed in the domiciled country.

As of March 26th 2016, dividend exemption to the taxation of dividends paid to and/or received from foreign legal entities are not applicable to the structure or several structures if the main purpose or one of the main purposes of them is to obtain a tax advantage, which contradicts to the object and purpose of EU Council Directive (2011/96/EU Directive and its partial amendments 2014/86/EU and 2015/121/EU) regarding common tax system, which is applicable for parent and subsidiary companies of various EU member states. The taxation exemption of dividends received from foreign legal entities, are not applicable to dividends, which were used to reduce the profit of foreign legal entities, which is subject to corporate income tax or an equivalent tax.

Due to the recent initiatives to fight against tax avoidance and aggressive tax planning Lithuanian Tax Authority pays more attention to the substance of holding companies. Therefore, holding companies investing in RE subsidiaries should have an adequate substance in order to benefit from dividend exemption rule.

Procedures of Calculation, Declaring and Paying the advance Corporate Income Tax (CIT)

Advance CIT due can be calculated based on result of the historic tax periods as follows:
- advanced CIT for the first six months of the tax period (I and II quarters) is calculated according to the CIT liability from the tax period which was before the last tax period (advance CIT for the first six months of 2019 is calculated according to the actual amount of CIT paid for the year 2017);
- advanced CIT for the seventh-twelfth month of the tax period (III and IV quarters) – according to the CIT liability of the previous tax period (advance CIT for the second half of 2019 is calculated according to the actual amount of CIT paid for the year 2018).

The annual CIT return should be submitted and tax should be paid until the 15th day of the sixth month of the next tax period.

The advance CIT return when CIT is calculated according to historic CIT liability, should be filed:
- for the first six months of the tax period – not later than on the 15th day of the third month of the tax period;
- for the seventh-twelfth months of the tax period – not later than on 15th day of the ninth month of the tax period.

Alternatively, advance CIT can be calculated based on forecasted annual CIT amount. In such case, the advance CIT return should be submitted and advance CIT should be paid not later than on the 15th day of the third month of the tax period.

Depreciation of Fixed Assets

The depreciation of fixed assets is calculated separately for each asset using the straight-line method, double declining balance depreciation method or production method. Generally, buildings may be depreciated over periods from 8 to 20 years (new buildings over 8 years), machinery and plant – over five years.

Land is not subject to tax depreciation.

Withholding tax on Sale of Real Estate

Income from the sale of real estate situated in Lithuania and derived by a foreign entity is subject to a WHT of 15%. WHT on income sourced in Lithuania must be withheld and paid to the state budget by both Lithuanian entities and permanent establishments in Lithuania.

Withholding Tax on Interest

Interest paid from Lithuanian companies to foreign companies established in the EEA or in countries with which Lithuania has a double tax treaty are not subject to WHT in Lithuania and no holding requirements are applied. In other cases 10% WHT is applied.

It is highly advised to analyse the facts thoroughly before applying withholding tax exemptions.

Deduction of Interest Expenses Limitation Rules: Thin Capitalisation and EBITDA

Interest on the debt in excess of the controlled debt-to-fixed-equity ratio of 4/1 is non-deductible for corporate income tax purposes if the company cannot substantiate that the same loan under the same conditions would be received from a non-associated party. This is applicable in respect of the controlled loans provided and/or third party loans guaranteed by a related party.

Additionally, as of January 1st 2019, a new interest limitation rule has been introduced. An entity is given the right to deduct interest costs exceeding interest revenue up to a 30% of taxable EBITDA or up to €3m. If an entity belongs to the group of entities, the above criteria shall be applied jointly for all Lithuanian entities and permanent establishments of foreign entities in Lithuania that belong to the same group. Restrictions do not apply if an entity's financial results are included in the consolidated financial results of a group, and the equity-to-asset ratio of that entity is not more than two percentage points lower than the equivalent ratio of the group. Interest costs exceeding interest revenue could be carried forward without time limitation. Mentioned rules do not apply to financial institutions and insurance companies.

Ensure compliance with thin capitalisation and EBITDA rules. If 4/1 ratio is exceeded, consider repayment of debts or increase of equity. Consider EBITDA deductibility restrictions.

Transfer Pricing

All related-party transactions have to comply with the arm's length principle. According to the Lithuanian transfer pricing regulations, companies may apply the following methods, although traditional methods should be given preference.

According to the new transfer pricing guidelines, in force from January 1st 2019, transfer pricing documentation consists of two files: 1) master file which describes inter-company transactions in the worldwide context of an entity's group and 2) local file which includes more detailed information and analysis about the local entity's inter-company transactions.

Local file should be prepared by all Lithuanian entities and foreign entities' permanent establishments with annual previous period's revenue exceeding €3m, as well as all banks, insurance companies and credit institutions (disregarding revenue).

Master file is mandatory if an entity belongs to the international group of companies and its previous period's revenue in Lithuania exceeds €15m.

Moreover, transaction threshold of €90,000 has been introduced. If an entity enters into multiple similar transactions with one associated party, the threshold is applicable for the total amount of all transactions with that party. If the transaction is inextricably linked to another transaction, the same threshold of €90,000 for the two transactions is applied jointly. No threshold is applied on transactions with associated parties that are registered or otherwise organised in black-listed territories.

Documentation can be in any language, however, tax authorities may request to provide official translations to Lithuanian.

Documentation should be prepared until 15th day of the 6th month after the end of the tax period when such transaction between associated parties took place. Additional transition 6-month period is provided for a preparation of Master File for transactions performed in 2019.

Transfer pricing documentation (including comparative data analysis) can be updated every three years if the terms and conditions of the controlled transactions do not change significantly.

Penalties, amounting from €1,820 to €6,000 for non-compliance with the transfer pricing documentation procedures for transactions between associated persons could be imposed for CEO of the company.

The arm's length principle should be duly followed and documented in order to avoid negative tax consequences.

Loses Carried Forward

Operating tax losses can be carried forward for an unlimited period of time. Losses incurred from the disposal of securities can be carried forward for a period of five years and can only be offset against income of the same nature. Only up to 70% of current year's taxable profits can be offset against tax losses carried forward. The carry back of tax losses is not allowed under Lithuanian law.

Check if there are any tax losses that can be carried forward.

Land Tax

Land tax applies on land owned by companies and individuals, except for the forest land. The tax base depends on the full average market value according to the mass valuation, which is performed not rarer than every five years. There is a possibility to apply the property value determined during the individual valuation if it differs from the market value by more than 20%.

Land tax rates range from 0.01% to 4% depending on local municipalities. Local municipalities must set tax rate before July 1st of the previous tax period. In Vilnius, the Land tax rates established for 2019 are:

- 0.08% – tax rate for individuals;
- 0.12% – tax rate for companies;
- 4% – for the land that is not used and for the land with buildings recognised as unauthorised construction.

As of 2020, tax rate for individuals and companies will be 0.12%.

The taxable period for land tax is the calendar year. Returns are sent by the State Tax Authorities to taxpayers by November 1st of the current year and the tax due has to be paid by November 15th of the current year.

Land tax rates in specific municipality should be followed in case of possible tax rate changes.

Land Lease Tax

Users of state-owned land are subject to land lease tax. The minimum tax rate is 0.1% and the maximum rate is 4% of the value of the land. The actual rate is established by the municipalities.

The taxable period for land lease tax is a calendar year. Tax due has to be paid by November 15th of the current calendar year.

Personal Income Tax

For local and foreign individuals sale of real estate located in Lithuania is subject to 15% PIT. Tax is levied on the capital gains, i.e. sales proceeds less acquisition costs (however, a foreign individual can achieve this only by submitting an additional request for re-calculation of tax to the Lithuanian Tax Authority, since initially the tax is calculated on the gross proceeds).

Income from rent of real estate located in Lithuania for local and foreign individuals is subject to 15% PIT on gross income. If rental income is received from registered individual activity, PIT is levied on the profits (income less expenses). Upon certain conditions, individuals can opt to pay a fixed amount of tax on rent of privately owned real estate once a year.

There is no separate gift tax applicable in Lithuania – the gifts received by individuals are subject to personal income taxation. Income received as gift from spouses, children (adopted children), parents (foster parents) brothers, sisters, grandchildren and grandparents, as well as income not exceeding €2,500 during the calendar year received as a gift from other individuals is non-taxable.

Procedure of Tax Return Filing

Taxpayers can submit tax returns only electronically.

14 Luxembourg

Corporate tax rate

The aggregate income tax rate for 2019 is 24.94% for entities registered in Luxembourg City:

- Standard corporate income tax rate is 17% for taxable income exceeding €200,001. Companies with a tax base of less than €175,000 benefit from a reduced rate corporate income tax rate of 15%. Companies with a tax base between €175,000 and €200,001 are subject to a corporate income tax of €26,250 plus 31% of the tax base above €175,000;
- Municipal business tax is also levied at rate generally varying from 6.75% to 10.50% depending on where the company is located (the municipal business tax rate is 6.75% if the company has its registered office in the Luxembourg City).

Luxembourg undertakings are also contributing to the Luxembourg employment fund for 1.19% of their taxable income (i.e. 7% rate assessed on the 17% income tax).

Losses carried forward

Tax losses incurred before January 1st 2017 may be carried forward indefinitely by the company that has incurred them.

Tax losses incurred as from FY 2017 may be carried forward for a maximum period of 17 years.

Tax losses cannot be carried back in Luxembourg.

Net Wealth Tax (NWT)

Companies resident in Luxembourg are subject to an annual Net Wealth Tax on their unitary value (net asset value) to be determined as at January 1st of each calendar year.

The following rates are applicable:

- for a unitary value up to and including €500m: 0.5%;
- for a unitary value exceeding €500m: 0.05% on the portion of the unitary value above €500m and €2.5m (i.e. €500m at 0.5%).

Some exemptions are available under the Luxembourg participation exemption regime (e.g. shares in certain companies) or by virtue of the applicable Double Tax Treaties (e.g. real estate located abroad).

The tax liability can in principle be eliminated or reduced if a specific reserve, equal to five times of the tax is created before the end of the subsequent year and maintained for the following five years.

Minimum Net Wealth Tax

A minimum NWT charge applies for all corporate entities having their statutory seat or central administration in Luxembourg. Such entities for which the sum of their fixed financial assets, transferable securities and cash at bank (as reported in their commercial accounts presented in the standard Luxembourg form) exceeds 90% of their total gross assets and €350,000, are subject to a minimum NWT charge of €4,815.

All other corporations might be subject to a minimum NWT ranging from €535 to €32,100, depending on the amount of their total assets as shown in the balance sheet.

Withholding Tax

There is no withholding tax on interest.

Generally, dividends are subject to 15% withholding tax unless the conditions of the Luxembourg participation exemption regime are fulfilled or more favorable tax treaty rates are available.

Liquidation proceeds paid by a Luxembourg company are not subject to withholding taxes in Luxembourg.

Director fees related to seating at the board are usually subject to a 20% withholding tax.

VAT

VAT Grouping implemented in Luxembourg

The VAT grouping legislation has been introduced in Luxembourg with effect from July 31st 2018 (via Law No 671 of August 6th 2018). Some of the feature of the VAT group include:
- Enhances consolidation for VAT purposes;
- Is an optional regime, choice is left to the taxpayer, but all-in or all-out, limited opt-out possibilities;
- Only Luxembourg resident companies and a local branch of a foreign company can join.
- Applicable for any sector/industry but the three following links need to exist simultaneously:
  - Financial links;
  - Economic links and
  - Organisational links.
- Members cannot be part of more than one VAT group;
- Must be set up for at least 2 calendar years.

Although this is a new regime in Luxembourg, VAT groups are already used in other jurisdictions as a way to mitigate irrecoverable VAT costs and cash flow effects on intra-group charges.

VAT and Transfer Pricing

The Luxembourg VAT law has been amended (via Law No 671 of August 6th 2018) to implement Article 80 of the EU VAT Directive with effect from July 31st 2018. This law aims at avoiding VAT loss by allowing the VAT authorities to disregard consideration agreed between related parties to retain the open market values under the following situations:
- When the consideration for a supply has been underestimated while the purchaser has a limited recovery right;
- When the consideration for an exempt supply has been underestimated while the supplier has a limited recovery right and
- When the consideration for a supply has been overestimated while the supplier has a limited recovery right.

Directors' fees

Since January 1st 2017, directors' fees paid to directors (private individuals) are subject to 17% VAT, based on the Circular issued on September 30th 2016. Since January 1st 2017, increase of the enforcement powers of the VAT authorities:
- Personal liability of the delegated administrators, directors and "de jure" or "de facto" managers is engaged in case of VAT underpayments/late payments/non-compliance with VAT law if it can be proved that they failed in the performance of their duties.
- General increase of penalties.

This Circular is under scrutiny, and may need to be modified, further to the Court of Justice of the European Union case law C-420/18 dated June 13th 2019.

FAIA requirement

The Luxembourg VAT Authorities may require certain VAT taxpayers to provide all the information necessary for their audit on an electronic structured audit file (the so-called *'Fichier d'Audit Informatisé de l'Administration de l'enregistrement et des domaines' – 'FAIA'*).

As a general rule and based on the guidance from the Luxembourg VAT Authorities, this FAIA file can be requested to (1) VAT registered entities under the normal regime and that are subject to the Luxembourg Standard Chart of Accounts and (2) which perform more than 500 transactions per year.

These requests are more and more frequent and the affected companies should ensure that they are able to generate the file and can provide it when requested since failure to provide may attract penalties.

Anti Tax Avoidance Directive (ATAD) I

On December 18th 2018, the Luxembourg Parliament voted for Bill (n°7318) (the 'Law'), implementing ATAD I in Luxembourg domestic law. The Law was published on December 21st 2018 and entered into force on January 1st 2019. The Law covers the following measures:

Interest limitation rules

The Law sets out new interest deduction limitation rules restricting deduction of "exceeding borrowing costs" up to a higher of i) 30% of the taxpayer's EBITDA or ii) €3m. Exceeding borrowing costs not deductible in a tax period may be carried forward without time limitation. Interest capacity which cannot be used in a given tax period may be carried forward for five years.

The Law also provides for a grandfathering to be applied to any loans granted to a Luxembourg company before June 17th 2016 and to the extent that these loans have not been modified since this date and will not be modified afterwards. Borrowing costs arising from long-term infrastructure projects (where the project operator, borrowing costs, assets and income are all in the European Union) are also excluding from the scope of the interest limitation rules.

Controlled foreign company rules (CFC)

The Law sets out new CFC rules targeting non-distributed income of CFCs arising from non-genuine arrangements, which have been put in place for the essential purpose of obtaining a tax advantage.

If a CFC is identified, the Luxembourg company may have to include totally or partially the non-distributed income earned by the CFC entity/-ies following a functional analysis.

Intra-EU anti-hybrid rule

The Law includes anti-hybrid provisions covering only intra-EU hybrid instruments and hybrid entity mismatches.

Based on the Law, where a hybrid mismatch (i.e. difference in the legal characterisation of a financial instrument or entity) or the commercial or financial relations between a taxpayer and an associated enterprise in different Member States give rise to a deduction of the same expenses/losses in both Luxembourg and the Member State where the expenses are originated (double deduction), or deduction in Luxembourg and non-inclusion of the corresponding income in the net revenues in the other Member State (deduction with no inclusion) such advantage will be eliminated either via a denial of deduction in the Member State of the recipient (in case of double deduction) or denial of the deduction in the Member State of the payer (in case of deduction without inclusion).

For the purpose of this provision an associated enterprise implies a 25% participation (in case of hybrid financing instruments) and a 50% participation (in case of hybrid entity) threshold in voting rights, capital ownership and profit entitlement.

General anti-abuse rule (‘GAAR’)

The Law aims at modernising the existing general anti-abuse rule as provided by the Adaptation Law. Under the Law, there is an abuse of law if the legal route which, having been used for the main purpose or one of the main purposes of circumventing or reducing tax contrary to the object or purpose of the tax law, is not genuine having regard to all relevant facts and circumstances.

Exit tax rules (will come into force on January 1st 2020)

The Law modifies the existing exit taxation rules and amends the existing taxation deferral rules to provide for a payment of tax in instalments over five years.

The payment of the Luxembourg tax arising on the gains upon transfer of assets outside Luxembourg in any of the circumstances listed in ATAD may be made in instalments over a period of five years. However, this is possible only where the transfer is to an EU Member State, or an EEA State with which Luxembourg has an agreement on the recovery of taxes.

Anti Tax Avoidance Directive (ATAD) II

On August 8th 2019, the Luxembourg Government tabled a Bill before the Luxembourg Parliament setting out draft legislation (the 'Draft Law') that will implement the EU Anti Tax Avoidance Directive regarding hybrid mismatches with third countries ('ATAD 2') into Luxembourg domestic law.

As anticipated by ATAD 2, the Draft Law will in general apply as from the tax years starting as from January 1st 2020, with the additional "reverse hybrid" measures that comprise Article 9a of ATAD 2 applying from the 2022 tax year.

The provisions of the Draft Law apply whenever there is a "hybrid mismatch" under:

1. a "structured arrangement" or
2. between "associated enterprises" or
3. between a head office of an entity and a permanent establishment or
4. between two or more permanent establishments of the same entity or
5. in cases of dual tax residence.

Essentially any link, where there is a 50% or more right to votes, capital ownership or profits, causes two entities, or an individual and an entity, to be associated enterprises (except in relation to payments under a financial instrument – here a threshold of 25% is sufficient to create an associated relationship).

In relation to the "acting together" concept, the Draft Law deals specifically with investors (either physical persons or entities) in an investment fund that own, directly or indirectly, less than 10% of the shares or units of the fund and are entitled to less than 10% of the profits of that fund. Unless demonstrated otherwise, any such investor in a fund is not to be regarded as "acting together" with any other investor. This means that in these circumstances any such "less than 10%" investor should not be "associated" with the fund vehicle, and as a consequence also not be "associated" with the entities the fund vehicle controls.

Hybrid mismatch definition

Deductions without inclusion

To the extent that a hybrid mismatch results in a deduction without inclusion, the deduction shall be denied for the Luxembourg payer or, as a secondary rule if the deduction is granted to the foreign payer, the amount of the payment shall be included as taxable income in the hands of the Luxembourg payee.

Double deductions

To the extent that a hybrid mismatch results in a double deduction, the deduction shall be denied for the taxpayer that is the investor. If the deduction is granted in the jurisdiction of the investor, the deduction shall then be denied for the taxpayer that is the payer. Nevertheless, any deduction shall remain deductible to the extent that there is dual inclusion income of that tax year. Furthermore, payments, expenses or losses which may not have been deductible in a given year may still be deductible subsequently, to the extent that dual inclusion income arises in a future tax year.

Imported mismatches, hybrid transfer and tax residency mismatches

- A deduction for a payment will be denied to the extent that it gives rise to an "imported mismatch". The Draft Law uses the exact same definition of an imported mismatch as that in ATAD 2;
- To the extent a hybrid transfer is designed to produce a relief from withholding tax on a payment derived from a transferred financial instrument to more than one of the parties involved, the relief will be limited in proportion to the net taxable income regarding the payment. Contrary to the general rule, the portion of a withholding tax that may not be creditable shall in this specific case not be deductible for Luxembourg tax purposes;
- The deduction will be denied to the extent dual residency results in double deduction. The payment, expense or loss will however remain deductible when the other jurisdiction involved is a Member State with a DTT in force with Luxembourg and provided the taxpayer is considered as a Luxembourg resident under that DTT.

Post 2021 reverse hybrid mismatches

With effect as from the 2022 tax year, Luxembourg transparent partnerships will become liable to corporate income tax in relation to net income, to the extent that such income is not otherwise taxed under the Luxembourg domestic tax law or the laws of any other jurisdiction, provided one or more associated non-resident entities i) holding in aggregate a direct or indirect interest in 50% or more of the voting rights, capital interests or rights to a share of profit in the Luxembourg partnership ii) consider the Luxembourg partnership to be a taxable person.

Draft Law confirms that, while the Luxembourg partnership will be considered as a tax resident for corporate income tax purposes, it will be exempt from Net Wealth Tax.

In line with the exclusion provided for in ATAD 2, collective investment vehicles are out of the scope of this provision. For the purpose of this rule, collective investment vehicles are defined as an investment fund or vehicle that is widely-held, holds a diversified portfolio of securities and is subject to investor-protection regulation in the country in which it is established. The Commentary clarifies that this definition includes undertakings for collective investment in the sense of the Law of December 17th 2010, specialised investment funds ('SIFs') covered by the Law of February 13th 2007, reserved alternative investment funds ('RAIFs') covered by the Law of July 23rd 2016, and other alternative investment funds ('AIFs') not falling within the above categories but covered by the Law of July 12th 2013 (implementing the EU AIFM Directive) relating to managers of alternative investment funds although only to the extent that such AIFs are widely-held, hold a diversified portfolio of securities and are subject to investor-protection regulations.

DAC 6 – Disclosure for certain cross-border arrangements

On August 8th 2019, the Luxembourg Government tabled a Bill before the Luxembourg Parliament setting out draft legislation (the 'DAC 6 Draft Law') that will implement the Directive (EU) 2018/822 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements (commonly referred as 'DAC 6').

DAC 6 makes it mandatory for intermediaries (or taxpayers, if there is no intermediary, or if intermediaries are subject to professional secrecy as defined by the Member States' domestic laws) to report some cross-border transactions and arrangements to the domestic tax authorities, and will trigger the subsequent automatic exchange of information to tax authorities of all EU Member States through access to a central directory.

The Luxembourg Government has opted to make a straightforward transposition of the Directive. As matters of example, no reporting will therefore be applicable in relation to purely domestic arrangements, and all taxes are in scope except VAT, customs duties, excise duties, compulsory social security contributions and fees for documents issued by the public authorities or consideration paid for public services.

Hallmarks and Main Benefit Test

Cross-border arrangements may be reportable if they meet at least one of the "hallmarks" set out in the DAC 6 Draft Law, which is identical in wording to the list of hallmarks in Appendix IV of DAC 6. These hallmarks may be generic or specific.

Generic hallmarks, and a number of specific hallmarks, may only need to be considered if they meet the so-called "main benefit test". This will be the case if obtaining a tax advantage is the main benefit, or one of the main benefits, that a person is expecting to derive from an arrangement. The DAC 6 Draft Law takes the position that the tax advantage may either be obtained in the EU or in a third country, and that it is an objective test.

Timing of reporting

Reportable cross-border arrangements whose first implementation step occurs between June 25th 2018 and July 1st 2020 are to be reported as from July 1st 2020, and by August 31st 2020 at the latest. As from July 1st 2020, there is a thirty-day turnaround period to report to the domestic tax authorities.

Transfer Pricing

Disclosure obligations

As from 2017 tax return, the following TP related information would need to be disclosed:
- if the Luxembourg company engages into transactions with related parties;
- if the Luxembourg company opts for the simplification measure stated in section 4 of the 2017 TP Circular (L.I.R. n° 56/1–56bis/1 of December 27th 2016).

As from 2018 tax return, Luxembourg entities are required to indicate in their tax return whether they have performed any transaction.

Development concerning Country-by-Country (CbCR) reporting

A grand-ducal regulation has been issued on March 18th 2019 (the *Mémorial* A N° 163), amending the revised grand-ducal regulation published on February 13th 2018. In case the ultimate parent is resident in a jurisdiction that is not listed in the mentioned regulation, a CbC report will have to be filed either by a "surrogate entity" resident in a jurisdiction listed in the grand-ducal regulation or by an affiliate in Luxembourg. Exceptions may apply, on a case-by-case basis, if countries mentioned in the regulation have CbC reporting obligations but starting from a different fiscal year. In case of CbC reporting and notifications finalised before the regulations, MNE groups shall review them to ensure they have been done in compliance with the list of "exchanging" jurisdictions listed in the regulations.

The grand-ducal regulations only indicate that exchange of information will take place from Luxembourg to each of the other jurisdictions listed. It is important to note that there are jurisdictions, which are exchanging CbC reports with Luxembourg, although Luxembourg may not be exchanging with such countries, i.e. so-called "non-reciprocal" jurisdictions. In case MNE groups have the ultimate parent company in such jurisdictions, the Luxembourg tax authorities may not accept that those groups can satisfy their CbC reporting obligations by using a Luxembourg group entity as a "surrogate entity" filing in Luxembourg.

Substance in Luxembourg

Over the past few years, we have noticed an emerging trend in various jurisdictions where portfolio companies are located, that tax administrations tend to challenge the actual substance of foreign holding companies.

According to Luxembourg income tax laws, a company is considered to be resident in Luxembourg, and therefore fully taxable therein, if either its registered office or central administration is located in Luxembourg.

To avoid the risk of challenge by other tax authorities, it is usually recommended that it can be evidenced that a Luxembourg company is effectively managed and controlled in Luxembourg and that minimum substance exists in Luxembourg (e.g. bookkeeping, phone line, etc.). In particular, with respect to the day-today management it is recommended to have at least one local director in charge of the day-to-day management with a real decision power (to be assessed in light of the decision power of the foreign directors).

Transfer pricing requirements related to the substance have been reinforced and highlight the need to have a majority of the board of directors tax resident in Luxembourg and that the personnel is sufficiently qualified to control the transactions performed.

15 Netherlands

Corporate Income Tax Act

Budget day

Corporate income tax rate

The CIT rate for the first €200,000 of profits is to be reduced to 16.5% in 2020 and 15% in 2021. The rate for profits over €200,000 however, will continue to be 25% in 2020 and will not be reduced to 22.55% as announced last year.
As of January 1st 2021, the top rate should be reduced to 21.7% rather than the 20.5% announced last year.

Amendment of liquidation loss rules

According to the consultation document, the deductibility of a liquidation loss is to be limited as from 2021.

For qualifying subsidiaries established in EU/EEA countries (territorial restriction), a deduction would only be allowed for interests of more than 25% (material restriction). For subsidiaries established in non-EU/EEA countries and/or for interests of 5%–25%, a liquidation loss should be deductible up to a maximum amount of €1m.

The liquidation loss can only be deducted if the settlement of the participation is completed within three years after termination of the business activities or the decision to that effect (temporal restriction). Similar rules will also apply with regard to the termination of a permanent establishment. The expectation is that both the above-mentioned percentage and the maximum amount will be increased in the future. There is no draft bill available yet. It is highly recommended to closely monitor any developments in this respect.

Conditional withholding tax on interest and royalties

Draft legislation for a conditional withholding tax on interest and royalty payments has been introduced to affiliated entities in:
- countries that do not tax profits or tax profits at a statutory rate of less than 9%,
- countries on the EU list of non-cooperative jurisdictions, or
- in tax abuse situations.

The withholding tax rate is equal to the highest CIT rate. As the law should enter into force on January 1st 2021, the 2021 CIT rate of 21.7% should apply.

It is expected that BVs/NVs, Coops and similar foreign entities (e.g. LuxCos) holding Dutch real estate may be in scope of the conditional withholding tax as withholding agents. It is therefore highly recommended to closely monitor any developments in this respect and carefully analyse whether the conditional withholding tax will apply in the relevant structure.

Amendments to substances rules

Under the Dutch Tax Budget 2020 it has been announced that a Dutch tax inspector can still determine that there is tax abuse, even though the Dutch substance requirements are met. This is in particular relevant in cases where an entity relies on the objective test of the i) Dutch CFC rules, ii) the substantial interest rules, iii) the dividend withholding tax exemption at source, or iv) in case of the new conditional withholding on interest. The impact thereof is further described below.

These amendments are a response to the so-called “Danish beneficial ownership cases” decided by the Court of Justice of the EU (CJEU) on February 26th 2019.

i) Impact on Dutch CFC rules

Pursuant to the implementation of ATAD I (2019), so-called CFC rules have been included in the CIT Act. In the event of genuine economic activities, CFC rules should not apply.

It is announced that the CFC rules would still apply if such CFC meets the Dutch substance requirements, but the inspector successfully determines that the main purpose, or one of the main purposes, is to apply the exception.

If CFCs do not meet the Dutch substance requirements, taxpayers will have an opportunity to demonstrate that the CFC carries out genuine economic activities. If they succeed in doing so, the CFC rules should not apply after all. In both cases, the Dutch tax authorities and the taxpayer can rely on the indicators of abuse included in the Danish beneficial ownership cases.

ii) The Dutch Dividend Tax Act

To apply the Dutch dividend withholding tax exemption at source, a company should demonstrate that:

- the interest in the Dutch company paying dividends is not held with the main purpose or one of the main purposes to avoid the payment of dividend withholding tax (subjective test); and
- there are sound business reasons that reflect economic reality (objective test).

Even though the objective test may be met if sufficient relevant substance is available, a tax inspector can still argue that there are no sound business reasons that reflect economic reality.

Vice versa, if the recipient of the dividend (i.e. the direct shareholder) does not meet the substance requirements, both the recipient of the dividends and the taxpayer have the opportunity to demonstrate that there is no tax abuse and the withholding tax exemption therefore should apply.

In both cases, the Dutch tax authorities and the recipient of the dividends or taxpayer can take guidance from the indicators of abuse included in the Danish beneficial ownership cases. Under the explanatory memorandum of the Dutch proposals, the presence or absence of economic activities may be based on all facts and circumstances. The following indicators are especially relevant:

1. the management of the company;
2. its balance sheet;
3. the structure of the costs and expenditure actually incurred; and
4. the staff that it employs and the premises and equipment that it has.

Furthermore, the economic activities must be relevant in the light of the holding of shares. The mere holding of shares does not classify as an economic activity, according to the explanatory memorandum.

iii) The Conditional withholding tax

A similar anti-abuse provision will be introduced for the conditional withholding tax as for the Dutch Dividend Tax Act as described above.

iv) The Substantial interest tax

A similar anti-abuse provision will be introduced for the Substantial interest tax as for the Dutch Dividend Tax Act as described above.

Measures to combat hybrid mismatches (‘ATAD 2’)

On Tuesday July 2nd 2019, the Dutch Bill implementing the so-called Anti Tax Avoidance Directive II (ATAD II) was submitted to the Dutch parliament. The Bill introduces measures countering the tax effects of “hybrid mismatches”. Such mismatches may result, for example, due to a difference in tax characterisation of an entity or a financial instrument between the two countries. This may result in a deductible payment that is, however, not included in the tax base at the level of the recipient. The Dutch ATAD II Bill aims to prevent this outcome.

The Bill therefore ensures that the EU Council Directive for the prevention of tax avoidance with regard to hybrid mismatches, ATAD II, is fully implemented into Dutch law.

If an entity within the structure is characterised differently by two different countries (e.g. structures involving transparent entities or US investors) it is highly recommended to assess the impact of the new rules of the proposed Bill.

The same applies if a certain investment structure, uses financial instruments that are characterised differently for tax purposes by different countries.

The draft legislation introduces a documentation requirement pursuant to which a taxpayer needs to substantiate why the hybrid mismatch measures do not apply. If a taxpayer does apply the hybrid mismatch measures in his tax return, the documentation must show how the hybrid mismatch measures have been applied.

Definition of permanent establishment/ permanent representative

A formal definition of permanent establishment and permanent representative is to be introduced which definition is in line with the OECD Model Tax Convention 2017. This definition will apply in non-treaty situations. The definition is applicable to corporate income tax, personal income tax and wage tax.

The law also explicitly stipulates that, in treaty situations, the Netherlands will use the definition of the term “permanent establishment” from the relevant tax treaty.

Earnings stripping rule decision

The earnings stripping rule, an interest limitation rule based on a taxpayer’s EBITDA, was introduced in 2019. On the basis of this rule, the (excess) non-deductible interest is carried forward to future years. This carried forward interest is determined in a decision.

The Tax Authorities are now given the possibility to revise the decision retrospectively, upon certain changes of ultimate interest in the taxpayer. This revision possibility is in line with the rules applicable to loss assessments.

Limitation of interest on corporate income tax

Currently, no interest is payable on corporate income tax due if a return is submitted within four months after the end of the tax year and if the final assessment is imposed in accordance with the return. Under the current scheme therefore, interest on tax can already be charged on the period before the end of the tax return deadline (six months). This is considered unfair and the scheme is now going to be changed so that interest on tax is only payable after six months.

Payment discount corporate income tax

Currently, if a provisional corporate income tax assessment is paid at once (as opposed to an optional payment in instalments), a payment discount applies. This payment discount for corporate income tax is to be abolished as of 2021.

Investment institutions

The Dutch government is currently investigating the possibility for Dutch investment institutions (REIT or *fiscale beleggingsinstelling* ['FBI']). Direct investments in Dutch real estate by so-called FBIs may not be possible in the future. The outcomes of current court decisions in this regard will be awaited and are to be taken into account in this investigation. Evaluation therefore is expected in 2021.

Landlord levy

Two conditional reduction measures are to be introduced to encourage social housing, which reductions reduce the landlord levy due.

Firstly, there will be a reduction to a maximum of €25,000 per new public sector rented home in a designated housing shortage area.

Secondly, there will be an exemption for new temporary homes (to a maximum of 15 years) which are intended for, among others, students, informal carers, residence permit holders and labour migrants.

DAC6 mandatory exchange of information

An obligation is to be introduced to exchange information with the Tax Authorities about certain cross-border advice. This obligation lies with (tax) consultants and in some cases taxpayers and is the result of European regulations.

The intention of this exchange of details is to enable EU Member States to amend their tax legislation and regulations in order to counteract these legal, but undesirable, cross-border structures.

This legislation may also influence behaviour because taxpayers may want to avoid constructions which fall under the scope of the information exchange. Put briefly, the proposed legislation relates to all taxes except VAT, import duties and excise duties. Although, the legislation will only come into effect as of July 1st 2020, it will largely have a retroactive effect to June 25th 2018.

Real Estate Transfer Tax

RETT Rate

Currently, the standard RETT rate is 2% for the acquisition of Dutch residential real estate and 6% for the acquisition of all other Dutch real estate. The 6% rate will increase to 7%. The government indicates to increase this rate by 2021, although the legislative proposal itself mentions the introduction by 2020. The effective date is therefore still unclear.

The reduced rate of 2% for the acquisition of Dutch residential real estate (or rights to which these are subjected) is not planned to be adjusted at this stage.

16 Norway

Rental income

Rental income in a Norwegian corporate investor is subject to the general Norwegian corporate tax rate of 22% (applicable rate as from the income year 2019).

Deduction for costs

All costs related to operation and administration of the property, including depreciation, are as a starting point deductible. This includes interest on loans obtained to acquire, maintain or improve the property (subject to general restrictions).

Depreciation

The acquisition of land and sites is not depreciable for tax purposes, but must be capitalised.

Buildings/assets used for business purposes will normally be depreciable in accordance with the declining balance method. The buildings/assets are allocated to different depreciation groups based on type of asset.

- Office buildings may be depreciated annually at a maximum rate of 2%.
- Buildings (other than office buildings), plants, hotels, rooming houses, restaurants, etc. may be depreciated annually at a maximum rate of 4%.
- Buildings with such simple construction that, from the date of its erection are assumed to have a useful life of no more than 20 years may be depreciated according to the declining balance method with a maximum rate of 10% annually.
- In addition unmovable equipment that serves the use of the building (e.g. as elevators, cooling plant) may be depreciated annually at a maximum rate of 10%.

Assess the allocation of building/assets within the relevant depreciation groups.

Maintenance costs and improvement costs

Maintenance costs are tax deductible in the year of accrual.

As a starting point, investments made on a property must be capitalised along with the building, building equipment or land to which it refers. The depreciation rate varies significantly depending on the building/asset.

In regard to improvements made for a specific lessee, depreciation depends on the ownership of the relevant improvements. If the lessee is considered the owner of improvements the lessee may depreciate the cost of improvements on a linear basis over the lease period (normally higher than the 2% on business buildings). Ownership of the improvements depend on an assessment of whether the lessor have had an economic advantage of the improvements.

Assess the tax treatment of maintenance costs and ensure proper regulation/treatment of costs related to lessee improvements.

Stamp duty

A 2.5% stamp duty is payable on the transfer of real property in Norway. The stamp duty is calculated on the sales value (i.e. the market value) of the property. There is no stamp duty on sublease of property, or on the transfer of shares or parts in limited liability companies or partnerships holding real property.

Tax exemption method

Capital gains on shares owned by a Norwegian limited liability company, which is comprised by the tax exemption method, are 100% tax exempt.

Furthermore, dividend distributions from a Norwegian subsidiary where the Norwegian parent company owns and controls more than 90% of the shares and voting rights, are also 100% tax free. The same applies to dividends from foreign subsidiaries within the EEA if the subsidiary is actually established and carries out genuine economic activity there (substance requirements based on the ECJ ruling in the Cadbury-Schweppes case).

Dividend distributions to a Norwegian parent company that do not meet the conditions mentioned above, will be subject to 22% tax on 3% of the dividends (effective tax rate of 0.66%).

Ensure more than 90% ownership and control in the holding structure within Norway to mitigate tax leakage of 0.66% on distributed dividends.

Property tax

From 2016 municipalities have had the option to levy property tax on real estate within their territory. The tax rate vary from 1‰ to 7‰ of the assessment value (market value) of the property. The assessment value is normally set for 10 years and there are restrictions on appeal against this assessment.

Many existing rent agreements have clauses pertaining to potential property tax. If a municipality introduce property tax, this may have significant impact on the income on properties within the territory.

Budget for property tax if the relevant municipality have introduced or announced an introduction of property tax. Furthermore, review existing rental agreements for possibilities to adjust the rent and the assessment value of the property.

Limitation of interest deduction

Norway has two sets of rules for limitation of the tax deductibility of interest expense, the first applying to each single entity and the other to groups. These rules apply where annual net interest expenses exceed a threshold amount of NKr5m per company. Where the threshold amount is exceeded, the right to deduct interests on debt to related parties is limited to 25% of taxable earnings before interest, taxes, depreciation, and amortisation (tax EBITDA). To be considered a related party, direct or indirect ownership or control by at least 50% is required. Please note that external debt backed by guarantees or security from related parties may be reclassified as internal debt.

In addition to the above, interest deduction limitation rules also applies to companies that are part of a consolidated group for accounting purposes, and limit interests to both related and unrelated parties. The threshold amount is NKr25m for the Norwegian part of the group as a whole. Where the threshold amount is exceeded, deductions are limited to 25% of taxable EBITDA. An equity escape applies to either to each Norwegian company separately, or to the Norwegian part of the consolidated group as a whole. In the first case, the equity ratio in the balance sheet of the Norwegian company is compared with the equity ratio in the consolidated balance sheet of the group. In the other case, the equity ratio for a consolidated balance sheet of the Norwegian part of the group is compared with the balance sheet of the group. In both cases, the Norwegian equity ratio must be no more than two percentage points lower than equity ratio of the group as a whole. A company qualifying for the equity escape clause may deduct its full interest expenses, except interest expenses to related parties outside of the group.

An adjustment under these interest limitation rules is likely to result in additional tax payable. However, current year tax losses may be offset against increased income. Disallowed interest expenses can be carried forward for 10 years.

Note that the interest limitation rules for Norwegian entities, interest limitation rules for Norwegian groups and the arm's length principle all operate alongside one another.

We recommend that the financing structure should be carefully considered in the light of the new interest limitation rules that entered into force in 2019. If covered by the interest limitation rules for 2019, it should be considered whether any measures could be taken to limit the non-deductible interest expenses.

Transfer pricing

All transactions between related parties have to be at an arm's length. Transactions that do not comply with the arm's length principle may be reclassified for tax purposes and result in penalty tax.

The arm's length principle should be duly followed and documented.

Tax consolidation

Norwegian tax law is based on the principle that each company is a separate taxpayer, irrespective of whether it belongs to a Norwegian or international group. However, Norwegian tax law allows for tax consolidation/group relief by way of group contributions.

A group contribution is a gratuitous and unilateral transfer of value from one taxpayer to another within the same group. In short, the group contributions allow a group company to offset its profits against tax losses in another group company.

There are three main conditions for rendering group contributions with tax effect:
- Both the rendering and the receiving company must be Norwegian limited liability companies (or certain other types of companies mentioned in the Tax Act). If certain conditions are fulfilled, group contributions may be rendered to/from a Norwegian permanent establishment (PE) of a foreign limited liability company tax resident in a state within the EEA area. Provided the conditions are fulfilled, Group contributions may also be rendered between Norwegian PE's of foreign limited liability companies, or to dormant Norwegian branches with a loss carried forward.
- The rendering and receiving taxpayer must be within the same tax group, i.e. a common parent (Norwegian or foreign limited liability company) must directly or indirectly own and control more than 90% of the shares and voting rights in both companies. The ownership test is made at December 31st in the income year.
- The group contribution must be lawful, e.g. be resolved in accordance with Norwegian Company law and be within the dividend distribution capacity of the rendering company (which sometimes requires careful planning upfront to make sure that the rendering company has sufficient dividend distribution capacity to give away its taxable profits as a group contribution).

If the above-mentioned conditions (and certain other minor conditions) are fulfilled, a group contribution is deducted from the rendering taxpayer's taxable income and is regarded as taxable income for the receiving taxpayer. The group contribution may exceed the rendering company's taxable income in the year in question; however, the part of the group contribution, which exceeds the year's taxable income, is not deductible, nor is it taxable for the receiver if the above-mentioned conditions (and certain other minor conditions) are fulfilled.

Group contributions are normally decided at the annual general meeting of the shareholders in the year following the income year. If the companies within the Norwegian group draw up statutory company accounts according to IFRS, careful long-term planning with respect to the group contribution capacity may be necessary.

Ensure more than 90% ownership and control of subsidiaries at year end to allow for group contributions with tax effect. Careful planning may be required to have distributable reserves available for group contributions.

Voluntary registration for VAT liable letting of premises

The lease of premises is as a starting point VAT exempt (without credit) in Norway. Letting of premises can however be subject to VAT if the lessor is voluntary registered for the lease of premises and the tenant uses the premises in VAT liable activity.

A lessor can either become voluntary registered for the lease of premises by filing an application to the tax authorities or by acknowledging that the company is voluntary registered by invoicing the tenant with VAT. The latter option, with acknowledging the voluntary registration, is only possible if the lessor already registered for VAT.

VAT on transaction costs

The tax authorities have traditionally been very restrictive on accepting deduction of input VAT on transaction costs.

The Directorate of Taxes has previously accepted VAT recovery on costs relating to the purchase of subsidiaries that are directly included in an existing VAT group. Furthermore, the Directorate also accepted VAT recovery on costs related to the sale of a subsidiary that has been part of the same VAT group as the parent company.

In a statement from the Directorate of taxes in December 2016, the above accepted deduction has been withdrawn and the Directorate of Taxes state that their new view is that there is no right for deduction of input VAT on transaction costs related to purchase or sale of shares and/or real estate.

Adjustment obligations/overview/agreement

Adjustment regulations for input VAT apply for capital goods investments. The regulations apply to immovable property where input VAT exceeds NKr100,000 and machines where input VAT exceeds NKr50,000. These rules may also apply to infrastructure.

The adjustment rules imply that there is a lock-in period of 10/5 years for input VAT deducted on investments in respectively immovable property/machines. If the VAT liable use of any premises/machines has changed during a year, such as from VAT liable to VAT exempt, then any liability to adjust VAT should be considered.

Mergers, demergers and acquisitions are deemed as a change in use of the assets and will, as a main rule, trigger an obligation to repay deducted input VAT in accordance with the adjustment regulations.

However, this can be omitted if written agreements on the transfer of adjustment obligations are made with the acquiring company (adjustment agreement). Such an agreement must be in place within the reporting due date for the VAT term when the merger takes place.

According to Norwegian VAT regulations, companies are also required to have an overview of investments subject to the VAT adjustment obligations. Such overviews shall contain certain specific information about the capital goods, VAT deducted, adjustment period, etc.

Lease of property – Tenant confirmations

For the lease of property, the lessor is required to collect a tenant confirmation. This confirmation should confirm, to which extent, the leased property is used in VAT liable or VAT exempt activity. This ensures good routines and control of the activity performed in the premises.

Tenant confirmations should be collected for all tenants at year end.

17 Poland

Mandatory Disclosure Rules

As of January 1st Tax Mandatory Disclosure Rules (MDR) were introduced in Poland. Polish regulations substantially extend the scope and obligations resulting from DAC6 Directive.

In general, “tax arrangements”, i.e. arrangements fulfilling so called “hallmarks” is subject to mandatory disclosure to Polish tax authorities. Some of the hallmarks require to be connected with tax benefit, while others do not. Namely, in case of “generic hallmarks” tax arrangements would be reportable provided that main (tax) benefit test is met. In the case of “specific hallmarks” and “other specific hallmarks” (the latter resulting from purely domestic legislation not provided for by DAC6), occurrence of hallmark will be sufficient to recognise a “tax arrangement” under Polish law (main benefit test is irrelevant in such case). This means that there may be frequent situations when an arrangement will not be classified as a reportable cross-border arrangement in other EU countries, whereas in Poland the same arrangement will be subject to disclosure.

Moreover, taxpayers having over PLN8m costs or revenues in previous tax year may be obliged to introduce internal MDR procedure.

Failure to report or other lack of internal MDR procedure may be connected with fines, up to PLN10m (approx. €2.3m) with respect to entities and at the same time up to PLN21m (approx. €4.7m) with regard to individuals responsible for such non-compliance.

Impact of the discussed changes on your obligations should be closely verified. In particular, it is recommended to analyse whether any of your transactions are reportable (based on our practice, real estate transaction often fulfil at least one of the hallmarks) as well whether internal MDR procedure is required for you. Should you require checks whether any of your on-going (or past) transactions are reportable, our dedicated MDR team may provide such support.

General guidance on transfer tax treatment of real estate transactions

Historically, property deals were typically structured as asset deals on a piecemeal basis (subject to recoverable VAT @23%). However, over the last few years, the tax authorities started to challenge the above treatment and reclassify such transactions into enterprise deals subject to Civil Law Activities Tax (thus denying recovery of input VAT). The above triggered a lot of confusion and uncertainty among investors as to how real estate deals should be structured from transfer tax perspective.

In December 2018, the Ministry of Finance issued a general guideline regarding transfer tax treatment of real estate deals. In the view of the general guidelines, the tax authorities seem to be leaning currently towards the classification of such deals as sales of assets on a piecemeal basis. At the same time, an “enterprise approach” should be seen as an exception to the above general rule (applicable only in specific cases).

Nevertheless, classification of commercial real properties is not clearly addressed in the law and there are technical arguments in favour of classification thereof as a going concern (enterprise or organised part thereof). Thus, structuring the transactions as asset deal is associated with potential reclassification of the object of transaction into a going concern deal. In such case the buyer is exposed to: i) risk of denial of input VAT recovery (23% of market value of the property; if this occurs after refund had been made, interest for late payment are charged on the amount to be repaid to the tax office), and so called VAT sanction (up to 30% of overstatement of the refund request) and ii) risk of assessment of Civil Law Activities Tax (CLAT @2% plus late payment interest).

Proper classification of the object of the transaction is crucial to identify tax implications and tax risks for the parties of the transactions. The guidelines are helpful for the analysis and increase the level of tax comfort; however, additional security measures (such as individual tax rulings or side letters) are still recommended to secure the position of the parties.

Withholding tax

Beneficial owner

Starting from 2019, a more restrictive definition of a beneficial owner has been introduced. According to new rules, a beneficial owner is an entity fulfilling the following conditions:
- receives a receivable (payment) for its own benefit and decides independently about the way of utilisation of the receivable (payment) and bears the economic risk due to the loss of the receivable (payment) in whole or in part; and
- does not act as an intermediary, proxy, trustee or another entity legally or factually obliged to transfer the mentioned payment in whole or in part; and
- conducts real business activity in the country of its registered seat, if receiving receivable (payment) is obtained within the business activity.

"Due care" obligations of the payment remitter

In line with new WHT regulations, the tax remitter is obliged to act with "due care" while applying reductions or exemptions resulting from double tax treaties/ EU Directives (including the verification of the beneficial ownership status/ business substance/business purpose of the payment recipient). The above "due care" requirements are applicable regardless of the amount of payment.

Anti-abuse rule

As of 2019 withholding tax exemption under EU Directives are not applicable if application thereof is contrary to the object and purpose thereof and obtaining tax benefit was the main or one of the main reasons of a transaction or series of transactions and activities were artificial.

Penalty payment

Changes to the WHT rules provide also for a penalty payment (so called 'WHT sanction') in the form of additional liability of 10% of the tax base of the payment, in relation to which the remitter applied a reduced WHT rate or did not collect WHT. Sanction covers cases where the remitter issued incorrect statement in reference to the possessed documentation and carried out verification/ remitter did not make the required verification with reference to WHT/verification performed was not adequate to the nature and scale of the remitter's activity.

The above sanction might be doubled in respect to the surplus over PLN15m (approx. €3,5m), if the payment exceeds PLN15m.

New WHT regime

As of January 1st 2020 new WHT collections regime will be applicable in relation to payments exceeding PLN2m (this new regime came into effect as from January 1st 2019, however its application has been already postponed twice by the authorities).

The general rule for such payments exceeding PLN2m (per recipient per year) would be that the tax remitters should withhold tax on such payments at a standard rate of 20%/19% (without automatically applying the exemption from WHT/reduced tax rate stipulated in the applicable Double Tax Treaty). Then, a procedure for reclaiming of the originally paid WHT should be available – subject to detailed check of the eligibility for beneficial WHT treatment by the tax authorities (with a waiting period for the refund of up to six months).

As an exception to the above general rule, the new mechanism allows the remitters not to withhold tax in relation to payments exceeding PLN2m per annum if:

- the remitter submits a statement confirming that i) he possesses all documents necessary for applying reduced WHT rate/exemption from WHT and ii) he is not aware of any circumstances which speak against granting tax exemption. The remitter will be held responsible for the completeness of the documents and correctness of the facts considered during the above process (fines and penalties under the Fiscal-Penal Code may apply). Moreover, an additional tax liability (as a rule – of 10%) may be imposed, if – during a tax audit – the tax authorities question the results of the certification process.
- alternatively, an opinion confirming the eligibility for beneficial WHT treatment is obtained. The opinion shall be issued within six months from the date of application at the latest and should be valid for 36 months. Application for the Opinion shall be subject to fee of PLN2,000.

For clarity, for payments up to PLN2m (approx. €460k) per annum, the remitter is entitled to apply withholding tax relief under standard rules (assuming conditions for reduced rate/exemption are met and that 'due care' standards are met).

Draft WHT guidelines/“Look through” approach

In the draft WHT guidelines issued by the Ministry of Finance in June 2019 it is stated that conduit companies, i.e. those not meeting the definition of BO, will not be entitled to DTT/directive benefits. However, the shareholders of such conduit companies might be able to benefit from WHT reliefs resulting from DTT/directives applicable to them, if they would be considered taxpayers with respect to the payments from a Polish entity and would meet the relevant conditions (e.g. would be the beneficial owners of the payment). Therefore, it may be argued that e.g. if the beneficial owner status of immediate shareholder is questioned, the payment of interest may still benefit from the WHT exemption/reduction under the terms that all the interest is transferred through this entity to upper level holding and such upper level holding is the beneficial owner of the funds. However, this approach is not yet clear due to lack of market practice and ambiguous wording of the draft guidelines. Monitoring of further practice in this area would be essential. Also, securing the applicability of this approach via tax ruling may be required.

Given the broad scope of changes and more restrictive regulations the possibility of applying exemptions or reduced WHT rates on payments to foreign entities should be closely verified. This may include i) comprehensive analysis of the structure aimed at identification of the beneficial owner or ii) obtaining an opinion confirming the entitlement to apply WHT exemption/reduced rate.

Also, taking into consideration that the amended regulations are relatively new, the development in the practice of tax authorities in this respect should be closely monitored. In particular, further guidelines are expected to be issued in this area by MoF (so far only draft version is available).

Minimum tax

Since 2018, minimum CIT on commercial buildings with initial value exceeding PLN10m (approx. €2.4m) was introduced.

The minimum tax is payable at 0.42% annually on an initial value of a building exceeding PLN10m. The minimum tax is in practice deductible against regular CIT – only excess of the minimum tax over regular CIT for a given tax year must be actually paid to a tax office.

As of January 1st 2019, the regime was slightly amended:
- minimum tax applies to all buildings subject to lease regardless of their type (not just office buildings and shopping centres);
- minimum tax applies only the parts of buildings actually subject to lease, i.e. vacant areas should not be subject to the minimum tax;
- the PLN10m threshold applies to a taxpayer regardless of the number of buildings owned (single exemption amount for a taxpayer for whole portfolio of buildings held);
- the exemption amount may be shared (decreased) with related parties in certain cases. The definition of a related party is not entirely clear. Based on the literal wording of these provisions, it seems that the threshold should be shared between the parties which are related due to capital links i.e. if one entity holds directly or indirectly at least 25% of the shares in the capital of other company;

- refund mechanism will be introduced allowing the taxpayer to apply to the tax authority **for a refund of the excess minimum tax** (i.e. excess of minimum tax in a given year over 'regular' CIT liability). The minimum tax shall be reimbursed if the tax authority confirms that there were no irregularities in the amount of "regular" CIT liability (in particular debt financing costs of the acquisition or construction of the building were in line with market conditions). This change also applies to the minimum tax for 2018. In our view, it is likely that the application for the refund of excess minimum tax will result in tax audit/checking activities in relation to the CIT settlements. Having in mind the wording of changes, the main area of tax authorities interest may be transfer pricing (arm's length level);
- targeted anti-abuse clause was implemented – transfers of assets or a conclusion of financial leasing agreement made with the sole purpose to avoid the minimum tax may be disregarded by the tax authorities.

Given the above changes, checking whether the refund of excess of "minimum CIT" is applicable in your case may be recommended.

White List

As of September 1st 2019, the provisions regarding the so-called white list became effective. One of the obligations arising from these regulations is to verify vendor's bank account number prior to making payment. Starting from January 1st 2020, error in the application of white list provisions will be the basis for imposing significant sanctions.

Pursuant to the provisions on the white list, before making payments under transactions exceeding PLN15,000, the taxpayer is required to verify that the bank account to which the payment is made is on the list kept by the Ministry of Finance (this applies to transactions with entities which are active VAT registered taxpayers in Poland).

Payment to an account not included on the list may have the following consequences:
- expenditure will not be considered a tax deductible cost,
- the buyer will be jointly and severally liable for the supplier's VAT obligations (in respect of payments made).

To avoid the sanctions indicated above, you must notify the relevant tax office within three days of making the transfer about the payment being made to a non-listed bank account.

It is recommended to implement effective procedures allowing you to meet of white list requirements on your future payments (including identification of whitelisted transactions, verification whether the bank accounts to which you make payments are included on the list, archiving the result of the check if the validation is positive or making a notification if the validation is negative, i.e. the bank account is not on the list). PwC is open to assist in applying the above changes.

Transfer pricing

Transactions concluded between related parties – both cross-border and domestic – should comply with the arm's length principle. Depending on the value of intercompany transactions, taxpayers may be obliged to report and prepare statutory transfer pricing documentation related to transactions exceeding certain thresholds on an annual basis. Failure to comply with this requirement may result in personal sanctions pursuant to penal fiscal code and in case of TP assessment in additional income subject to taxation at a rate of up to 49%.

As of 2019 changes to transfer pricing rules have been introduced. The new law grants the tax authorities additional tools. They are now able to re-characterise or even disregard related party transactions if they conclude that unrelated entities would not enter into transaction declared by the taxpayer or would conclude different transaction. Consequently, when assessing the arm's length level of remuneration in a given transaction, they could refer to other transactions or terms that in their opinion could have been applied by unrelated parties.

Safe harbors have been introduced for two transaction types, i.e. loans meeting specific requirements and low-value-adding services. In the case of the former, an official announcement on the arm's length level mark-up has been published. For the latter, a mark-up of 5% is recommended (less than 5% in case of acquisition of services and more than 5% in case of rendering services).

Also, obligation of documenting certain domestic transaction is limited. The local transfer pricing documentation does not have to include description of domestic transactions conducted between Polish taxpayers, who are not exempt from income tax, are not located in the special economic zone and do not incur losses. Certain other limitations from the transfer pricing documentation requirements are also provided.

New transactional materiality thresholds applicable for TP documentation (local file) have been introduced, i.e.
- PLN10m (approx. €2.3m for transactions concerning tangible assets and financing), and
- PLN2m (approx. €0.5m for other transactions).

The new thresholds should, in practice, result in reducing the scope of documentation requirements, especially for small and medium-sized taxpayers.

Materiality threshold for master file is set at PLN200m of consolidated revenue. According to the new regulations, the master file may be prepared in English. Translation into Polish will only be required at the explicit request of the tax authorities.

The scope of mandatory elements of transfer pricing documentation has also changed. In particular, taxpayers must present actual result achieved on a specific related party transaction (which will in most cases require segmentation of profit and loss account).

Benchmarking studies has now become a compulsory element of the documentation for each transaction described in a local file, except for those to which safe harbors apply. Until the end of 2018, benchmarking studies were obligatory for taxpayers exceeding the materiality threshold of €10m revenue or costs. If conducting such analysis is impossible, a taxpayer is obliged to prepare an analysis justifying compliance of the related party transaction with the conditions that would have been set by unrelated entities.

Taxpayers are also required to submit a new electronic form (TP-R form), which replaces the previous CIT-TP/PIT-TP reporting forms. Taxpayers are now obliged to explain any discrepancy between the actual results achieved on related party transactions and results of relevant benchmarking studies.

The new requirements oblige taxpayers to submit a statement to the tax authorities confirming that 1) the transfer pricing documentation had been prepared and 2) related party transactions described therein had been conducted according to the arm's length principle. The statement must be signed by all management board members. Submission of a false statement may lead to personal fines. The deadline for filing a statement on the preparation of local transfer pricing documentation is permanently extended to nine months after the end of the tax year for local documentation. The deadline for preparing the master file is 12 months after the end of the tax year.

Given the very broad scope of changes in the area of TP, it is highly recommended to monitor them closely in order to ensure that you comply with all the new obligations and requirements.

18 Portugal

Losses carried forward

Tax losses can be used to offset taxable profits arising in the following 5 years. No carry back is allowed. Deduction of tax losses is limited to 70% of the taxable profit of the year, with the possibility of carrying forward the remaining 30% within the carry forward period. Furthermore, rules regarding the utilisation of carry forward tax losses under the FIFO method were revoked.

No tax losses carry forward is allowed for the purpose of assessing the local and state surtaxes.

Any direct transfer of more than 50% of the share capital or of the majority of voting rights of a company in Portugal may lead to the loss of the tax losses carry forward generated prior to the acquisition year of that same company. Exemptions apply in the case of intra-group corporate restructurings. Otherwise, waiver of such rule may be available (restrictive requirements).

Within 30 days following the transfer of shares, transfer of the majority of voting rights, it may be necessary to file a request with the Portuguese Ministry of Finance.

It is recommended to explore structuring alternatives where you intend to reorganise your investment structure.

Dividends distribution

Dividends can be exempt from WHT under the application of the domestic participation exemption regime, if the following conditions are met:
- The Portuguese company is subject and not exempt from CIT and it is not subject to the tax transparency regime;
- The beneficial owner of the income is an entity resident i) in other EU Member State, ii) in other EEA Member State (provided such EEA Member State is bound by an agreement for tax cooperation within the scope agreed within the EU), or iii) in a country that has a DTT concluded with Portugal that foresees the exchange of information;
- The beneficial owner is subject to and not exempt from a tax mentioned in the EU Parent-Subsidiary Directive, or a tax of a similar or identical nature to Portuguese CIT (for non-EU cases) and it cannot be 60% lower of the Portuguese CIT rate, i.e., currently, 12.6%;
- The entity that pays the dividends cannot be resident in an blacklisted jurisdiction;
- Minimum shareholding held for a consecutive period of one year; and
- Shareholding threshold of at least 10%.

This regime is applicable to both EU and non-EU residents. It is recommended to verify if all the above mentioned conditions are met before approving a dividends distribution.

Despite the above, the WHT exemption on dividends is not applicable in case of structures or constructions that are mainly or exclusively tax driven, i.e., aimed to reduce, defer or avoid taxation which would be due otherwise and do not have a business purpose or economic rationale.

Transfer Pricing

All related-party transactions have to comply with the arm's length principle. Failure to present appropriate documentation to the tax authorities may result in the challenging of such transactions and penalties for tax purposes.

Additionally, companies with net sales and other income of €3m or more (with reference to the previous fiscal year) should prepare the transfer pricing documentation file.

The arm's length principle should be duly followed and documented.

Interest Capping Rules

Net Financial Expenses (NFE)'s deduction is capped at the higher of a fixed cap of €1m or a variable cap of 30% of the sum of the tax result (either profit or loss) plus NFE and allowed depreciation and amortisation of the year. This rule covers indebtedness with both related parties and independent parties, as well as between resident and non-resident entities.

The concept of NFE includes, among others, the depreciation or amortisation charge related to interest capitalised in the acquisition or construction cost of the assets.

The part of the NFE that is not deductible can be carried forward over a period of five tax years, as long as the capping is complied with.

When the amount of the NFE considered CIT deductible is lower than the 30% cap, the immediate and successive carry forward of the unused limit is allowed to be added for the calculation of the 30% cap for the following five tax years, until the total amount is used.

In case of fiscal unities, the parent company can elect for this rule to be applicable on a group basis, that should be kept for a period of three tax years.

There should be in place a control of the amounts of non-deductible NFE and unused 30% that can be carry forward for five years.

Cross-border financing

As a general rule, interest due to non-resident entities is subject to WHT in Portugal. Reduced WHT may be available when the beneficiary can apply a DTT and WHT full exemption may be available under the Interest and Royalty Directive provisions, provided that all the requirements foreseen in the directive are met.

Financing is also subject to stamp tax, although some stamp tax exemptions are available.

Some alternatives may be structured to mitigate the WHT and/or the stamp tax issues on cross-border financing.

Careful analysis of the tax impact of the various financing alternatives should be sought beforehand.

Real Estate Municipal Taxes (IMI)

IMI is due by the real estate owner on December 31st of each year (and paid in the following year). IMI rates range between 0.3% and 0.45%.

IMI rate for real estate held by entities resident in blacklisted jurisdictions is 7.5%.

Municipalities can increase the IMI rate applicable to urban real estate properties, when vacant for more than two years and located in designated areas of urban pressure.

In this situation, the IMI rate can be increased six times. An additional increase of 10% in each of the following years is also possible. However, it is capped at 12 times of the applicable IMI rate.

In case a direct investment is completed before the end of 2019, it should be taken into consideration that the owner of the real estate is responsible for the payment of the amount for the entire year (and not only from the period after the real estate is acquired) on December 31st 2019. The IMI impact will increase in case the owner of the real estate (corporation) of the real estate is resident in blacklisted jurisdiction.

Real Estate Taxes

Additional to the IMI (AIMI) is due on residential property and plots of land for construction.

The owners, usufructuaries, surface rights or undivided inheritances of residential property and plots of land for construction as at January 1st of each year, are liable to the payment of AIMI.

In the case of real estate financial leases, lessors are not allowed to charge the AIMI on the lease payments, if the tax registration value of the property does not exceed €600,000.

For companies, the AIMI rate is of 0.4% of the sum of the tax registration value of all applicable urban properties held by each taxpayer, reported as at January 1st of each year.

AIMI rate for real estate held by entities resident in blacklisted jurisdictions is 7.5%.

Properties that benefited from IMI exemption in the previous year are excluded from AIMI taxable basis.

CIT tax credit

Taxpayers have the option of deduct the AIMI paid, limited to the fraction of the tax corresponding to the income generated by properties subject to AIMI, in the scope of lease or accommodation activities.

AIMI is assessed by the Portuguese tax authorities in June of each year, being the respective payment made in September.

AIMI is due in case of owing residential property and plots of land for construction. The tax basis is the same as per IMI, i.e., the tax registration value.

Value Added Tax (VAT) claw-back rules

In the case of recovery of input VAT related to the construction or acquisition of real estate, and where a subsequent VAT-exempt transaction is entered into (e.g. a VAT-exempt lease agreement), VAT claw-back rules are triggered, and thus a VAT payment back to the Revenue is required. Other situations may also trigger the VAT claw-back rules. If so, they all should be included in the December VAT periodical return (filed and paid by February of next year).

Under the VAT claw-back rules, it is also required to pay VAT back to the Revenue whenever real estate is vacant for a period of more than five years. However, in February 2018, the ECJ ruled that this rule is against the VAT Directives to the extent the taxpayer is able to demonstrate its intention to lease the property. Although the Portuguese legislation has not been changed to reflect this decision, companies can consider following such court decision.

Before year-end, it should be verified whether the VAT claw-back rules will be triggered and, if so, the correspondent VAT adjustment should be paid back to the Revenue in February of the following year.

Capital Gains

Capital gains realised by non-resident entities with the sale of shares in a Portuguese company whose assets are comprised in more than 50% by real estate located in Portugal, are subject to tax at 25% therein.

Are also liable to tax at 25% in Portugal the capital gains, whenever they result from the transfer of share capital or similar rights in any entity (non-resident in Portuguese territory) when, in any given time in the past 365 days, the value of those shares or rights result, directly or indirectly, in more than 50% of immovable property or rights in rem over immovable properties located in Portugal, excluding agricultural, industrial and commercial activities but not buy-sell of real estate.

It is recommended to explore structuring alternatives where you intend to sell shares in real estate companies or to reorganise your corporate structure.

Real Estate Investment Trusts (SIGIs)

REITs were introduced in Portugal with effect from February 1st 2019, following similar REIT models implemented in Europe.

SIGIs, with tax residence and place of effective management in Portugal, are joint-stock companies (‘sociedades anónimas’) with the minimum share capital of €5m.

It is possible, upon decision of the general meeting, to convert already existing real estate companies into SIGI.

Additionally, SIGIs shares must be listed on a regulated market in Portugal, in another EU Member State or in an EEA Member State (which as committed to administrative cooperation in tax matters similar to those in the EU), within one year following its incorporation date.

SIGIs have a free float requirement of 20% from the end of the 3rd year after their admission and from the 5th year onwards, this requirement increases to 25%.
SIGIs must have as main activity:
1. acquisition of real estate, surface rights and/or other real estate rights for letting;
2. acquisition of shares in the capital of other SIGIs or companies resident in Portugal or in another EU Member State, EEA Member State, under certain conditions;
3. acquisition of units or shares in Collective Investment Vehicles (CIV), specialised in residential letting, governed by Portuguese law having similar profit distribution rules.

SIGI's portfolio must be comprised by real estate and investments in real estate entities representing at least 80% of the total assets and by real estate let or allocated to other atypical contractual forms related to the granting of the use of space in properties, which may include the provision of services, representing at least 75% of the total assets.

Both real estate assets and shareholdings above-mentioned must be held for at least three years from their acquisition date. Additionally, SIGI's indebtedness cannot exceed, at any time, 60% of their total assets.

SIGIs must distribute 75% of their annual profits and 90% of their annual profits that derive from dividends and other income from shares held in real estate entities.

Regarding the applicable tax regime, SIGIs are subject to the same tax regime as the one applicable to regulated real estate investment vehicles (i.e., CIVs), as follows:
- Subject to corporate income tax at 21% (but not to local and state surtaxes) and exempt on investment income, rental income and capital gains tax. Additionally, expenses related to these income categories are not deductible;
- Income from profit distributions is subject to WHT at a final 10% rate for non-resident investors and 25% and 28%, as payment on account, for resident entities and resident individuals, respectively;
- Income or gains arising from distributions, share redemption and sale and purchase of shares are deemed to derive from immovable property located in Portugal, so Portugal may retain its taxing rights under DTT.

As SIGIs are subject to the tax regime applicable CIVs means that there will be no tax differentiation in the choice between these investment vehicles.

The fact that this regime allows, under certain conditions, existing joint-stock companies and certain types of real estate investment companies to convert into SIGI broadens out the opportunities for their use.

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Exceeding borrowing cost capping rules

Following the implementation of ATAD 1 in the Romanian tax legislation on January 1st 2018, the deductibility of exceeding borrowing costs incurred in a fiscal period is capped, as presented below.

Definitions of key concepts:

- Cost of debt includes interest related to any type of debt, other equivalent costs from an economic perspective (e.g. payments related to profit participating loans, convertible bonds, zero-coupon bonds, financial leasing, interest capitalised from an accounting perspective in an asset value/ depreciation related to the interest component that was capitalised, derivatives or hedging instruments, guarantee commissions, etc.
- Exceeding borrowing costs represent the difference between any debt-related costs, in connection to both loans granted by financial institutions or intra-group entities – including, but not limited to: interest and foreign exchange expenses, capitalised interest, intermediation fees, commissions, etc. – and income from interest and other equivalent income from an economic perspective.
- The computation base (adjusted fiscal profits) is determined as revenues minus expenses recognised as per accounting rules, minus non-taxable revenues, plus the CIT expense, exceeding borrowing costs and deductible tax depreciation.

Limitation of exceeding borrowing costs:

2018: Two thresholds applied: €0.2m plus 10% of the computation base (adjusted fiscal profits).

The fix cap was applied only if the computation base was positive and greater than zero. Otherwise, exceeding borrowing costs are non-deductible during the current tax period, but can be carried forward indefinitely and deducted subject to the above deduction tests yearly.

2019: The above thresholds were increased starting January 1st 2019 to €1m and 30% adjusted fiscal profits, and the fixed cap of €1m applies irrespective of whether there is a negative/positive computation base.

The above limitation rules apply to any type of maturities (i.e. long-term/short-term) and any type of loans, i.e. intra-group or external loans (including bank loans), as well as to interest and net FX losses carried-forward from previous years and computed based on Fiscal Code provisions in force by December 31st 2017 (i.e. thin cap and interest cap rules)

No limitation applies if the debtor is an independent enterprise (i.e. is not part of a group performing consolidation for financial accounting purposes, has no related parties and no permanent establishments).

Holding legislation

Although there is no Romanian holding legislation, specific holding tax incentives (i.e. participation exemption rules) apply in Romania starting January 1st 2014.

Dividend income obtained by a Romanian holding company from a Romanian subsidiary is non-taxable (no condition).

The same incentive applies if dividend income is obtained by the same Romanian holding company from a non-resident subsidiary situated in i) an EU member state, as well as ii) in a non-EU member state with which Romania concluded a Double Tax Treaty (DTT) if some holding conditions are met (e.g. minimum 10% stake held directly for at least one year at the date the dividend income is booked from an accounting perspective; this is usually the dividend distribution date).

Capital income derived by i) a Romanian holding company from the disposal of shares in a Romanian/DTT state based subsidiary, as well as by ii) a non-resident located in a state Romania has a DTT with, further to the disposal of shares in a Romanian subsidiary, are also non-taxable if the above participation exemption criteria are met.

Liquidation income derived by a Romanian holding company further to liquidating a resident/DTT state based entity is non-taxable, subject to the same participation conditions referred to above.

Withholding tax exemption

Outbound dividends paid by Romanian legal entities to other Romanian legal entities or other EU member state based entities are subject to a standard 5% dividend tax, respectively 5% Withholding Tax (WHT) rate, unless the participation exemption conditions are respected.

Participation exemption applies and no tax is due at source if holding conditions are met (e.g. minimum 10% stake direct held directly for a minimum one-year period). A potential 5% tax withheld prior to observing these conditions can be refunded once the exemption rule kicks-in. Beneficial ownership requirements are also observed.

The second mechanism to reduce the 5% WHT in case of non-Romanian dividend recipients relies on applicable DTT, most DTTs concluded by Romania do not offer currently more favourable conditions than the 5% domestic tax.

There is no dividend tax on income paid by a Romanian legal entity to privately managed and optional pension funds.

Outbound interest and royalties paid by Romanian legal entities to other Romanian legal entities are not subject to tax at source.

Interest and royalties arising in Romania and beneficially earned by another EU/EEA (e.g. Switzerland, Liechtenstein, Norway) member state entities are WHT exempt in Romania, provided a direct minimum 25% stake in the Romanian income payer's share capital is held for an uninterrupted minimum two-year period at the payment date. These provisions apply to direct payments made between affiliated companies or between sister companies (e.g. companies with common shareholder having a minimum 25% stake). Otherwise, 16% domestic WHT applies or the more beneficial rate provided under eligible DTT. A potential WHT applied prior to observing these conditions can be refunded once the exemption rule kicks-in.

As a rule, 16% WHT applies to Romanian-sourced gross interest income. As of June 1st 2015, non-residents from EU/EEA member states concluding a DTT with Romania can register as Corporate Income Tax (CIT) payers in Romania and opt for the net basis taxation, i.e. they can reduce their initial WHT liabilities by claiming expenses (e.g. refinancing costs, foreign exchange losses, commissions, operational costs, all strictly in regards to the transaction generating the Romanian sourced interest that is payable by the Romanian tax resident), against the interest income. 16% CIT tax would thus apply on the fiscal profits derived from Romania. Any WHT paid in excess of the CIT such assessed may be claimed subsequently. To do so, non-residents can appoint a tax agent in Romania.

There is also a 50% WHT rate applicable if income is paid to a state with which Romania has no exchange of information treaty and the income is connected to an artificial transaction.

Anti-abuse rules

There are standard anti-abuse rules consisting in the substance over form principle, anti base erosion, transfer pricing aspects, as well as mandatory exchange of information.

The **substance over form** rule implies that the tax authorities may disregard a transaction which does not have an economic purpose, by adjusting its tax effects, or they may reclassify the form of a transaction/activity in order to reflect its economic content. The principle also includes the definition of cross-border artificial transactions, which are excluded from the application of DTTs.

Moreover, these provisions may be coupled with anti-abuse rules for preventing unlawful tax practices, aimed at obtaining tax benefits contrary to the principles of the EU Parent-Subsidiary and Interest and Royalties Directives.

On this note, the Romanian dividend tax exemption further to implementing this Directive in the domestic legislation does not apply to hybrid instruments (i.e. amounts qualifying as dividends in the paying entity's jurisdiction have an interest nature in the recipient's jurisdiction).

Additionally, the Romanian interest and royalties WHT exemption further to implementing this Directive in the domestic legislation does not apply unless the beneficial ownership aspect is not considered, or for interest/royalties payments performed in excess of the market level, etc.

The **anti base erosion rules** comprise the excess borrowing costs rules presented in the above section.

Transfer pricing rules apply to related party transactions, which must be done at arm's length, in comparable situations to third parties.

The provisions of the **Directive on administrative cooperation in the field of taxation as regards mandatory automatic exchange of information in relation to reportable cross-border arrangements (DAC6)** have not been implemented yet in the domestic tax legislation. Once transposed, the obligation to disclose specific transactions to the respective tax authorities will arise, in order to detect potentially aggressive tax arrangements. Romania has time until December 31st 2019 to implement such rules in its domestic legislation, but given the inclusion of a retroactive clause, in practice it has to apply these provisions as of June 25th 2018.

Last but not least, the **Multilateral Instrument (MLI)** was developed further to Action 15 of BEPS Action Plan with the aim of ensuring a fast implementation of measures included in the other actions of the plan. MLI supplements and "modifies" existing bilateral or multilateral tax conventions (not override nor substitute for them). Romanian has signed the MLI and may produce effects for most DTTs concluded by Romania. Any developments in this respect should be followed closely in order to assess their impact on current and future investments in Romanian companies through non-resident vehicles.

Losses carried forward

Fiscal losses accumulated starting with the fiscal year 2009 can be carried forward for seven consecutive years. The recovery of the annual fiscal losses is made in order of their registration, at each payment term of profit tax.

Also, losses can be carried forward in case of company reorganisations (spin offs, mergers). Therefore, tax loss refresh opportunities may arise.

Tax credits/Avoidance of double taxation

Romanian taxpayers (e.g. Romanian tax residents and/or Romanian permanent establishments) that are subject to corporate income tax both on the territory of Romania and in the foreign state with which Romania concluded a DTT (e.g. via a permanent establishment, or WHT) have the right to deduct from the corporate income tax due in Romania the corporate income tax and/or the WHT paid abroad, if the DTT agreement provides as a method of avoidance double taxation the credit method.

The tax credit is granted if the following conditions are cumulatively fulfilled:
- the provisions of the DTT concluded between Romania and the foreign state in which the tax was paid applies;
- the tax paid abroad does not exceed the domestic 16% corporate tax;
- the tax paid abroad, for the income obtained in the foreign state, was actually paid by the taxpayer;
- the income for which tax credit is granted is part of income categories subject to corporate income tax.

Tax prepayments

Corporate income tax is generally declared and paid on a quarterly basis, with annual reconciliation.

Exceptions apply to some categories of taxpayers, such as banks, which are obliged to estimate, declare and prepay the annual CIT liability also on a quarterly basis, but based on the prior year CIT liability. The interim estimation that is settled quarterly is reconciled annually versus actual current year results.

The rest of taxpayers may opt for the same tax prepayment system. Once the option is made, it becomes mandatory for at least two consecutive fiscal years.

Accounting and fiscal period

The standard accounting and fiscal period is the calendar year.

However, companies may opt for a fiscal year that is different from the calendar year, if the parent has a different year. The first amended fiscal year also includes the previous period of the calendar (i.e. January 1st – the day preceding the first day of the amended fiscal year), representing a single fiscal year. Taxpayers have to communicate to the territorial fiscal authorities the change in the fiscal year at least 15 calendar days after the start of the amended fiscal year.

Tax incentives

There are several tax incentives provided to Romanian taxpayers. The most relevant ones for real estate investors are presented below.

Recent tax incentives introduced for the real estate sector

Entities in the real estate sector with expressly mentioned NACE codes (e.g. developers, constructors, architects, etc.) and acting as employers may benefit during January 1st 2019–December 31st 2028, from 10% income tax exemption and partial social security charges exemption. The downside is that such real estate entities are obliged to pay an increased minimum gross wage of RON3,000 per month for 2019.

Reinvested profits in certain assets that are used for business purposes is CIT exempt.

Such assets include, for example, new technological equipment (machinery, tools and working plant), computers and peripheral equipment, machines and cash registers, control and billing and software products and starting 2017, rights to use software (either developed or acquired).

Some conditions must be followed, such as: the asset must be new, it cannot be depreciated by using the accelerated depreciation method, the asset must be held by the taxpayer for at least half of its useful life and maximum five years.

Fiscal depreciation

Some asset categories, can be depreciated faster for tax purposes using the accelerated or declining balance depreciation method, in addition to the straight-line depreciation. For example, buildings can be depreciated only straight-line, whereas equipment, computers and peripherals may benefit from all types of depreciation methods. More details are included below.

Depreciation methods for movable fixed assets

Movable fixed assets can be depreciated using the straight-line method, but also the reducing balance method or the accelerated method may be used.

Under the reducing balance method (or digressive depreciation), depreciation is computed by applying a coefficient of 1.5, 2 or 2.5 to the straight-line depreciation rates, depending on the useful life of the asset (i.e. between 2–5 years, between 6–10 years and more than 10 years, respectively). Their useful life generally varies between 4 and 15 years depending on the type of the machinery (please note that for more specific industrial machinery the useful lives can vary outside this limit).

Under the accelerated method, depreciation in the first year is up to 50% of the acquisition costs, although taxpayers usually go for 50% in year one. The straight-line method is used for the remaining 50% of the remaining useful life of the asset.

Revaluation of real estate property

Revaluations are recognised for tax purposes, unless they generate value decreases below initial recognition value.

Companies are required to treat part of the revaluation reserve built by revaluations performed starting January 1st 2004 as a taxable item together with each depreciation of revaluation surpluses (quarterly) or with the asset expense (if the asset is sold or written off).

Property taxes

Building tax

Starting January 1st 2016, building tax will follow property status (residential vs. nonresidential properties, or mix purpose building). Based on this criterion, different percentages apply:
- for residential building: 0.08%–0.2%;
- for non-residential building: 0.2%–1.3%;
- for non-residential buildings owned and used by legal entities in agricultural activities: 0.4%.

For non-residential buildings, the taxpayer may revalue the property every three years by commissioning an interdependent authorised valuator. Such revaluation must not be reflected accounting wise and is performed on the basis of specific valuation standards approved only for tax purposes, which may trigger different tax values by reference to fair values and accounting values. Not exercising the right to revalue the assets will result in higher taxation percentage, i.e. 5%.

Building tax rates may be increased by up to 50% based on local tax authority decision.

Changes in the building legal title do not attract further local taxes. The local taxes are owed for a full year by the owner of the building as of December of the previous year.

The owner of more than one residential building will no longer be taxed differently.

Land tax

Land tax is a fixed value per square metre, which is set by the local council depending on various factors (e.g. surface, type of settlement, rank, location, etc.)

Both building and land taxes are paid in two instalments, by March 31st and September 30th.

Exemptions:

Some categories of immovables are exempt from local tax, such as:
- buildings and land located in industrial parks, scientific and technological parks, in business incubators (in compliance with state aid legislation)
- buildings that are classified as historical monuments are related land
- buildings used for sports activities are related land
- Silos, greenhouses, solaria and other similar immovables that are used in the agri-business are related land
- buildings located in ports and those destined for navigable canals and pumping stations destined for the canals (except for rooms used for economic activities)
- highways

Transfer pricing rules

The Romanian transfer pricing rules are aligned with OECD principles. Transfer pricing rules require that transactions between domestic and cross-border related parties (defined as having a minimum 25% direct or indirect shareholding or common control) be carried out at market value, otherwise adjustments may be performed.

Failure to present appropriate documentation to the tax office may result in the non-acceptance for tax purposes of group charges and penalties.

Effective January 1st 2016, contemporaneous Transfer Pricing Documentation (TPD) requirements have been introduced for large taxpayers performing related party transactions above specific materiality thresholds. Such TPD rules must be met by March 25th of the year following the one transactions were done.

Special construction tax

As of January 1st 2014, a tax was imposed on certain categories of constructions. The level of this tax was increased in 2015 by 1% from the value of the constructions recorded in the taxpayer books as at December 31st of the previous year. The tax does not apply anymore starting January 1st 2016.

Transfer of business

As of January 1st 2016 the amendments applicable to domestic mergers, total or partial spin-offs, transfer of assets and exchange of shares are harmonised with those applicable to similar cross-border transactions. These amendments exclude the neutrality of the contribution in kind to a company’s equity, except for cases where a transfer of a going concern takes place.

Also, transfers carried out during a partial spin-off will be neutral for corporate income tax purposes only if a transfer of a going concern takes place, the transferor maintains at least one line of activity and shares are issued in exchange; certain specific conditions apply and must be observed.

Micro-company tax regime

Starting with January 1st 2018 a micro-enterprise is a Romanian legal person that cumulatively satisfies the following conditions on December 31st of the preceding fiscal year:

- obtained incomes that have not exceeded the equivalent in lei of €1m;
- the social capital of the legal person is owned by persons other than the state, local authorities and public institutions;
- are not under the dissolution through liquidation procedure registered with the Trade Registry or with the Courts

The micro-enterprises tax regime is applicable if a company had a turnover of less than €1m per year, with the above mentioned conditions being fulfilled as well. The tax rate on turnover is different, depending on the number of employees:

- 1% for companies with at least one full-time employee;
- 3% for companies with no employees.

Companies may opt out of the micro-company and switch to the corporate income tax regime by increasing the share capital to at least RON45,000 and having at least two full-time employees.

No fiscal losses can be accumulated while a micro-company.

Net rental income

At an individual level, starting with January 1st 2016, the deductible expenses percentage applicable when determining the net rental income, as well as the net income from the lease of agricultural assets was increased to 40%.

VAT treatment on immovable property

Under the current Romanian VAT legislation, the VAT treatment applied to supplies of immovable property depends on both the status of the property owner and the nature of the property.

The Romanian VAT legislation provides, as a general rule, that the sales of plots of non-buildable land, based on the town planning certificate and of buildings qualifying as old from a VAT perspective are subject to the VAT exemption without deduction right. Thus, the VAT exemption is not applicable for building land and new buildings.

From a VAT perspective, a building (or parts thereof) qualifies as new, if it is sold by the end of the year following its first usage/occupation. A construction that has been transformed, whereby the value of the transformation exceeds 50% of the building's value after transformation is also considered a new building. Building land represents any unimproved/improved land on which constructions can be erected on, according to the town planning certificate.

The following VAT treatment may be applicable for the sale of immovable assets, depending on their nature:

- **Reduced VAT rate of 5% –** for supplies of dwellings and houses delivered as part of social policy, including old people's homes, retirement homes, orphanages and rehabilitation centres for children with disabilities. This category includes also dwellings and parts thereof supplied as housing with a maximum useful surface of 120sqms, excluding outbuildings. The reduced rate applies if the value of the house acquired by any single person or family is less than RON450,000, exclusive of VAT. The reduced VAT rate is also applicable to the supply of the land beneath the house on the condition that it does not exceed 250sqms, including the footprint of the house.
- **VAT exemption –** if the immovable asset is a plot of non-buildable land, according to the town planning certificate or it qualifies as an old building for VAT purposes.
- **Taxation under the reverse charge mechanism –** for supplies of plots of building land or new buildings, provided that both the purchaser and supplier are registered for VAT purposes in Romania.
- **Standard VAT rate of 19% –** for supplies of plots of building land or new buildings, in case the conditions for the application of either the reduced VAT rate or reverse charge mechanism are not fulfilled.

If the immovable asset consists of a single property identified by a single cadastre number and is made up of a building and the land on which it is built, the VAT treatment related to the entire immovable asset will be the one applicable to the property (i.e. building or land) which has a higher value, according to a valuation report, or, if their values are equal, the one applicable to the immovable asset which has a larger surface.

The supply of land on which a building is erected, but where a demolition process is in progress, would be also treated from a VAT perspective as a sale of land.

Moreover, the rental/leasing of real estate property is deemed as a VAT exempt operation without deduction right.

Nevertheless, the landlord/lessor or the owner of the immovable property has the option to apply VAT for any such operations, by way of submitting a notification for taxation to the tax authorities.

Real Estate investors should assess the correct VAT treatment related to the supply/rental of real estate properties.

VAT deduction right

Any taxable person registered for VAT purposes in Romania has the right to deduct the VAT related to its acquisitions of immovable properties, if the goods/services are purchased for the purposes of performing taxable transactions.

Taxable persons performing acquisitions related to the construction of real estate envisaged to be used for performing operations both with and without deduction right will be able to fully deduct the input VAT during the investment process. Nevertheless, depending on the actual use of the investments with respect to the construction of real estate, the deducted input VAT should be adjusted accordingly.

The VAT deduction right is also granted for acquisitions of immovable assets from inactive or temporarily inactive taxpayers in debt enforcement proceedings, where the supply is considered taxable.

VAT adjustment for capital goods

Where the landlord/lessor does not opt to tax the rental fees/lease instalments, while input VAT was deducted on acquisition/ construction of the real estate property, VAT should be adjusted annually within the adjustment period for 1/20 of the VAT costs incurred on the acquisition, manufacture or construction of those goods.

If the real estate property is sold within the VAT exemption regime, while VAT was deducted upon acquisition/construction, the input VAT should be adjusted one-off for a period of 20 years or for the remaining adjustment period.

The adjustment should be performed in accordance with the percentage of the real estate property rented/leased/sold within the VAT exempt regime, insofar as such transactions are performed within the 20 years adjustment period.

The VAT adjustment should be performed in the period the event generates the adjustment occurs or in the last fiscal period of each year.

Opportunities and benefits of applying VAT-exemption should be considered for sale or rent of real estate.

VAT transfer of business

The partial or total transfer of assets performed during a spin-off or merger is outside the scope of VAT if the beneficiary is a taxable person established in Romania.

Under certain conditions, also the partial or total transfer of assets performed to a Romanian established company through a sale or contribution in kind qualifies as a VAT neutral transfer of business. Specifically, the operation is seen as a transfer of business if the transferred assets form, from a technical point of view, an independent structure capable of carrying out economic activities. Also, the beneficiary must continue the economic activity which was transferred to him and not immediately liquidate it or sell the assets which were transferred to him. In this respect, the beneficiary must provide the transfer with a statement on own responsibility attesting that this latter condition is met.

In addition, the beneficiary is regarded as the assignor' successor for purposes of adjustment of the VAT deduction right.

In case the taxation regime is applied for transfer of business, the tax authorities will allow the VAT deduction if the taxation regime was not applied for tax purposes.

Real Estate investors should review if the above conditions are met in order for the transfer of business to qualify as a transfer of going concern for which no VAT is due.

Established businesses in Romania

VAT refund

Although, based on the Romanian legislation VAT recovery should be made within 45 days of the date of filing the VAT return or 90 days from their submission (in case the resolution of the application requires a tax inspection), in practice the VAT refund process is a lengthy procedure (especially in Bucharest), subject to a prior tax inspection. The company can benefit from a fast VAT refund, if it achieves a low score in the risk analysis performed by the tax authorities or in case the amount is below a certain threshold.

Non-Romanian businesses

A company established in another EU Member State could claim a refund from the Romanian tax authorities of the VAT paid for goods/services acquired in Romania, based on the 9th EU Directive (VAT refund for taxable persons established in the EU). The VAT refund is granted under certain conditions and if the operations performed by the company in Romania do not entail a VAT registration requirement or a fixed establishment of the company in Romania.

In addition, Romania implemented the refund procedure based on the 13th EU Directive for VAT related to purchases made in Romania by non-EU established businesses under reciprocity conditions. In principle, a non-EU business will be entitled to benefit from a VAT refund, under the 13th EU Directive, for the VAT paid on goods/services purchased in Romania, if its operations herein do not entail a VAT registration requirement or a fixed establishment in Romania.

VAT split payment system

Starting with August 2019, the VAT split payment system will remain only optional for the taxable persons registered for VAT purposes in Romania.

Romania has removed the mandatory requirement for VAT split payment system following an order that was issued last November by the European Commission. The measure required customers to pay manually the VAT element of supplier’s invoices into a special and restricted account of the supplier.

Real Estate investors should assess the impact of these new changes on their existing future plans.

20 Slovakia

Real estate transfer tax

There is no real estate transfer tax in Slovakia.

Capital gains on the sale of real estate

There is no specific capital gains tax.

Slovak tax resident corporate owners of real estate are subject to tax on profits realised on the sale of real estate at the flat corporate income tax rate of 21%. Losses realised on the sale of buildings, are generally tax-deductible for corporate income tax purposes. However, losses from sale of land and real estate depreciated for tax purposes in 6th depreciation group (this limitation does not apply to technical improvement of real estate done by tenant) are not tax deductible.

Profits of individuals from sale of real estate may be exempted from personal income taxation, where certain conditions are met (i.e., holding period, way in which the ownership title was obtained, etc.). Otherwise, the profits are included into individual's tax base which is subject to progressive tax rate (19%/25% depending on the level of the tax base).

Also see below the comments re decrease of income tax rate for certain type of taxpayers.

Other alternatives for disposal of real estate should be considered.

Capital gains on the sale of shares

Income of a Slovak tax resident company from the sale of shares in Slovak and foreign joint-stock companies, ownership interests in limited liability companies, or limited partnerships (hereafter 'participation') may be exempt from corporate income tax (21%) if certain conditions are met. In particular, the following criteria should be met:

- direct holding of at least 10% of shares or ownership interests for at least 24 months (in cases where the criterion was already met before January 1st 2018, the 24 months period would be calculated from January 1st 2018, i.e. exemption may be applicable from January 1st 2020 at the earliest); and
- Slovak tax resident company seller performs substantial functions in Slovakia, bears and manages risks associated with the participation ownership and has adequate personnel resources and material equipment to perform these functions.

However, the above tax exemption does not apply to taxpayers who trade in securities, to the sale of companies in liquidation, bankruptcy or restructuring, or to taxpayers in liquidation.

Capital gain of Slovak tax resident individual from the sale of shares is generally subject to tax at 19%/25% (depending on the level of tax base). However, capital gain from sale of shares listed on recognised stock exchange may be exempted from tax, subject to certain conditions.

Also see below the comments re decrease of income tax rate for certain type of taxpayers.

In case of real estate acquisition, a careful structuring is required in order to reach tax neutral exit from investment.

Change of the tax rate

Based on the already approved Amendment of Slovak Tax Law coming into force from January 1st 2020, the new reduced income tax rate at 15% will be introduced for corporate taxpayers, entrepreneurs and self-employed individuals that achieve income (revenues) of up to €100,000 for the relevant tax period. The reduced rate will apply for the first time for the tax period starting January 1st 2020. If the taxpayer uses a fiscal rather than a calendar year, the reduced rate will apply for the first time the period beginning during 2020. For the taxpayers not meeting above criteria, current tax rates remain valid.

From 2020 income tax burden in Slovakia will be lower for certain types of the taxpayers.

Rental income

Rental income is part of the corporate income tax base of Slovak tax resident and is taxed as an ordinary income. It is subject to the standard corporate tax rate, which is 21% (see comments re change of tax rate since 2020 above). Rent paid to legal entities or individuals is tax-deductible on a cash (paid) basis. Nevertheless, rental payments are tax-deductible up to the amount, which actually relates to the particular tax period (special rules would apply to micro taxpayers).

Rental income of individuals is subject to progressive tax rate (19%/25% depending on the level of the tax base). Please also take into account expected tax rate reduction mentioned above.

The cash flow model should be reviewed in order to assess the level of tax burden.

Tax depreciation

Real estate, as other fixed assets, is subject to tax depreciation on an annual basis. Most buildings of a permanent nature are depreciated 20 or 40 years respectively using a straight-line method of tax depreciation.

In case that an asset is rented, the annual tax depreciation costs on leased fixed asset (including real estate) cannot exceed the annual rental income on such asset. The unclaimed tax depreciation costs on leased assets due to the above limit can be claimed after the end of statutory tax depreciation period.

The taxpayer can decide to interrupt (defer) tax depreciation of tangible assets for one or several tax periods. The depreciation period is then prolonged by the number of taxable periods in which the asset was not depreciated.

Tenants can depreciate technical enhancements done in rented premises in certain cases.

Special rules would apply to micro tax payers since 2021.

Land cannot be depreciated.

The company's fixed assets register should be reviewed to ensure correct depreciation. Interruption (deferring) of tax depreciation may provide the possibility to utilise tax losses which would be lost otherwise.

Tax losses carried forward

A company may carry forward and utilise a tax loss equally over a period of four years following the year in which the loss arose (25% per year max). If a taxpayer is not able to utilise the full portion of the tax loss available for deduction in that respective period, such unutilised part of the loss is lost for deduction permanently.

Carry back of losses is not available in the Slovak Republic.

Based on the already approved Amendment of Slovak Tax Law coming into force from 2020, company (not being a micro taxpayer) will be allowed to utilise a reported tax loss over five consecutive tax periods, up to 50% of the tax base declared in the respective tax period (the rule would apply to tax losses generated in periods starting from 1.1.2020). This means that the period for tax loss utilisation will be extended by one year, and the condition for equal utilisation will be cancelled.

The new rules would also apply to micro taxpayers, in respect of tax losses generated during tax periods since 1.1.2021, where above mentioned 50% limitation would not apply.

Optimise the tax base by maximum utilisation of the tax losses from previous years.

Tax-deductible costs

A company owning property in Slovakia can deduct interest expenses and property-related costs, e.g. tax depreciation (with exceptions as stated above), repairs, maintenance and utilities, from its taxable rental income, subject to the general conditions in the Slovak Tax Act. Property management fees can also generally be treated as tax-deductible.

Interest expenses on loans from a related party may be deducted for tax purposes, provided the following conditions are met:

- Loan principal is used to generate, secure or maintain taxable income and it is properly documented.
- The level of interest and related expenses is at arm's length level (which would be supported by proper transfer pricing documentation).
- The deduction of interest and related expenses is allowed by Slovak thin capitalisation rules (i.e. limited up to 25% of an adjusted current year EBITDA of the debtor).

Interest expenses under an intercompany loan (as well as any other expenses incurred in respect of a related party) would not be tax deductible in portion corresponding to the amount (these rules would be replaced since January 1st 2020, see 'anti-hybrid rules' below):

1. double deduction is achieved;
2. of a non-taxable income (income not subject to tax);
3. of funds if the funds are used (directly/indirectly) by a related party to repay (fully/partially) the expenses as stated above under points 1. or 2.

Interest expenses under the loan used for purchase of shares may be tax deductible only in the period when such shares would be sold (provided participation exemption of such sale would not apply).

In case of individuals owning a property in Slovakia and receiving rental income, the type of deductible expenses depends on the treatment of property.

The costs of the company should be properly documented in order to support its relation to taxable income generating activity of the company and its tax deductibility.

Thin capitalisation

The limit for the maximum amount of tax deductible interest and related fees on credits and loans between related parties is established as 25% of the adjusted earnings before interest costs, tax, depreciation, and amortisation (EBITDA).

In general, thin capitalisation provisions do not apply to financial institutions, some real estate companies, collective investment schemes, and leasing companies. Other exceptions or restrictions may apply.

Financing structure should be properly analysed in order to avoid negative tax implications or trapped cash.

Transfer pricing

Under Slovak legislation the transaction of Slovak corporate taxpayer with its foreign and Slovak related parties are subject to transfer pricing control. The tax legislation reflects the transfer pricing methods commonly used in OECD member countries. These transfer pricing methods include comparable uncontrolled price, resale price, cost plus, profit split and transactional net margin methods. The legislation provides local tax authorities with the flexibility to use these methods, or a combination thereof, when reviewing related party transactions.

Taxpayers are obliged to keep transfer pricing documentation supporting the arm's length level of prices used in transactions with their foreign and Slovak related parties.

The arm's length principle should be followed and the appropriate documentation should be in place for tax assessment. Proper transfer pricing review and planning is crucial.

Business combinations

There are following alternatives for the business combinations:
- Sale of business as a going concern (further 'BGC').
- Contribution of the BGC to share capital.
- Sale of individual assets and liabilities.
- Contribution of individual assets to share capital.
- Mergers and demergers.

Application of different options may allow for recognition of a step up in values of assets for tax purposes, recognition of goodwill, etc. The corporate tax related impact would depend on the actual facts/circumstances.

From Value Added Tax (VAT) point of view, sale of company's shares is VAT exempt in Slovakia. In case of mergers and acquisitions when the taxpayer dissolves without liquidation, such a business transfer should be out of scope of Slovak VAT if certain formal conditions are fulfilled. Similarly, transfer of a set of assets/obligations which meets the conditions for transfer of going concern should be also out of scope of Slovak VAT.

The effectiveness of each option depends on the particular situations in hands. Therefore, a detailed analysis is required to choose the best option.

Anti-avoidance rules

General: According to the Slovak tax law, in principle, the tax authorities have the right to reclassify the transaction(s) based on its substance and not formal view in cases where the transaction does not have economic justification and where at least one of the reasons was to avoid tax payments, to reduce the tax base or to obtain tax advantages, which the taxpayer would otherwise not be able to obtain ('GAAR').

Dividends: Slovak tax law states that dividends should be subject to tax in Slovakia if received by taxpayer

1. as a result of a measure or multiple measures which cannot be considered as based on proper business reasons corresponding to the economic reality, and
2. where the main or one of the main purposes of such measure(s) was obtaining of benefits which would not be granted otherwise.

Business combinations: There are also specific anti-tax avoidance rules which may deny tax neutrality of cross-border business combinations (merger, demerger, in-kind contribution of business), in case the main or one of the main purposes of transaction was reduction of tax due or tax liability avoidance. Where a transaction was not performed with valid commercial reasons, such as restructuring or rationalisation of activity, it may be expected that that the transaction was mainly performed for tax reasons subject to GAAR.

Changes in Double tax treaty (DTT) network: Slovakia ratified the Multilateral convention to implement tax treaty related measures to prevent base erosion and profit shifting (MLI). MLI among others may restrict application of DTT benefits.

Hybrid Mismatches: The Amendment of Slovak Tax Act valid from January 1st 2020 will transpose Council Directive (EU) 2017/952 as regards hybrid mismatches with third countries into Slovak law which may limit tax deductibility of expenses. In general, the rules adopted by Slovakia should follow the rules stipulated under the Directive.

The new and existing structures should be reviewed in order to assess the impact of Slovak anti-tax avoidance rules. The changes in the legislation should be monitored in order to assess the impact on the business.

Exit Tax

The exit tax applies to income when taxpayers (Slovak tax residents and non-residents with a permanent establishment (PE) in Slovakia) transfer outside of Slovakia:

1. Individual property (transfer carried out by a tax resident from their headquarters in Slovakia to a PE in another country, or by a tax non-resident from their PE in Slovakia to their headquarters of a PE in another country);
2. Business activities (transfer carried out by a tax resident to another country, or by a tax non-resident from their PE in Slovakia to another country);
3. Tax residence (tax resident is no longer Slovak tax resident).

The tax is calculated by applying a 21% tax rate to a specific positive tax base calculated based on Slovak tax law.

The impact of the future exit options in the light of the exit tax should be considered in respect with the long-term planning.

CFC Rules

The rules for CFCs seek to tax income artificially diverted by a Slovak parent company to a CFC if the income is paid without economic justification or to obtain a tax advantage for the Slovak company.

A company is considered a CFC if:

4. it is controlled or managed, directly or indirectly, by the Slovak company (e.g. by voting rights, share capital, or share in profit), and
5. the CIT paid in another country is lower than 50% of the tax the CFC would pay in Slovakia.

The CFC's income will be taxed in Slovakia by including the CFC's tax base in the tax base of the Slovak parent company to the extent it is attributable to the assets/risks related to the significant functions of the Slovak company, which manages and controls the CFC.

The CFC rules will be applied for tax periods commencing on or after January 1st 2019.

The Slovak CFC rules in general follows OECD approach.

Slovak source income

Generally, the gain from disposal of real estate located in Slovakia or the rental income from the real estate located in Slovakia is subject to Slovak taxation if paid to foreign tax resident under Slovak tax legislation.

Income of non-residents from transfer of shares in a Slovak company is also considered as a taxable income from a source in the Slovak Republic (regardless whether it is a Slovak real estate rich company or not) and is subject to Slovak taxation.

A tax securement of 19% applies to rent and sales price paid by a Slovak entity or individual to a non-EU/EEA entity/individual for real estate/shares located in Slovakia. A 35% securement tax rate applies on payments to taxpayers from "non-contracting states" (i.e. states that did not either conclude a double tax treaty or tax information exchange agreement with the Slovak Republic or where a Slovak taxpayer is not able to prove the beneficial ownership status of income recipient). Please note that since 2020 the term non-contracting state would be replaced by non-cooperative state, which may effectively increase the number of jurisdictions to which 35% applies.

No tax securement is required for rental payments/income from transfer of shares paid to EU/EEA-resident entities, assuming such non-resident is beneficial owner of received income.

The tax securement is considered a tax advance. The entity/individual receiving the rental income should file a Slovak tax return, and calculate its Slovak tax base (i.e., income less tax-deductible costs attributable to earning the income under Slovak tax law). If the tax return is not filed, the tax authorities can consider the tax securement to be a final tax.

Capital gains: The gain of non-resident from disposal of shares in a Slovak company is generally subject to ordinary corporate income tax rate applied for Slovak tax residents. In practice, some double tax treaties may provide protection from Slovak taxation of non-resident capital gain from disposal of shares in Slovak companies.

Dividends: In general, dividends distributed from profits generated after January 1st 2017 in favour of non-residents are subject to:
- 7% WHT, if paid to an individual (35% WHT in case of an individual from a 'non-contracting state or noncooperative state since 2020');
- 0% WHT, if paid to a company or a tax resident of a "contracting state/or cooperative state since 2020", provided such company is the beneficial owner of income; and
- 35% WHT, if paid to a company or tax resident of a "non-contracting state or noncooperative state since 2020", or where Slovak payer of income cannot prove the beneficial ownership status of income recipient.

The WHT, if any, may be decreased by the provisions of the effective DTT.

Generally, there is no withholding tax on dividends paid by Slovak entities out of profits arising in 2004-2016, unless GAAR apply.

Interest payments: If interest is paid by a Slovak entity to a foreign entity, it is subject to withholding tax of 19%/35% (in case of taxpayers from non-contracting states [or noncooperative state since 2020] or where Slovak taxpayer is not able to prove the beneficial owner status of income recipient) under Slovak domestic law. However, most DTTs reduce the withholding tax on interest to nil. Moreover, as a result of implementation of the interest provisions of the EU Interest and Royalty Directive into Slovak tax law, interest paid by a Slovak entity to a related company seated in another EU Member State that is the beneficial owner of the interest income, is not subject to Slovak tax, provided certain conditions are met.

Slovak withholding tax is not levied on non-resident's income sourced from Slovakia in case, the foreign company receiving the income has a Slovak permanent establishment (PE) to which the gain can be attributed.

There are options to reduce Slovak WHT burden.

Real estate tax (local tax)

Slovakia levies a real estate tax on companies and individuals owning land, buildings, flats or apartments, and non-residential premises in residential buildings, such as blocks of flats or apartments.

Generally, the real estate tax is payable by the registered owner of the land, building, or owner of the apartment. If the taxpayer cannot be determined, the tax is payable by the user of the land, individual or legal entity who uses the building. The real estate tax is governed by the Act on Local Taxes and includes the basic annual rates.

Generally, the tax liability depends on the area of ground occupied by the real estate in square metres, the number of floors, the nature and purpose of the building and its geographical location.

Budget for additional payments in relation to the real estate tax (local tax) should be considered.

Local development fee

From 2017, the municipality may establish in its territory or part of cadastral area a local one-off development fee. The development fee may vary from €3 to €35 per each square meter of ground space occupied by the finished building. The municipality can set the fee rate for various buildings differently. The municipality issues decision on application of the development fee once building permit is valid and the development fee is due within 15 days after the decision became valid.

Constructor should check if the local development fee for a building applies in its area and consider a budget for additional payments in relation to this fee.

Value added tax (VAT)

Transactions with real estate (sale or lease) can be either subject to 20% VAT or exempt from VAT in Slovakia. Supply of real estate or part thereof with related construction land is generally subject to 20% VAT if supply is made within first five years from:
- the first building approval or putting it into operation for the first time; or
- building approval received after reconstruction if its cost is at least 40% of the respective real estate value.

After this five-year period supply of real estate is normally VAT exempt without a right to deduct related input VAT. However, the supplier can decide not to apply the VAT exemption. In this case, VAT reverse-charge should apply for supplies to the Slovak VAT payers.

At the same time, option no to apply VAT exemption is not available to supplies of residential buildings, flats and individual suites in residential buildings.

Supply of land is VAT-exempt, except for construction land which is subject to Slovak VAT.

Lease of real estate is generally VAT exempt without a right to deduct related input VAT. However, leasing real estate to another taxable person, a taxpayer can decide whether to exempt it or not.

At the same time, lease of flat, detached house and lease of a suite in a residential building or parts thereof should be always VAT exempt. While, certain transactions such as e.g. letting of accommodation facilities (accommodation services) or parking premises, should be always taxable.

The following transactions in the construction sphere falling under the Section F of CPA Statistical classification of products performed between two Slovak VAT payers are subject to VAT reverse-charge:
- supply of construction works;
- supply of building or parts of buildings under the framework of the construction or similar agreements;
- supply of goods along with assembly and installation, if assembly and installation can be considered as construction works.

Slovak established taxable person not registered for VAT supplying a building, part of building or construction land automatically becomes a Slovak VAT payer upon such a supply and will have to charge VAT on it if upon its performance they reach VAT registration turnover threshold of €49,790.

A taxpayer is obliged to adjust the tax deduction, if during a 20 year period from acquisition/construction of real estate, he changes the purpose of its use (from VATable to VAT exempt and vice versa, or from business to non-business and vice versa).

The period for archiving invoices received in relation to immovable property is 20 years.

In many cases, Slovak VAT payers can decide whether to charge VAT on lease or sale of real estate or not. In certain cases for VATable supplies of real estate between two Slovak VAT payers VAT reverse-charge should apply.

VAT group

It is possible to create a VAT group in Slovakia that enables those persons connected economically, organisationally and financially, with their seat, place of business or fixed establishment in Slovakia to register for Slovak VAT as a single VAT payer. As a result, the transactions within the VAT group are not subjected to VAT.

VAT grouping makes sense when VAT group members are performing VATable supplies within the group and supply recipients are not entitled to full deduction of related input VAT.

21 Spain

Corporate Income Tax (CIT)

According to the Spanish CIT Act the standard tax rate is 25%.

Other rules such as the disallowance of real estate impairments, the definition of mere holding entities, the domestic-participation exemption regime, the restrictions on the utilisation of carry-forward tax losses, financial expenses capping-rule, etc. may be relevant for real estate investors.

Taxpayers shall pay special attention to these rules as well as to the interpretation made by the Tax Authorities by means of binding tax rulings.

It is recommended to analyse the impact that these rules may have in the investors' structures as well as the guidelines provided by the Tax Authorities.

CIT Payments on account

According to CIT payments on account rules, the rate for payments on account for companies with a turnover of €10m or over is 24% and a minimum payment on account rate of 23% of accounting profits is applicable for companies which exceed this threshold.

We highly recommend to plan when to carry out operations which generate tax-exempt income (distributions of dividends, sales of shares, etc.) as payments on account are made over these types of income.

Domestic withholding tax rate

Domestic withholding taxes applicable in 2016 onwards is 19%. It will be due unless an exemption or reduced rates are applicable to the case at hand.

Tax losses carried forward

Tax losses may be carried forward with no time limitation. However, the following general restrictions to the use of tax losses must be considered:

- Companies with a turnover below €20m during the previous 12 months should be entitled to offset 70% of the taxable profits.
- Companies with a turnover of €20m or more but below €60m during the previous 12 months should only be entitled to offset 50% of the taxable profits.
- Companies with a turnover of at least €60m during the previous 12 months should only be entitled to offset 25% of the taxable profits.
- €1m of losses will be compensated in any event.

These limits would not be applicable in the period in which the company is wound up.

Transfer pricing

Related party transactions must be arm's length. Generally, taxpayers are obliged to prepare transfer pricing documentation for transactions exceeding certain thresholds. Failure to comply with the documentation obligations may result in penalties being imposed.

In addition, it must be noted that a new tax form (No. 232) was approved by the end of August 2017 to declare transactions carried out between related parties.

The tax return should be filed during the month following the ten months after the end of the tax period which the information to be provided refers to. That is, for fiscal years ending December 31st 2019 the tax return should be filed between November 1st and November 30th 2020. Temporarily, for financial years commencing in 2019 and ending before December 31st 2019 (short fiscal year), the tax return should be filed also between November 1st and November 30th 2020.

Prepare a transfer pricing study covering the relevant transactions carried out with related parties in the period in accordance with the applicable regulations. File the tax form 232 in November.

Country by Country report (CbCR)

From 2016 certain entities are required to file a country-by-country report (CbCR). The report should be filed electronically and should must contain aggregate information in Euros relating to the tax year of the controlling company of the group and with respect to each country or jurisdiction in which the group operates.

This CbCR must be filed electronically through the tax form No. 231 within 12 months of the end of every tax period. Note that, unlike the Master and Local Files that will need to be “at the disposal” of the Tax Administration, the CbCR has to be filed every year.

We recommend to analyse if the CbCR obligation is applicable and prepare the relevant report, if necessary, in accordance with the applicable regulations.

Residence certificates

Withholding tax exemptions and reduced treaty rates must be supported with the relevant residence certificates validly issued by the corresponding Tax Authorities in a timely manner. This is especially relevant for interest and management fees.

Request and collect the corresponding residence certificates.

Real estate investment trust

A special Corporate Income Tax regime, namely a 0% tax rate, is granted for Spanish REITs (SOCIMI) subject to a number of requirements. Should they not be respected, the tax regime may be lost together with a three year ban to be imposed.

Review the compliance of the REIT requirements, in particular the asset and income tests.

Value Added Tax (VAT) – Immediate supply of information

From July 1st 2017, large companies (whose turnover for the prior year will have exceeded €6m) and any other companies which file monthly VAT returns are required to provide their invoicing records and VAT books for issued and received invoices to the Spanish Tax Authorities in real time.

It must be noted that this obligation, which implies that companies will need to adapt their accounting and invoicing systems accordingly, has multiplied the information, which the Spanish Tax Authorities have access to.

Tax on the Increase of Urban Land

The sale of urban lands is subject to the Tax on the Increase in Value of Urban Land (TIVUL). The taxable income is the deemed increase of value of urban land generated during the years of possession of the urban land. The taxpayer will be the seller.

The taxable quota is calculated on the cadastral value of the land applying the coefficients and rates applicable in the municipality where the asset is located. This tax is deductible for CIT purposes.

The Spanish Constitutional Court, in a judgement dated May 11th 2017, ruled the unconstitutionality of the TIVUL tax base calculation method. Thus, no IVULT should arise in case of a loss-making disposal.

Based on the latest judgement from the Spanish Supreme Court, dated July 9th 2018, the IVULT would be due unless the taxpayer is able to prove that the disposal has been done in a loss position. The reason behind this argument is that the Spanish Supreme Court understands that the unconstitutional character of the Law regulating the IVULT is only partial, thus, it would be unconstitutional only if the IVULT is levied on transfers or disposals in which there are no actual increase of the land's value.

Similarly, last April 2019, the Spanish Constitutional Court was asked about the unconstitutionality that could exist in those cases where, even existing a profit, the IVULT due by the taxpayer would absorb almost all of the profit or even exceed it.

To this day, the Spanish Constitutional Court has not ruled about this question yet.

Currently, there is a draft law proposal which provides: i) a change on the way in which the taxable basis is calculated; and ii) a confirmation excluding the IVULT in case the transaction does not effectively generate a capital gain.

It is expected that a modification of the TIVUL legislation will take place. It is not clear if a new tax base calculation method will be introduced or the former rules will be modified to address the situation in which capital losses exist.

22 Sweden

Limitation of deductions on capital loss

Deduction of capital losses on real property is limited to capital gains from real property. Companies with capital losses due to the sale of real property can hence not deduct the loss against income from other sources. The loss may however be transferred within a consolidated group. Capital losses on real property may be carried forward indefinitely if not utilised.

If capital losses on real property are to be deducted, ensure that capital gains on real property exist in the same fiscal year. Carry forward possibilities do exist.

Group taxation

To benefit from Swedish group consolidation for tax purposes, the companies giving and receiving the group contribution must have been part of the group (i.e. exceeding 90% ownership requirement) for the entire fiscal year. Notwithstanding this, newly started businesses and off-the-shelf companies can exchange group contribution with other Swedish group companies from the day they commence conducting business.

Ensure that any acquisition is completed before the end of the current fiscal year to benefit from the group contribution rules the following fiscal year. As group contributions need to be recognised in the accounts, make sure to discuss the possibilities before closing the accounts.

Losses carried forward

Mergers and acquisitions which imply a change of control (even if the indirect ownership does not change) over a company can limit the possibility to utilise tax losses carried forward in the following years. Tax losses from the year before the change of control may be forfeited and/or restricted in time. Exemptions may apply in case the companies were part of the same group before as well as after the acquisition or reorganisation.

Verify if any limitations are applicable in the specific case and be cautious in cases where tax losses carried forward are utilised against group contributions received.

Tax allocation reserve

Companies can delay tax payments for up to six years on 25% of the annual profit by means of a tax allocation reserve. This can benefit liquidity and balance out occasional annual losses since the latent tax debts can be used against future losses for the upcoming six years. Companies using this reserve are taxed annually on a hypothetical income/interest. The income/interest is calculated by multiplying the reserve by 72% of the interest rate on governmental loans. The rate on governmental loans (government bond yield) is normally between 2% and 5%, but since 2014 the governmental bond yield has been below 1%. However, for financial years starting after December 31st 2016, the government bond yield, can never be lower than 0.5 % for the purpose of this calculation. Lastly, as a result of the corporate tax rate being lowered in two stages (to 21.4% in FY 19 and 20.6% in FY 21), a tax allocation reserve reversed in a year with a lower tax rate than when it was offset, must be increased to in order to have a tax impact correlating to the tax rate when it was offset.

Cash flow models and profit forecasts should be checked to assess the situation. As tax allocation reserves have to be recognised in the accounts, make sure to discuss the possibilities before closing the accounts. Any reversals in FY19 needs to be increased to 103% of the nominal amount.

Capitalisation of investments

Investments made on a property can refer to either e.g. building, building equipment or land improvements. Depending on the classification, the depreciation rate varies quite significantly. In addition to this, there is a possibility to in some cases deduct the entire investment cost direct for tax purposes should the investment be considered as a tenant improvement for tax purposes. Given this, there is often an opportunity to identify what the investment cost relates to in order to obtain a correct and faster depreciation plan than what would have been the case should only capitalisation on building occur. Part of this area does not need to comply with the accounts why it can be very beneficial to analyse the possibility to directly deduct the cost for tax purposes when the investments are capitalised in the accounts.

Consider carefully what kind of investments that has been made and what asset types the investment should relate to.

Transfer pricing

Cross-border transactions between related parties have to be carried out in accordance with the arm's length principle, which means that prices should be set as if the transactions are carried out between two independent parties. If this principle is not complied with, or if one fails to present appropriate documentation to the Swedish tax authority, the taxable income can be reassessed to the taxpayer's disadvantage. Other penalties may also be incurred.

Duly follow the arm's length principle, monitor applied prices on intragroup charges and transactions and ensure documentation of cross-border activities.

Limitation of interest deduction

As of January 1st 2019, Sweden has implemented a new tax regulation for the corporate sector, providing for a further limitation for deduction on interest expenses. Previously, Sweden applied strict deductibility limitations on interest expenses on loans to affiliated companies ('interest deductibility limitations'), but with the new rules in place the right to deduct interest costs relating to external debt will also be restricted.

The new rules provide for a general limitation on the right to deduct net interest expense in the corporate sector. When calculating the net interest expenses it is possible to offset any interest income against external interest expenses (interest income and expenses are offset against each other and any net expense is subject to the new rules). Interest costs that have been considered as non-deductible according to the targeted interest deduction rules (please see below), should not be included when calculating the net interest expenses.

The right to deduct is, following the implementation of the new rules, based on a so-called EBITDA (Earnings Before Interest, Tax, Deprecations and Amortisations) rule. This means that a company's net interest expenses are deductible up to 30% of taxable EBITDA.

Companies which have net interest income are able to offset another company's non-utilised net interest expense against their own net interest income. A condition for this is that the companies can exchange group contributions under the Swedish tax consolidation rules, and that both of the companies report the deduction in their respective income tax returns.

A “safe harbor” rule has also been introduced, which provides that it is possible to deduct net interest expense up to a maximum of SEK5m without any limitation. For affiliated companies the total deductions for net interest expense for all companies may not exceed SEK5m if any of the companies makes use of this rule.

Net interest expense which is not deductible according to the EBITDA rule is to be carried forward during a period of up to six years. Interest expenses carried forward can however not be used against net interest income in another group company. If the safe harbor rule is applied, interest costs exceeding the SEK5m threshold cannot be carried forward.

Any additional interest expenses or one-off fees related to the repayment of external bank debt may be considered as interest and thus also subject to the EBITDA-restriction. Note also that for loans in a foreign currency, any exchange losses can be seen as an interest expense and exchange gains as an interest income.

The new rules have not replaced the previously used targeted interest deduction limitation rules. Instead, the new rules compliment the rules already in place. The targeted interest deduction limitation on intra-group loans have however been slightly narrowed in scope and only apply in specific cases where the structure/ debt relationship is specifically tax driven.

Deductibility on intra-group loans is possible if:
- The final recipient of the interest is domiciled within the EEA;
- The final recipient of the interest is domiciled outside of the EEA, in a state with whom Sweden has entered into a tax treaty and the recipient is subject to the rules of the tax treaty; or
- The final recipient of the interest is taxed on the interest income at a minimum effective tax rate of 10% according to the tax legislation in the state in which the recipient is domiciled, should the recipient only be taxed on that income.

However, even if one or several of the circumstances for deduction are fulfilled, the interest is not deductible if the debt solely or almost solely (90–100%) has been put in place in order to receive a substantial tax benefit.

Other changes regarding taxation of the corporate sector as of Jan 2019

A number of other changes with effect from January 1st 2019 has also been adopted:

The corporate tax rate has been/will be decreased in two stages, from 22% in 2018 to 21.4% in 2019 and to 20.6% in 2021.

A so-called primary deduction has been implemented for all rental buildings (residential and commercial) for costs incurred in new construction, in making additions to existing buildings and in the reconstruction of buildings. For these costs, depreciations can be made with an additional 12% in total during the first six years from the time the construction work was completed. If a rental building is acquired by way of an asset deal within six years from completion, the purchaser shall make a primary deduction for the remaining part of the six year period, which is then calculated based on the acquisition cost. However, it will only be possible to acquire the right to primary deduction for cost incurred in new constructions and not cost attributable to additions or reconstructions of existing rental buildings.

General rules have been introduced for calculating the interest part in financial leasing agreements. In case the interest part is not specified in the leasing agreement, or if it is not market-based, the interest part is to be determined by a special calculation model.

A prohibition on the deduction of interest costs in certain cross-border transactions has been introduced. In short, the intention is to have rules that limit the possibility of deducting interest costs in Sweden to situations where no taxable income is reported abroad or where a deduction of the same interest expense would otherwise have been granted to companies in two different countries.

Value Added Tax (VAT) regarding letting of premises

Letting of premises can be subject to voluntary VAT liability if the tenant is invoiced with VAT. Please note that the following requirements must be met;

1. the premises must be used for VAT-able purposes or by a tenant that can have the VAT refunded such as the Government, county councils etc., and
2. the letting must be for a continuous period of time.

It is recommended to not conclude a lease agreement for a shorter period than 12 months since short term leases may disqualify the letting from voluntary VAT liability. In case a short term lease is contemplated it is recommended to analyse the potential VAT effects this will have before the agreement is concluded.

The voluntary VAT liability commences once the tenant has moved in and is charged with VAT. Input VAT incurred prior to the optional VAT liability is as a starting point not recoverable.

However, in case of new construction, reconstruction or extension works it is possible to apply for so called voluntary VAT liability during the construction phase and thereby become subject to voluntary VAT even if there are no tenants which can be charged with VAT yet. Also, it is possible to recover VAT on construction costs that occurred before the property was subject to voluntary VAT liability retroactively. The right to deduct such VAT will occur once the tenants move in and are charged with VAT. The retroactive VAT recovery only covers costs for new construction, reconstruction and extension works, i.e. capitalised expenditures. Operational expenses invoiced before the voluntary VAT liability commenced are not recoverable.

VAT adjustments

If a property during any of the last ten years has been subject to new construction, reconstruction or extension works and the total input VAT on such measures during the year amounts to SEK100,000 or more, the property is considered as capital goods. If the VATable usage of any such property covered by the capital goods scheme has changed during the year, such as from VATable to non-VATable, the property owner is obliged to adjust the previously reported input VAT, i.e. to repay previously recovered VAT or to recover previously non-deducted input VAT.

Any adjustment should be submitted to the Tax Agency the first reporting period the years after the change of use of the premises occurred.

Check the VATable status of the premises at year end.

Simplification of rules regarding letting of premises

As from January 1st 2014, it is no longer required to apply for voluntary VAT registration for letting of premises. Instead, let areas that are invoiced including VAT are covered by voluntary VAT registration. All other requirements remains the same i.e. the premises must be used for VAT-able purposes and the letting must be for a continuous period of time.

Voluntary VAT liability during the construction phase can still only be obtained by applying to the Tax Agency.

Letting of space for equipment on a mast or antenna to a mobile phone operator will be subject to mandatory VAT.

Pop-up stores

The Supreme Administrative Court has ruled that a property owner can be subject to voluntary VAT in case of short term letting to tenants operating pop-up stores. According to the Tax Agency's interpretation, the ruling does not apply to short term leasing of other types of business where the tenant is more likely to conduct a VAT exempt business, for instance in case of ordinary office space.

Major and significant upcoming changes

Changes to the withholding tax rules

In autumn 2017, the Swedish government initiated an investigation to review the WHT act just described. The investigator will particularly analyse if the current WHT act needs to be adapted to the relevant EU-legislation and analyse the function of the anti-avoidance provision compared to the separate Swedish tax evasion legislation. The result of the analysis was to be presented by the December 15th 2018. The review period was then extended to end of March 2019. Nothing has however been issued since then and no further information has been given as to when a proposal can be expected.

ATAD II implementation

On May 29th 2019 the Council on Legislation presented their considerations regarding the implementation of regulations in the EU's directive against tax avoidance to neutralise the effects of hybrid mismatches. It should be noted that it is proposed that ATAD II will be implemented in Sweden by 2020 and 2022 as the directive stipulates. However, it should be noted that there is a bill prepared also including provisions on hybrid entities, thus an implementation of ATAD II with regards to hybrid entities may occur before 2022.

Such implementation would affect hybrid entity mismatches which might occur with regards to e.g. interest costs (already introduced into Swedish law) but also with regards to other costs. Consequently, a question which might arise in the future is if a cost which has been deducted in a Swedish limited liability company may be denied due to a hybrid entity mismatch following the implemented ATAD II, e.g. due to a double deduction. The Swedish implementation of ATAD II is not yet in force and it would have to be monitored if any hybrid entity mismatch situation would arise to due to the implementation of ATAD II.

However, according to the memorandum referred to the Council on Legislation, the hybrid regulations should be extended to include other expenditure in addition to interest. The hybrid rules shall be applied (as previously) to associated companies, but also in other circumstances where they lead to a tax benefit.

New case law regarding purchaser's obligation to adjust input VAT on investments

Following the ECJ case C-622/11, Pactor Vastgoed, a case regarding a purchaser's obligation to adjust input VAT on investments made by the previous seller, the Swedish Administrative Court of Appeal has ruled that the VAT directive has direct effect and that a purchaser of a property should not be obliged to adjust input VAT on investments made by the previous owner. The case has been appealed by the Swedish Tax Agency to the Supreme Administrative Court, which has referred the case to the ECJ as of September 2019.

23 Switzerland

Corporate Tax Reform

In May 2019, the corporate tax reform was accepted by the Swiss public vote with a majority of 66.4%. The Swiss tax reform introduces the following key measures:

- Introduction of a patent box into cantonal tax laws;
- Optional introduction of a 50% additional R&D cost deduction into cantonal tax laws;
- Optional introduction of a deduction on excess equity (Notional Interest Deduction; NID) for high tax cantons (e.g. Zurich);
- Rules concerning hidden reserves upon migration to/from Switzerland and transitional rules upon change of status of preferential regime companies;
- Maximum limitation of relief may not exceed 70% of profits subject to cantonal tax;
- Optional capital tax relief for cantons relating to participations, patents and intercompany loans;
- Introduction of 50% proportionality rule for withholding tax-free repayments of capital contribution reserves for companies listed on the Swiss stock exchange;
- Broadening of the lump-sum tax credit to enable ordinarily taxed Swiss branches of foreign companies to claim a lump-sum tax credit for foreign withholding taxes under certain circumstances.

Further, most cantons have – in addition to the above measures – announced that they intend to reduce their corporate income tax rates.

Most cantons are expected to implement the reform by January 1st 2020. Various cantons already had their cantonal vote on the implementation of the reform but in the majority of the cantons, the final amendment to the law is still in the political discussion or subject to a public vote.

The most recent information and details about the TRAF and the above measures can be found on our homepage: https://www.pwc.ch/ctr.

General income taxation

For Swiss real estate investments, the TRAF measures outlined above are not particularly relevant as they did – in the past – not benefit from the abolished tax regimes. However, Swiss real estate investors will benefit from the reduction of the cantonal tax rates which will reduce the current tax charge on real estate income in most of the cantons.

Deferred tax/liquidation tax

In Switzerland, there are two different kinds of taxation of capital gains on real estate. Some cantons apply ordinary income tax whereas other cantons apply a special real estate capital gains tax.

- The corporate tax reform that leads to reduced income tax will have an impact on the deferred tax position in cantons that apply income tax on real estate capital gains.
- On the other hand, the special real estate capital gains tax is not impacted by the corporate tax reform, meaning that in these cantons the deferred tax position is not affected by the corporate tax reform.

Recaptured depreciations and value adjustments are in all cantons subject to ordinary income taxes (which are going to be reduced in the future).

Applicable future tax rate

The following key cantons will reduce their overall ETR (ongoing income tax) due to the corporate tax reform as follows:

- Basel (BS): already reduced for 2019 from 22.18% to 13.04%
- Bern (BE): reduction not yet decided
- Geneva (GE): reduction from 24.16% to 14% (as of 2020)
- Zug (ZG): reduction from 14.51% to 11.91% (as of 2020)
- Zurich (ZH): reduction from 21.15% to 19.70% (as of 2021) respectively 18.19% (as of 2023)

Funds with direct ownership of Swiss real estate

Foreign funds with direct ownership of Swiss real estate will need to prepare additional accounts according to Swiss GAAP in order to benefit from a more preferential tax treatment.

24 Turkey

Corporate tax

Resident companies in Turkey are subject to corporation tax on their worldwide income. The standard corporate tax rate was increased to 22% from 20% for 2018, 2019, 2020 FY for tax period that begin on or after January 1st 2018. Corporate income tax law states exemptions which can be beneficially utilised by corporations (upon meeting certain conditions), such as dividend income received from resident or non-resident companies, earnings of corporations derived from their foreign establishments of representatives, 50% of capital gains derived from the sale of property or 75% of participation shares which are held by corporations for more than two years.

When filing the corporate tax return, it should be ensured that the taxpayers can benefit from such tax-exemptions, and that Corporate income tax law requirements are fulfilled.

Transfer pricing

If a taxpayer enters into transactions regarding the sale or purchase of goods and services with related parties, the parties should follow the arm's length principle. Transfer pricing regulations stipulate documentation requirements for taxpayers, who should complete the transfer pricing form every year and submit it as an appendix with the corporate tax returns. Taxpayers are also required to prepare an annual transfer pricing report including supporting documents for their international and/or domestic related-party transactions.

It should be ensured that Turkish transfer pricing documentation requirements are met.

Thin capitalisation rule

If the ratio of the borrowings from related parties exceeds three times the shareholders' equity of the borrower company, the exceeding portion of the borrowing will be considered as thin capital. Interest and other payments relating to thin capital and the related foreign exchange losses are non-deductible expenses while calculating the corporate tax base. For loans received from related party banks or financial institutions that provide lending also to third parties, the debt/equity ratio will be considered 1/6 instead of 1/3. The shareholders' equity represents the total shareholders' equity at the beginning of the given fiscal year.

A thin capitalisation analysis should be made by the taxpayer during the preparation of the corporate tax return if companies receive related party loans.

Controlled foreign corporation (CFC)

Corporations that are established abroad and are at least 50% controlled directly or indirectly by tax resident companies are considered controlled foreign corporations when certain requirements are met, such as being subject to an effective income tax rate lower than 10% in its home country, having a gross revenue more than TRY100,000 in the related period and having passive income (at least 25% of gross revenue). CFC profits would be included in the corporate income tax base of the controlling resident corporation irrespective of whether it is distributed or not.

CFC profits should be included in the tax base of the Turkish resident company if the foreign corporations meet the conditions of being a CFC.

Depreciation

Depreciation may be applied by using either the straight-line or declining-balance method at the discretion of the taxpayer. However, please note that once the taxpayer has started to apply the straight-line method, it is not possible to change the method in the following years, although the opposite is possible. While the applicable rate for the declining-balance method is twice the rate (determined by the Ministry of Finance) of the straight-line method, the maximum applicable rate for the declining-balance method is 50%.

Interest and foreign exchange costs regarding the financing of fixed assets should be added to the cost of fixed assets until the end of the year in which assets are taken into account. The depreciation method should be selected for the fixed assets which are purchased in the related year.

Foreign currency revaluation

Assets and liabilities denominated in foreign currency are revalued at year-end based on the exchange rates announced by the Ministry of Finance.

Foreign currency asset and liability accounts in foreign currency should be evaluated in each quarter.

Prepaid income

If corporations receive income in advance from future fiscal years, such as advanced rental income, these amounts should be followed in the balance sheet accounts and should be taken into consideration as income in the fiscal year with which the income is related.

During the calculation of the corporate tax base, it should be determined whether the income of corporations includes advanced income or not.

Doubtful receivables

Receivables which are relevant to the acquisition of commercial income and at the litigation stage or administrative action can be written as doubtful receivables in the year that the litigation process started. Provisions may be accounted for the doubtful receivable at the disposable value on the day of valuation.

It should be determined whether doubtful receivable provision amounts meet the conditions to be considered as a deductible expense during the calculation of the corporate tax base.

Bad debts

Account receivable whose collection is no longer possible, based either upon a judicial decision or upon other substantiated documents can be considered as bad debt. The bad debt amount can be regarded as an expense item in the related period.

In accordance with above mentioned regulation, the Law No 7104 (effective as of January 1st 2019) provides for VAT relief for uncollectable receivables that become worthless in accordance with the above mentioned regulation (Art. 322 of Tax Procedural Law).

Consequently, a supplier who has accounted for and paid VAT on a supply, but who has not been paid the price for that supply, will be able to claim the VAT it has paid (by increasing the input VAT).

It should be determined whether bad debt amounts and VAT claim meet the conditions for the application of the above mentioned regulations.

Value Added Tax (VAT) rate for the residential units

Although according to the former legislation, VAT rate for the residential units with a net area of less than 150sqm, was set as 1%, by the new Council of Ministers Decision which was promulgated on the Official Gazette No 28515 dated January 1st 2013, the VAT rate to be applied on the delivery of houses with a net area smaller than 150sqm has been amended.

The determination of the VAT rate to be applied (1%, 8% or 18%) on the deliveries of houses starting from the year 2013 will vary based on several different factors such as;

- building license obtaining date;
- construction class of the building;
- square meters of the house;
- whether it is built on a Metropolitan Municipality area or not;
- whether it is built on an area which is qualified as reserve construction or risky or on a location where risky building exist based on Law No 6306 on the Transformation of Areas Under Disaster Risk;
- Property tax value per square meter of the land.

In accordance with the Cabinet Decrees numbered 2018/11674 changes had been made in the VAT rate to be applied on the delivery of residential units. Within the scope of the latest update in the legislation, VAT implementation for the houses and the workplaces which are subject to 18% VAT is updated and decreased to 8% until December 31st 2019.

Turkish tax authorities have introduced new legislation regarding VAT exemptions for deliveries to non-resident individuals with valid work and residence permits, as well as Turkish citizens who work abroad for more than six months. This exemption is applicable for the first sale of new buildings built as residences or workplaces. Additionally, foreign currency should be brought to Turkey for this purpose. Please also note that there are other certain conditions to be fulfilled for the application of the exemption.

Taxpayers should pay closer attention while deciding the correct VAT rate to be calculated, as all the above mentioned criteria should be considered at the same time.

Title Deed fee

“Title Deed Fee” is calculated according to the “Fee Law” for the transactions concluded at the title deed registry such as property buying/selling, registration of rental contract, annotations of any transaction made at registry etc. At the time of acquisition, title deed fee at the rate of 2% is applicable over the sales price for buyer and seller separately. Fee has to be paid to the tax office before the transaction made at the registrar. In accordance with the Cabinet Decree 2018/11674, title deed fee (for houses and workplaces) is reduced from 4% to 3%. These changes are valid until December 31st 2019.

Stamp Tax

Stamp tax applies to a wide range of documents, including but not limited to agreements, financial statements and payrolls. Agreement that states a monetary value is subject to stamp tax at a general rate of 0.948%. Lease contracts are subject to stamp tax at a rate of 0.189% of the rental amount.

Stamp duty rate to be applied on several agreements, which are specifically related to the real estate industry, has been reduced to 0% (zero) in 2017.

The corresponding agreements are;

- Officially drafted construction agreements on flat for land basis or revenue sharing;
- Construction and contracting agreements drafted among building contractors and sub-contractors within the scope of officially drafted construction agreements on flat for land basis or revenue sharing;
- Advisory service agreements with respect to the construction work on flat for land basis or revenue sharing;
- Service agreements of building inspection;
- Preliminary sale agreements in relation with residential units;
- Officially drafted promise to sell agreements in relation with immovable.

Stamp tax is capped at TRY2,642,810 (approximately €416,190) under the current foreign exchange rate, subject to annual revaluation) for the year 2019. All signatory parties are jointly held liable for the stamp tax payment. In practice, the parties come to a mutual agreement regarding the stamp tax payment.

For Turkish corporate income tax purposes, stamp tax that relates to real property can either be deducted as an expense or capitalised with the real estate and depreciated. If the stamp tax is not related to the real estate, it has to be deducted as an expense.

Resource Utilisation Support Fund (RUSF) rates

RUSF rates are to be applied on foreign loans obtained by Turkish resident individuals or legal entities (except for banks or financial institutions) in terms of foreign currency or gold (except for fiduciary transactions) was restructured based on the average maturities as follows;

- 3% on the principal if the average maturity period of the foreign currency credit does not exceed one year.
- 1% on the principal if the average maturity period of the foreign currency credit which is between one and two years.
- 0.5% on the principal if the average maturity period of the foreign currency credit which is between two and three years.
- 0% on the principal if the average maturity period of the foreign currency credit over three years.
- 1% on the interest amount if the average maturity period of the foreign loan denominated in Turkish Liras does not exceed one year.
- 0% on the interest amount if the average maturity period of the foreign loan denominated in Turkish Liras which is over one year.

Before March 15th 2017, RUSF was applicable at 3% over the interest amount for Turkish Liras dominated loans regardless of the maturity of the loan. With the latest amendment announced on March 15th 2017 by the Council of Ministers Decision, RUSF rates for Turkish Liras dominated loans has been changed to 1% on the interest amount whose average maturity does not exceed one year and 0% on the interest amount whose average maturity period exceeds one year. Therefore, Companies should evaluate their financing situation according to the RUSF rates.

Deductibility of finance expenses

Law No 6322, which has entered into force on June 15th 2012, amends the general principles of the deductibility of the finance expenses for Turkish taxpayers. The arrangement shall be effective as of January 1st 2013. According to the related Law, a portion – yet to be determined by the Council of Ministers – of interest and similar expenses incurred on foreign resources will not qualify deduction for corporate tax purposes. According to the arrangement;

- Credit institutions, financial institutions, financial leasing, factoring and financing companies shall not be subject to finance cost restrictions,
- Cost restrictions shall apply exclusively to the portion of liabilities that exceed a company's shareholder's equity,
- Restrictions shall not exceed 10% and the rate may be amended per industry by the Council of Ministers,
- Restrictions shall not apply to interest rates and similar payments added to investment costs.

Please note that there was not any update development with respect to this interest expense deductibility principle since 2013. However, Companies should still evaluate their financing situation in accordance with the related interest expense deductibility principles.

Deemed interest deduction on cash injection as capital

The Law No 6637, which has been published in the Official Gazette dated April 7th 2015, introduced a new concept of tax incentives where Turkish resident companies are allowed a deemed-interest deduction over cash injection as capital from the corporate tax base of the relevant year. The provisions became effective on July 1st 2015.

According to the arrangement Turkish resident companies (except for those that operate in banking, finance and insurance sectors and public enterprises) would be able to benefit from a deemed interest deduction that is equal to 50% of the interest calculated on the cash capital increase in the registered capital of the existing corporations or cash capital contributions of the newly incorporated corporations based on the average interest rate by the Central Bank of Turkey for TL denominated commercial loans, from their Corporate tax base of the relevant year.

The Council of Ministers has been authorised to decrease the rate to 0% or increase to 100%. By the new Council of Minister Decree No. 2015/7910 dated June 30th 2015, cash capital increase rate has been re-determined between 0%–100% for various situations.

The amount to be considered for the deemed interest calculation will be limited only when the cash capital actually paid to the bank account of company by shareholders.

Additionally, the deemed interest deduction rate will vary different cases such as;

- The companies that are publicly traded in Borsa Istanbul (BIST) at the last day of the year in which the 50% interest deduction is benefited, the rate would be increased by;
  – 25 points, if the publicly traded rate of nominal/value or the amount of the registered shares of the company is 50% or less (totally 75%);
  – 50 points, if more than 50% of the nominal/registered shares of the company are traded in BIST (totally 100%).
- In the case, the capital increase made in cash has been used for investments with Investment Incentive Certificate on manufacturing or industrial plants, purchase of machines or equipment required for such plants or lands or states for building of such plants, the 50% rate has been increased by 25 points.
- The Decree reduces the rate to 0% for the capital increases made for the following cases:
  – Companies with 25% or more of their income composed of passive income, such as interest, dividend, rental income, royalties, capital gains on sale of shares;
  – Companies with 50% or more of its assets are composed of long-term securities, subsidiary companies and participations;
  – Invest capital or provide a loan to other companies which are limited only with the corresponding capital increase made in cash amount;
  – For the capital companies investing in lands and plots which are limited only with the corresponding investment amount;
  – Limited only to the amount corresponding to the decreased capital amount, if capital has been decreased in the period between March 9th 2015 and July 1st 2015.

As mentioned above, certain companies operating in real estate industry especially the ones earning rental income and making land investments may not utilise the above mentioned interest deductions.

Tax reduction for compliant taxpayers

Income Tax Law numbered 193 had been re-arranged last year to provide 5% discount for eligible taxpayers who are consistent in filing their tax returns on time and have no outstanding tax liability.

To qualify, taxpayers must meet the following conditions:

1. All tax returns belonging to the year the tax discount will be applied, and to the previous two years, must be submitted within the statutory period. In addition, the related due taxes must be paid within the statutory period. (The years 2016, 2017 and 2018 will be taken into account for evaluating eligibility for the discount to be applied in 2019). Late payments up to TRY250 will not be considered as a violation of timely tax payment.
2. The taxpayer should not be subject to any additional tax assessment by Turkish tax authorities in the year the discount is applied and in the two preceding years. (The years 2016, 2017 and 2018 will be taken into account for evaluating eligibility for the discount to be applied in the year 2019). Tax returns declared for correction or voluntary disclosure purposes are not regarded as a violation of the condition.
3. The taxpayer should not have unpaid tax debt exceeding TRY1,000.

The discount will be 5% of corporate income tax (income tax for individuals) liability declared on the annual tax return (the discount cannot exceed 1,2m TL).

The discount is applicable for annual corporate and income tax returns to be submitted after January 1st 2018.

Please note that, taxpayers who committed tax evasion in the year of discount application and in the four preceding calendar years are not allowed to benefit from the discount.

Taxpayers should pay attention to the utilisation of this tax reduction opportunity during the CIT declaration process.

The new wealth amnesty

Legislation published in the official gazette on July 19th brought into effect a new wealth amnesty programme which allows taxpayers to regularise their undisclosed assets until December 31st 2019 by paying a 1% tax on the value of the asset.

The regulation (similar with the previous legislation), is available to both individuals and companies. The tax authority will not demand any past taxes or penalties because of prior non-compliance.

In accordance with this legislation the following range of assets fall under the amnesty programme:
- Assets held abroad: money, gold, foreign currency, securities and other capital market instruments.
- Assets in Turkey: money, gold, foreign currency, securities, other capital market instruments and immovable assets.

The undisclosed asset may have been acquired in any year; the length of time the undisclosed asset has been in the possession of the taxpayer is irrelevant for the purposes of the amnesty. The disclosing taxpayer is not required to provide any details or supporting documentation regarding the date of initial possession.

In order to benefit from this amnesty, declaration of the undisclosed assets must be submitted on or before December 31st 2019. For offshore assets, the declaration will be made to banks and intermediary institutions. Domestic assets will be declared to the tax offices. It is not sufficient to only declare the assets to benefit from the amnesty; the foreign assets must also be repatriated into Turkey or be transferred into a Turkish bank or intermediary institution account within three months after declaration. The assets declared can be utilised by taxpayers until December 31st 2019 to close loans which they obtained from banks and financial institutions abroad and which were recorded in their legal books as of July 19th 2019. In this type of situation, the physical repatriation requirement for the asset will not apply.

A tax of 1% of the declared value of both foreign and domestic assets will be paid. Banks and financial institutions are responsible for declaring and paying the 1% tax to their tax office through a tax return by the end of the 15th day of the month following the declaration. For domestic assets declared to tax offices, the 1% tax must be paid by the end of month following the declaration.

No inspection, examination or investigation will be started and no tax or penalty will be imposed upon taxpayers for utilising this amnesty.

This amnesty is provided on condition that the declared tax is paid at the due date and other required conditions are satisfied.

25 United Kingdom

Due to the current system of taxation in the UK that applies to non-resident landlords holding UK property as investment, there is not a specific focus on the accounting year end as a key time to consider tax issues.

Typically, investors who acquire UK property invest through non-UK resident companies and are required to submit a UK income tax return for a fiscal year which runs from April 6th to April 5th. It is therefore common that the accounting year does not correlate with the fiscal year.

For these reasons there is generally no requirement to undertake specific actions at year end to secure certain tax treatments. However, it is important that the following issues are considered in relation to existing investments in UK real estate on at least an annual basis.

Taxation of rental income

Non-residents who receive rental income from direct investments in UK real estate have typically been subject to UK tax under the income tax regime at basic rate UK income tax at 20% on net income from the rental business (either through withholding or by direct assessment).

From April 6th 2020 however, non-UK resident companies will come within the charge to corporation tax on UK property rental income although withholding at the basic rate of income tax may still apply.

Apart from the differences in the tax rates which will apply (17% corporation tax from April 2020 rather than 20% income tax), there are differences in the way taxable profits are calculated depending on whether the profits are subject to corporation tax or income tax. As a consequence of bringing non-UK tax resident companies within the charge to corporation tax there will therefore be, amongst other things, additional restrictions on the deductibility of interest, deductions related to hybrid mismatches and restrictions on the amount of losses brought forward from earlier periods that can be offset.

The loss restriction limits to 50% the amount of profit against which brought forward losses in excess of £5m can be offset. However the loss restriction will only apply to losses accruing from April 2020. Income tax losses arising before April 2020 are available for carry forward in full against future UK property business profits of the non-UK resident company.

The non-UK corporate landlord will be subject to UK corporation tax filing and payment rules, which will include (except for the first corporation tax accounting period), the quarterly payment regime.

Also, the group relief provisions are extended to include profits/losses of such non-UK tax resident companies that will fall within the charge to corporation tax.

Non-residents which are non-corporates will continue to be subject to income tax on rental income. For individuals income tax rates are up to 45%.

Financing costs

Shareholder financing which is used for a UK property investment business should be provided on arm's length terms to comply with the UK transfer pricing rules in order to be fully tax deductible.

In addition, non-UK corporate landlords coming within the charge to corporation tax in respect of rental income from April 6th 2020 will become subject to the "corporate interest restriction" rules introduced in accordance with the OECD's BEPS project. The starting point is to restrict finance cost deductions to 30% of tax EBITDA. There is also a GBP £2m de minimis and the option of using an alternative group ratio or a public infrastructure exemption if this will provide a better result.

Support for the level of shareholder financing and the terms on which this financing is provided should be retained. It should be considered what support is available for the shareholder financing for each UK property investment.

In addition, the impact of the corporate interest restriction should be considered.

Capital allowances

Capital allowances provide tax relief for capital expenditure on plant and machinery in UK properties, and, since October 29th 2018 providing certain requirements are met, also the cost of the construction, conversion and renovation of certain buildings ('Structural Buildings Allowances').

Each UK property investment should be reviewed to ensure the maximum entitlement to capital allowances is being claimed.

Disposals by non-residents

Prior to April 6th 2019, only certain direct disposals of UK residential property were subject to UK tax for non-UK residents. However, from April 6th 2019, UK tax is charged on capital gains made by non-residents on direct and certain indirect disposals of all types of UK immovable property.

The indirect disposal rules apply where a person makes a disposal of an entity in which it has at least a 25% interest (or any interest in certain collective investment vehicles which include UK REITs and PAIFs) where that entity derives 75% or more of its gross asset value from UK land.

The 25% ownership test applies where the person holds at the date of disposal, or has held within two years prior to disposal, a 25% or more interest in the property-rich company. This holding may be directly, or through a series of other entities, or via connected persons.

The 75% "property richness" test looks at the gross assets of the entity being disposed of. Where a number of entities are disposed of in one arrangement, their assets will be aggregated to establish whether the 75% test is met.

There is a trading exemption, so that disposals of interests in property-rich entities where the property is used in a trade are excluded from the charge, and existing reliefs and exemptions available for capital gains continue to be available to non-UK residents, with modifications where necessary. Those who are exempt from capital gains for reasons other than being non-UK resident continue to be exempt (for example, overseas pension schemes and certain charities).

In addition, the provisions of any relevant double tax treaty however need to be considered.

All non-UK resident companies (including deemed companies) are charged to corporation tax rather than capital gains tax applicable to individuals and certain trusts on their gains. The provisions relating to annual tax on enveloped dwellings (ATED)-related CGT on UK residential property have been abolished.

Losses arising to non-UK residents under the new rules are available. However, from April 2020, the offset by companies of carried forward capital losses will be limited to 50% only of the capital gains arising in a later accounting period, subject to a de minimis applied on a group basis.

The gain or loss is calculated using the market value of the asset but there is an option to calculate the gain or loss on a disposal using the original acquisition cost of the asset. However, where the original acquisition cost is used in the case of an indirect disposal, and this results in a loss, this will not be an allowable loss.

Accounting changes

A non-resident company is required to calculate the profits of its UK property rental business in accordance with UK GAAP if it does not already prepare accounts under UK GAAP or IFRS. Otherwise it is the company's UK GAAP/IFRS accounts which are used to calculate the profits of the UK property rental business. It is necessary therefore to keep up with any changes in UK GAAP and investors should consider the implications for their UK tax liability.

Residential property

Non-resident owners of residential property in the UK are potentially subject to an annual tax in relation to their ownership (Annual Tax on Enveloped Dwellings or ATED). Prior to April 2019, a specific UK capital gains tax charge applied to non-UK resident investors in UK residential property. However, from April 6th 2019, gains on residential property fall within the UK capital gains provisions applying to non-UK resident investors generally (see above).

Individual non-resident owners of residential property in the UK have from April 2017 been subject to restrictions in relief for finance costs against their higher (40%) and additional rate (45%) income tax liabilities. Between 2017 and 2020, current reliefs are being phased out and replaced with a basic rate (20%) tax reduction.

Landlords of fully furnished residential properties were historically able to claim an annual "wear and tear" allowance of 10% of the rental income. From April 2016, the wear and tear allowance was replaced by relief for the actual cost of replacement furniture, furnishings, appliances and kitchenware provided for the tenant's use.

Asia Pacific

1 India

Foreign investment framework in real estate sector in India

Direct investment by foreign investors in property situated in India

A foreign investor is not permitted to own immovable property directly in India. However, this restriction does not apply to a Non-resident Indian, Person of Indian Origin (other than for agricultural land, plantation property, farm house) and a foreign company acquiring immovable property (through a branch or project office or other place of business in India) for carrying out its business activities.

Investment in securities of Indian Company engaged in construction and development and other real estate related activities

A foreign investor can invest in permitted securities of an Indian company undertaking construction and development of real estate projects, Special Economic Zones (SEZs), industrial parks, business centres, townships, hotels, etc., including leasing of stabilised assets subject to certain conditions provided under the Foreign Direct Investment (FDI) policy of the Government of India.

A foreign investor is permitted to exit the project on completion, or after development of trunk infrastructure, or fulfilment of three-year lock-in period, whichever is earlier. However, lock-in condition is not applicable to investments made in Hotels & Tourist Resorts, Hospitals, SEZs, Educational institutions, and Old Age Homes.

Additionally, investment can also be made through the Foreign Portfolio Investment route. Recently, a new voluntary retention route of investment has been introduced by the Indian regulatory authority, Reserve Bank of India, to encourage Foreign Portfolio investors in order to undertake long term investments in the Indian debt market.

Corporate tax

The profits of an Indian company are generally subject to a corporate tax rate of 30% or 25%[1] (plus applicable surcharge and health and education cess) as may be applicable.

[1] If turnover or gross receipt of the company in Financial Year ('FY') 2017–18 i.e. April to March is less than Indian Rupees ('INR') 4 billion.

Recently, an amendment has been introduced, which provides and Indian company an option to pay corporate tax at the rate of 22% (plus applicable surcharge and health and education cess) on its income. The benefit of lower tax rate would be available if such Indian company does not avail the specified exemption or incentives. Once this option is exercised, the Indian company cannot subsequently withdraw it. Further, such Indian companies exercising the option to pay tax at the rate of 22% would also not be required to pay minimum alternate tax (MAT).

The manner of taxation for an Indian company engaged in real estate sector depends on the nature of the activity carried out by the company.

Construct and sell model

Indian companies engaged in development and construction of residential projects, typically, follow a “construct and sell” model.

Income from sale of property under this model is characterised as business income and taxable at applicable rates, on a net income basis. Development and borrowing cost incurred to develop the property is considered as part of inventory and allowed as deduction.

Construct/Purchase and lease model

Indian companies engaged in development of office space e.g. Commercial Park, SEZ development follow “construct/purchase and lease” model. Certain Indian companies also follow hybrid models e.g. retail mall assets, where it could be combination of fixed lease and revenue share of the tenants.

The taxability under “construct/purchase and lease” model would largely depend on the facts and business objectives of the company.

In a case where the primary objective of the company is to lease property together with provision of other related facilities/amenities, it should be characterised as business income and would be taxed in a manner similar to “construct and sell” model however, the borrowing cost incurred to develop the property is usually capitalised and depreciation allowance can be claimed by the company in that respect.

Further, Central Board of Direct Taxes has issued a Circular stating that the income arising on letting out of buildings/developed space, along with other amenities, in an Industrial Park/SEZ is to be treated as profits and gains of business or profession subject to fulfilment of conditions prescribed under the notified schemes.

In case, the company earns rental income only from leasing (without provision of related facilities/amenities), such rental income is characterised as income from house property. There is a specific tax computation mechanism prescribed to determine the quantum of income taxable under the head income from house property.

A standard deduction of 30% of rental income, in addition to deduction for interest expenses and property taxes paid at actuals is provided for before arriving at taxable income under this head.

Characterisation of income earned by a company engaged in earning rental income from leasing activity has been a matter of debate and been subject to protracted litigation with the tax authorities. The taxability is a function of systematic/organised activities carried out by the taxpayer to provide services to the lessees.

Change in Accounting policy

Generally, Indian Company engaged in real estate sector has been recognising income and accruing expenses based on the Percentage-Of-Completion Method (POCM) as against Project Completion Method (PCM).

On March 28th 2018, the Ministry of Corporate Affairs (MCA) has notified Ind AS* 115, “Revenue from contracts with customers”, effective for accounting periods beginning on or after April 1st 2018 (replacing Ind AS 18, ‘Revenue’ and Ind AS 11, ‘Construction contracts’ and related appendices, including the guidance note on real estate). The objective of the new revenue standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries and across capital markets.

The core principle of Ind AS 115 is that an entity will recognise revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. This core principle is described in a five-step model framework:
1. identify the contracts with customers;
2. identify the separate performance obligation;
3. determine the transaction price of the contract;
4. allocate the transaction price to each of the separate performance obligations and
5. recognise the revenue as each performance obligation is satisfied.

The complexity of applying this approach and of producing the detailed disclosures required by the new standard in the real estate sector may require modifications to existing accounting systems and, in some cases, entities may conclude that they should develop new systems and processes.

Prior to Ind AS 115, real estate companies in India that were reporting under Ind AS followed accounting prescribed under the Guidance Note on Accounting for Real Estate Transactions (Guidance Note) issued by the ICAI. The objective of the Guidance Note is to recommend the accounting treatment to be followed by the companies dealing in real estate as sellers or developers and covers all forms of transactions in real estate. According to the Guidance Note, an entity can start recognising revenue on a percentage of completion basis only when:

a. 25% of the construction and development cost of the project has been incurred;
b. 25% of the saleable project area is secured by contract and
c. 10% of the contract consideration as per the agreement of sale has been realised.

Ind AS 115 does not refer to the Guidance Note, this may result in a change in the profile of revenue and profit recognition for real estate companies. Real estate companies will need to consider:

- whether revenue should be recognised over time or at a point in time;
- the extent to which distinct goods or services are supplied, which should be accounted for separately;
- whether particular costs relating to obtaining a contract must be capitalised;
- whether revenue must be adjusted for the effects of the time value of money;
- how to account for contract modifications and
- the impact of new guidance where pricing mechanisms include variable amounts.

The new standard requires significantly more disclosures relating to revenue and entities will need to ensure that appropriate processes are in place to gather the information. The new standard may also have an impact on an entity's budgeting and reporting process, IT systems, internal control systems, employee key performance indicators (KPIs) and bonuses. It may also have tax implications in many circumstances. Hence, early identification of the implications of the new standard is imperative.

On March 30th 2019, MCA notified Ind AS 116*, "Leases", the new lease accounting standard which is effective for annual reporting periods beginning on or after April 1st 2019.

Ind AS 116 has replaced the guidance in Ind AS 17, "Leases". Ind AS 116 defines a lease as a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration. Under Ind AS 116 lessees have to recognise a lease liability reflecting future lease payments and a "right-of-use asset" for almost all lease contracts. This is a significant change compared to Ind AS 17, under which lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). Ind AS 116 gives lessees optional exemptions for certain short-term leases and leases of low-value assets.

In the statement of profit and loss lessees will have to present interest expense on the lease liability and depreciation on the right-of-use asset. In the cash flow statement, cash payments for the principal portion of the lease liability and its related interest are classified within financing activities. Payments for short-term leases, leases of low-value assets and variable lease payments not included in the measurement of the lease liability are presented within operating activities.

The accounting by lessors will not significantly change. As under Ind AS 17, the lessor will continue to classify leases as either finance or operating, depending on whether substantially all of the risks and rewards incidental to ownership of the underlying asset have been transferred. For a finance lease the lessor recognises a receivable, and for an operating lease the lessor continues to recognise the underlying asset.

Ind AS 116 adds significant new, enhanced disclosure requirements for both lessors and lessees.

On transition, lessees can choose between full retrospective application or a simplified approach that includes certain reliefs and does not require a restatement of comparatives. In addition, as a practical expedient entity are not required to reassess whether a contract is, or contains, a lease at the date of initial application (that is, such contracts are 'grandfathered').

In the absence of any particular method prescribed under Income-tax Act, 1961 for recognition of revenue, the taxability of Indian Companies engaged in real estate sector would be linked with the accounting method generally deployed by respective taxpayers.

However, Indian Company may continue to follow different method for the purpose of Income-tax Act, 1961 which has been followed consistently over the years and accepted by the tax authorities subject to any specific method under the Income Computation and Disclosure Standards.

*Indian Accounting Standards (Ind AS) is mandatorily applicable for listed companies, companies with prescribed quantum of net-worth and companies that are holding companies, subsidiaries, joint ventures and associates (under Ind AS) of such listed companies or companies with prescribed net-worth.

Taxation of notional rental income

Notional rental income, in respect of building and land appurtenant thereto should be considered to be nil for a period up to two years from the end of the FY in which the construction completion certificate is obtained from the relevant authority, provided that the building and land appurtenant thereto are held as stock-in-trade and has not been let out during the whole (or any part) of the year.

However, if the building and land appurtenant thereto is not held as stock – in-trade, notional rent could be chargeable to tax from the date construction completion certificate is obtained.

Joint development agreement (JDA)

Execution of JDA between the owner of immovable property and the developer triggers either business income or capital gains tax liability in the hands of the owner based on the fact that whether such immovable property has been held as stock-in-trade or capital asset.

In case of business income in the hands of property owners, tax would be chargeable on the date on which possession of property is handed over.

However, in case of capital gains tax liability in the hands of the property owners, there are divergent views and practices as regards the timing and computation. Generally, the capital gains tax liability is triggered in the hands of the land owner in the year in which the possession of immovable property is handed over to the developer for development of a project. With a view to clarify and minimise the hardship caused due to timing difference in the hands of Individual and Hindu Undivided Family (HUF), tax provisions relating to capital gains from JDA, below are the key provisions:

- Timing of taxability – Year in which the completion certificate for the project (whole or part) is issued by the relevant authority. If the share in the project is sold prior to the receipt of the completion certificate, taxability in the year of actual sale
- Deemed consideration for levying tax on share in the project – Aggregate of the stamp duty value of the relevant share of project on the date of issue of the completion certificate and cash consideration received
- Tax cost base for eventual sale of built up area – Deemed consideration to be treated as cost of acquisition for computing taxable income on subsequent transfer of share in the project
- Tax deduction at source – Tax deduction at the rate of 10% on the portion of cash consideration.

However, the timing of capital gains tax liability in the hands of taxpayer other than Individual and HUF continue to be subject matter of dispute with tax authorities.

Please refer to “Indirect taxes” section for implications of JDA under Goods and Service Tax Act, 2017 (GST).

Conversion of nature of properties held as “inventory” to “capital asset”

Any profit or gains arising from conversion of nature or treatment of immovable property held as inventory into a capital asset shall be chargeable to tax as business income based on the Fair Market value (FMV) (determined in a prescribed manner) of the inventory on the date of such conversion.

Further, for computing capital gains arising on the transfer of such converted capital assets, the aforesaid FMV shall be the cost of acquisition thereof and the period of holding shall be reckoned from the date of such conversion.

Sale of properties

Sale of properties held as capital assets (i.e. not held for trading purposes) – Long-term capital gains are generally taxable at 20% (plus applicable surcharge and health and education cess) and short-term capital gains are taxable at 30% (plus applicable surcharge and health and education cess).

Anti-abuse provision

Sale of properties without consideration or for an inadequate consideration is subject to taxation at a deemed value (usually determined based on the values imputed for stamp duty purposes).

However, in order to minimise hardship in case of transactions in the real estate sector, where the variation can occur in respect of similar properties in the same area because of a variety of factors, safe harbour provisions were introduced. Thus, from April 1st 2019 onwards no adjustments shall be made in a case where the variation between stamp duty value and the sale consideration is not more than 5% of the sale consideration.

Corporate restructuring

Transfer of properties which may occur by way of corporate restructuring (such as amalgamations, demergers, etc.) could be tax neutral subject to conditions.

Tax incentives

Investment linked tax incentives

Investment linked tax incentives are available for certain asset classes (such as certain slum redevelopment or rehabilitation projects, affordable housing projects etc. which meet the requisite certain criteria).

Slum redevelopment projects/Affordable Housing projects

Indian company is eligible to claim deduction of any capital expenditure incurred in the year of expenditure subject to certain conditions for any specified business such as:

- developing and building a housing project under a scheme for slum redevelopment or rehabilitation; or
- developing and building a housing project under a scheme for affordable housing; or
- building and operating a new hotel of two star or above category; or
- building and operating a new hospital with at least one hundred beds for patients; etc.

Profit linked tax incentives

Profit linked tax incentives are provided, amongst others, to companies, i) developing and building affordable housing projects; and iii) SEZ units, subject to conditions.

a. SEZ Unit related:
   Profit linked incentives to SEZ units has been phased out for units not commencing activities by April 1st 2021.
b. Affordable Housing projects related:
   With a view to provide affordable housing as part of the larger objective of “Housing for all”, tax incentive is provided in form of 100% profit-linked deduction to the tax payer engaged in developing and building affordable housing projects, if such housing project is approved by competent authority after June 1st 2016 but before March 31st 2020 subject to certain conditions.

Key eligibility conditions for an affordable housing project, inter alia, are as follows:

- The carpet area of the residential unit does not exceed 60sqm for specified metropolitan cities or 90sqm for other locations;
- The plot of land measuring not less than 1000sqm in specified metropolitan cities or not less than 2000sqm in other locations;
- Stamp duty value of a residential unit is less than INR4.5m.

Minimum Alternative Tax (MAT)

Where the tax liability of an Indian company (computed in the manner prescribed) is less than 15% of its adjusted book profits, MAT at the rate of 15% (plus applicable surcharge and health and education cess) on such adjusted book profits is payable by companies that do not opt to pay corporate tax at the rate of 22% (plus applicable surcharge and health and education cess).

MAT credit is available to be carried forward for 15 years.

Real Estate Investment Trusts (REITs)

REIT is an investment vehicle launched by a Sponsor in the form of a trust duly registered with the Securities and Exchange Board of India (SEBI). REITs are required to be listed on the stock exchange and hold completed and rent-generating properties in India either directly or through holding company (Hold Co) or Special Purpose Vehicles (SPVs) that hold rent-generating properties in India which inter alia includes office buildings, shopping malls, apartments, warehouses, etc.

Conditions associated with REIT, inter alia, include the following:
- REITs are prohibited from investing in vacant land or agricultural land or mortgages (with certain exceptions)
- At least 80% of the value of a REIT to be in completed and rent generating assets. Such property to be held for not less than three years from the date of acquisition of property by REIT/Hold Co/SPVs.

REITs have been accorded effective tax pass through status, whereby certain specified income of the REITs are taxable in the hands of the unitholders of the REIT – for non-residents, relief under the applicable tax treaty is available, if any. There is, however, no specific pass through for distributions of gains from disposal of property or shares.

Dividend income[2] received by the REIT from SPVs should be exempt from tax in the hands of the REIT. However, where the total income of the REIT includes dividend income received from Indian companies, in excess of INR1m, there is a risk of such excess dividends being taxed at the rate of 10% (plus applicable surcharge and health and education cess).

Sale of units of the REIT is subject to a preferential tax regime i.e. long-term capital gains is taxable at the rate of 10% and short-term capital gains is taxable at 15% (plus applicable surcharge and health and education cess). These preferential rates are however applicable subject to payment of Securities Transaction Tax (STT) on the sale transaction.

Where, however, STT is not paid on sale of REIT units, the long-term capital gains would be taxable at 20% and short-term capital-gains at 30% (plus applicable surcharge and health and education cess) as the case may be applicable.

Tax on repatriation to non-residents

Income earned on investments made by non-residents in an Indian company is typically in the form of capital gains, interest and dividends.

[2] The company declaring dividend is liable to pay dividend distribution tax (DDT) at the rate of 15% to be grossed up, plus surcharge at 12% and health and education cess at 4% on tax and surcharge. Further, an exemption has been provided from the levy of DDT in respect of dividend declared, distributed or paid by the company to the REIT, subject to the REIT holding 100% of the equity share capital of the company and the dividend declared being out of current income.

Ordinarily, long-term capital gains on sale of unlisted shares are taxable at 10% (without giving any relaxation for inflation). Further, short-term capital gains on sale of other securities are usually taxable at 40% (plus applicable surcharge and health and education cess) in case of transferor being foreign companies.

In case of sale of listed equity shares after April 1st 2018, long-term capital gains is taxable at 10% and short-term capital gains is taxable at 15% (plus applicable surcharge and health and education cess), subject to payment of STT both at the time of acquisition and disposal. In computing the long-term capital gains on sale of listed equity shares acquired prior to January 31st 2018, cost of acquisition can be increased to the extent of market value of such shares as on January 31st 2018, if any. Similar capital gains tax treatment on listed shares is extended in case of foreign institutional investors as well.

Dividend from Indian Companies is exempt from tax in the hands of the recipient.

Interest income is generally taxable at 40% (plus applicable surcharge and health and education cess) in the hands of foreign companies. However, in certain specified cases, interest income could be subject to concessional tax rate of 5% (plus applicable surcharge and health and education cess), subject to conditions. Further, non-residents are also eligible for certain relief under the applicable tax treaty, subject to conditions.

Transfer pricing

The Income-tax Act 1961 provides that the price of any international transaction between Associated Enterprises (AE) is to be computed with regard to the arm's length principle. However, such transfer pricing legislation is not applicable when the computation of the arm's length price has the effect of reducing income chargeable to tax or increasing losses in India. This is aligned with the legislative intent to protect the Indian tax base.

Further, the provisions relating to domestic transactions have been rationalised so as to reduce compliance burden and ensure effective reporting.

Thin Capitalisation Norms

Where an Indian company or a permanent establishment of a foreign company incurs expense by way of interest or similar consideration exceeding INR10m, in respect of any debt from a non-resident AE, any excess interest as defined shall not be deductible in computation of income from business.

Excess interest is defined as the i) total interest in excess of 30% earnings before interest, tax, depreciation and amortisation (EBITDA) or ii) interest paid to AEs, whichever is lower.

The excess interest, which is disallowed can be carried forward to the following FY and allowed as a deduction against profits of the subsequent years, subject to the maximum allowable interest expenditure stated above.

The excess interest can be carried forward for a period of eight FY immediately succeeding the FY in which excess interest is computed.

Losses carried forward	Losses of a particular FY are typically allowed to be carried forward for the next eight FY, subject to fulfilment of certain conditions. There are no time limits for carrying forward unabsorbed depreciation. Where there is a change in shareholding of closely held companies beyond 49%, unexpired losses (but not unabsorbed depreciation) should lapse. However, to be eligible to carry forward losses, it is important to file annual income-tax returns on or before the prescribed due dates.
Reorganisation of SEZ units/ developers	Any re-organisation of SEZ units can be undertaken only with the prior approval of SEZ authorities subject to the condition that the developer/co-developer shall not opt out or exit out of the SEZ and continues to operate as a going concern. Following are certain examples of reorganisation: • Change in shareholding pattern; • Business transfer arrangements/merger/demerger; • Change of constitutions; etc. Further, the authorities have clarified that prior approval is required before the SEZ entity/unit is recognised by the new name/arrangement in all the records.
General Anti-Avoidance Rule (GAAR)	GAAR provisions could be invoked by the Indian income-tax authorities in case an arrangement is found to be “impermissible avoidance arrangement”. GAAR provisions are effective from FY 2017–18. The guidelines for application of the provisions of GAAR have also been prescribed. The onus to prove that the main purpose of an arrangement was to obtain any tax benefit is on the income-tax authorities. The tax payer can approach the Authority of Advance Rulings for a ruling to determine whether an arrangement can be regarded as an impermissible avoidance arrangement. However, GAAR applies to impermissible avoidance arrangements, irrespective of the date on which they have been entered into, in respect of tax benefits obtained from the arrangements on or after April 1st 2017.
Stamp duty	Stamp duty is generally applicable on document of sale of immovable property. The rate of stamp duty varies from state to state. Typically, the stamp duty ranges from 5% to 15%. Corporate restructurings/transfer of shares also attract stamp duty.
Municipal tax	Municipal corporations or other local bodies are entitled to recover property taxes from buildings constructed in cities and towns. The property taxes are levied on “rateable values”, fixed on the basis of market value of the property or the rental returns, which the property owners derive from the property.

Indirect taxes

Taxability under GST law

GST does not apply on sale or purchase of land, or a building which is complete, or on the value of land in any construction project. However, “construction of building”, “works contracts”, “leasing of land or building” and any other “construction-related activities” have been treated as “supply of service” and are therefore taxable under the GST law. GST would apply on sale of under-construction of residential and commercial properties i.e., prior to the receipt of Occupancy Certificate (OC) from Governmental authorities.

Prior to April 1st 2019, GST was applicable on sale of under-construction of residential and commercial properties i.e., prior to the receipt of OC at 18% (12% in case of specified affordable housing projects or slum rehabilitation projects) with Input Tax Credits (ITC) and a flat 33% abatement for value of the land; the effective rate of GST were 12% and 8%.

From April 1st 2019, the Government has introduced several concepts in the GST regulations which mirror GST provisions under the Real Estate (Regulation and Development) Act, 2016 (RERA) such as “Promoter”, “Real Estate Project”, “Carpet Area”, etc. The GST rates applicable to new projects commencing after April 1st 2019 and ongoing projects as on March 31st 2019 (for which the option to pay tax as per the revised framework has been exercised by a developer) are summarised below:

Segment	GST rates with effect from April 1st 2019
Affordable housing	1%[1] (without ITC)
Other residential housing	5%[1] (without ITC)
Commercial property located within a residential property	5%[1] (without ITC)

[1] Effective GST rate after 1/3rd land deduction

W.e.f. April 1st 2019, the concept of “Affordable Housing” under the GST law was amended to mean units sold with:
a. Carpet area not exceeding 60sqm (in metropolitan cities) and 90sqm (in non-metropolitan cities); and
b. Value not exceeding INR4.5m.

Also, to avail the benefit of the lower GST rates introduced w.e.f. April 1st 2019, various conditions are required to be adhered to by the developers; for instance, fulfilment of threshold limits for procurements from GST registered dealers, maintaining project-wise details, bar on availment of ITC, etc.

GST also applies on services such as property management and maintenance, leasing of land, renting of immovable property for commercial purposes, services of real estate agents, architects, etc. However, GST is not applicable on the following services which are specifically exempted:
- Renting of immovable property for residential use; and
- Lumpsum payment for long term leasing of land (30 plus years) for industrial purpose from a government entity.

It may be noted that litigation at various levels is currently underway on whether GST can be imposed on long term lease of land/building, which is otherwise treated as a sale from various perspectives.

ITC

The GST law allows utilisation of ITC of GST paid on inputs, input services and capital goods against taxes payable on construction or works contract services provided by developers. However, the GST law restricts ITC of GST paid on i) goods and services procured for construction of a building which is used on own account; and ii) works contract services when used in creation of an immovable property. Moreover, with the introduction of revised composition GST rates applicable effective April 1st 2019, there is an express restriction of availment of ITC by a developer of residential property operating under the revised GST framework.

Accordingly, credit restrictions apply to commercial constructions developed for leasing/rental purposes or immovable property constructed for self-use. The restriction of ITC for construction of commercial property for leasing/renting out is being debated by the industry in light of a recent favourable judicial decision[3] allowing ITC to the developer of a mall at the construction stage. A writ petition[4] on this issue is pending before the Delhi High Court.

Joint Development Agreement (JDA)

Under a JDA, land owners and developer jointly contribute to develop a property. The land owner transfers the development rights in the land to the developer and are usually remunerated by way of an area or revenue share in the project.

The taxability of transfer of development rights was widely disputed by the industry considering that ambiguity prevails on its classification as “land” (which is outside the ambit of GST). Post April 1st 2019, the Government has exempted the transfer of development rights by a landowner to the developer (registered under RERA) for development and sale of residential property prior to issuance of OC subject to certain conditions. Currently, there are divergent views as regards the timing and valuation for computation of GST on the supply of development rights.

Supplies to Special Economic Zone (SEZ) developers and units

Goods and/or services provided to SEZ developers and SEZ units are zero rated under the GST law. Thus, a person supplying goods and/or services to an SEZ developer or SEZ unit may make such supplies without payment of GST; also, as a consequence of zero rating, such supplier will be entitled to seek a refund of GST paid on items used for supply to the SEZ/SEZ unit. Property rental services provided by a SEZ developer continues to be GST free.

[3] Safari Retreats Private Limited vs Commissioner of Central tax (TS-350-HC-2019(ORI)-NT).
[4] Bamboo Hotel and Global Centre (Delhi) Pvt. Ltd (W.P.(C) 5457/2019).

Anti-profiteering

Anti-profiteering is a transitionary provision initially introduced for a period of two years (which has been further extended by two years), as per which businesses are required to mandatorily pass on benefits derived from reduction in rate or benefit from ITC to its customers. The industry is grappling to determine the actual benefit on account of GST as there is lack of clarity on how the benefit (if any) is to be calculated. The Government has been aggressive, especially with the real estate sector, to investigate businesses for non-compliance under anti-profiteering provisions and had issued the first administrative instruction on this issue for the real estate sector.

Additionally, as there have been instances of anti-profiteering notices issued to builders/developers on implementation of GST law, there could be incremental anti-profiteering compliances required to be maintained by builders/developers considering the reduced rate structure with effect from April 1st 2019. Also, certain anti-profiteering investigations on builders/developers have been completed which is indicative of the approach adopted by the authorities.

Real Estate (Regulation and Development) Act 2016 (RERA)

The Real Estate (Regulation and Development) Act 2016, seeks to protect the interests of buyers and to promote transparency, accountability and efficiency in the sector has become effective from May 1st 2016 and seeks to put in place an effective regulatory mechanism for orderly growth of the sector.

2 Indonesia

Rental income

Rental income on property owned either by a corporation or an individual is subject to final income tax at a rate of 10% from the gross rental fees (excluding VAT). This is withheld by a company tenant, but for individual and foreign tenants, the landlord is obliged to pay the 10% final tax due on the rental income through self-assessment mechanism. This 10% tax constitutes the final settlement of the income tax for that particular income.

Gross rental value is the total amount paid or payable by the tenant in whatever name or form with respect to land and/or buildings rented. The gross rental value includes repair costs, maintenance expenses, security expenses and service charges, regardless of whether these exist in a separate agreement or are included in the rental agreement. As the rental income is subject to final tax, all expenses related to the property rental business are non-deductible. Other income (after allowable deductions) of a real estate company, for example property management, will be subject to the normal corporate income tax at a flat rate of 25%.

The corporate tax rate of 25% may be reduced to 20% for listed companies that satisfy all of the following conditions:
- total shares held by the public amount to a minimum of 40% of the total paid in capital;
- total shares are held by at least 300 parties with each holding less than 5% of total paid in capital; and
- the above conditions must prevail for at least six months or 183 calendar days within one fiscal year.

Transfer of land and building

A transfer of rights to land and building will give rise to income tax on the deemed gain on the transfer/sale to be charged to the transferor (seller). The tax is set at 2.5% of the gross transfer value (tax base). However, for transfers of simple houses and simple apartments conducted by taxpayers engaged in a property development business, the tax rate is 1%. Furthermore, the income from transfers of rights to land and building involving Sale and Purchase Binding Agreement on land and building rights (Perjanjian Pengikatan Jual Beli, or PPJB) are also included in the final tax object. This tax must be paid by the time the rights to the land and building are transferred to the transferee. The tax paid constitutes a final settlement of the income tax for that particular income.

In general, the tax base is the higher of the transaction values stated in the relevant land and building right transfer deed and PPJB based on actual transaction value or amount that should have been received in the case of a related party transaction. However, in a transfer to the government, the tax base is the amount officially stipulated by the government officer in question in the relevant document. In a government-organised auction, the gross transfer value is the value stipulated in the relevant deed of auction.

A notary is prohibited from signing a transfer of rights deed until the income tax has been paid in full.

Duty on the acquisition of land and building rights

A transfer of land and building rights will typically also give rise to BPHTP duty on the acquisition of land and building rights liability for the party receiving or obtaining the rights. BPHTB is a part of regional taxes. Qualifying land and building rights transfers include sale-purchase and trade-in transactions, grants, inheritances, contributions to a corporation, rights separation, buyer designation in an auction, the execution of a court decision with full legal force, business mergers, consolidations, expansions, and prize deliveries.

BPHTB is based on the Tax Object Acquisition Value (*Nilai Perolehan Objek Pajak,* or NPOP), which in most cases is the higher of the market (transaction) value or the NJOP of the land and building rights concerned.

The tax due on a particular event is determined by applying the applicable duty rate of 5% to the relevant NPOP, minus an allowable non-taxable threshold. The non-taxable threshold amount varies by region: the minimum is IDR60m, except in the case of an inheritance, for which starts from IDR300m. The government may change the non-taxable threshold via a regulation.

BPHTB is typically due on the date that the relevant deed of land and building rights transfer is signed before a notary public. In a business merger, consolidation, or expansion, the duty is due on the date of signing of the merger, consolidation or expansion deed. In an auction, the duty is due on the date of signing of the Auction Deed by the authorised officer.

A notary is prohibited from signing a deed transferring the rights until the BPHTB due is paid.

Fiscal Depreciation

For tax purposes, permanent buildings are depreciable in 20 years and non-permanent buildings are depreciable in ten years using the straight-line method. Considered that non-permanent are temporary buildings which materials are not durable, while land is not depreciable.

Other expenses and income

Taxable business profits are calculated on the basis of normal accounting principles as modified by certain tax adjustments.

Where a final tax applies, expenses relating to rental and/or sales/transfers of property, including interest, depreciation, and other costs, are not deductible for corporate income tax purposes.

Withholding tax on sales of very luxury residences

A corporate taxpayer who sells the following luxury goods must withhold/collect (article 22) income tax at 1% (this has been reduced from the previous 5%) of the selling price excluding VAT and Luxury Sales Tax:
- Landed houses priced at more than IDR30 billion or building area of more than 400sqm;
- apartments, condominiums, and similar types of building selling for more than IDR30 billion or having building area of more than 150sqm.

Income tax collected is creditable for the purchasers of goods.

Tax loss carry forward balance and statutory of limitation for issuing a tax assessment

Tax losses may be carried forward for a maximum of five years.

A carry back of the tax losses is not permitted. Where a final tax applies, tax losses cannot be carried forward. A company is engaged in the property business (rental or sales of land and buildings) can no longer carry forward its tax loss.

Under the current Tax Administration Law, the Directorate General of Taxation (DGT) can issue an underpaid tax assessment letter for the years 2015 and onwards within five years after the incurrence of a tax liability, the end of a tax period (month), or the end of (part of) a tax year.

Real estate investment fund

The income that is received or obtained from the transfer of real estate assets to a Special Purpose Company (SPC) or Collective Investment Contracts in the form of a Real Estate Investment Fund (*Kontrak Investasi Kolektif – Dana Investasi Real Estate,* or KIK-DIRE) is subject to a 0.5% final tax on the gross value of the assets transferred. If the transfer is made to a related party, the gross value of the assets transferred is the amount that should have been received or obtained on the transfer. If the transfer is made to a third party, the gross value of the assets transferred is the amount that is actually received or obtained on the transfer.

The procedures for this final tax payment and reporting, which is similar to the general procedures in the event of land and building transfer. Further KIK-DIRE is considered to be a low-risk VATable entrepreneur, which is eligible to request for preliminary VAT refund.

VAT

VAT applies to real estate transactions at a rate of 10%. For these purposes, real estate transactions include rental and sales of real estate properties. Charges for common services for office buildings and the like are subject to VAT at 10% of the service charges.

VAT on the sale price of land and buildings, as part of a real estate or industrial estate price, is levied at the rate of 10% of the invoice value.

VAT on any self-construction work on the following buildings is levied at 2% of total costs incurred or paid, exclusive of the acquisition price of land:

- residential house or place of business; and
- building space which is equal to or bigger than 200sqm.

Excluded from the VAT is the delivery of a basic house, very basic house, basic apartment, rented cottage, student dormitory, and other housing as defined by the Minister of Finance upon hearing the consideration of the Minister of Settlement and Regional Infrastructures (e.g., religious and social buildings). In addition to the exemption, services provided by the building contractors for the construction of places which are merely intended for worship purposes are also excluded from VAT.

Luxury sales tax (LST)

LST is levied at 20% on apartments, condominiums, luxury house and town houses of the type of strata and/or non-strata title (disregarding the type of title), and those of similar type with a sale price of IDR30 billion or more.

Land and building tax

Land and building tax (*Pajak Bumi dan Bangunan,* or PBB) is a type of property tax chargeable on all land and/or buildings, unless exempted. PBB is a part of regional taxes which are governed under Regional Taxes and Retribution (Law in which each regional government has to issue a regulation to regulate PBB in its territory.

PBB is payable annually following a Tax Due Notification Letter (*Surat Pemberitahuan Pajak Terhutang,* or SPPT) issued by the Regional Government.

An individual or an organisation that owns a right to a piece of land, and/or takes benefits there from, and/or owns, controls, and/or takes benefits from a building can by law be regarded as the PBB taxpayer for that piece of land and/or building.

The PBB rate is maximum 0.3% and the tax due is calculated by applying the tax rate on the sale value of the tax object (*Nilai Jual Objek Pajak,* or NJOP) deducted by non-taxable NJOP. The non-taxable NJOP is set at IDR10m at the minimum. Any changes are to be made by issuing a regional regulation.

Profit distributions

Profit distributions in the form of dividends are subject to tax as follows:
For resident shareholders, dividends received from an Indonesian company by a limited liability company incorporated in Indonesia (*Perseroan Terbatas,* or PT), a cooperative, or a state-owned company, are exempt from income tax if the following conditions are met: the dividends are paid out of retained earnings; and for PTs and state-owned companies, the company earning the dividends holds at least 25% of the paid-in capital in the company distributing the dividends.

- If these conditions are not met, the dividends are assessable to the company earning the dividends at the ordinary tax rate together with the company's other income. Upon declaration, dividends are subject to article 23 income tax withholding at 15%. The amount withheld constitutes a prepayment of the corporate income tax liability for the company earning the dividends. Dividends received by resident individual taxpayers are subject to final income tax at a maximum rate of 10%.
- As for non-resident shareholders, the dividends are subject to withholding tax of 20% (or the applicable reduced treaty rate).

3 Japan

Reduction of corporate tax rates and local corporate tax

The effective corporate tax rate for small and medium corporations is approximately 34.59% for tax years beginning on or after April 1st 2018, once local taxes are taken into account. A small and medium sized company is a company i) whose paid in capital is no more than JPY100m and ii) that does not have a parent company whose paid in capital of JPY500m or more. Different rates apply to large corporations. The effective corporate tax rate for a foreign company which does not have a permanent establishment in Japan is approximately 24.22% for tax years beginning between April 1st 2018 and September 30rd 2019 and 25.59% for tax years beginning on or after October 1st 2019.

Limitation on the net operating loss deduction and extension of the applicable period

Large corporations can offset up to 50% of their taxable income by tax loss carry forwards for tax years beginning on or after April 1st 2018. The tax loss carry forward period is ten years for losses incurred in tax years beginning on or after April 1st 2018. For small and medium sized enterprises (and TMKs), the loss limitation percentage does not apply.

Increase Consumption tax

The current consumption tax rate is 10% from October 1st 2019. Some items, for example fresh food, remain subject to consumption tax at 8%. To cope with the multiple consumption tax rates, an invoicing method will be introduced, although not until April 1st 2023, with transitional measures in place for the interim period.

Amendments to the definition of permanent establishment (PE)

As part of a wider OECD blueprint for reforming the principles of international taxation, the definition of a permanent establishment (PE) was modified to align domestic Japanese tax law with the OECD's BEPS Action 7 (Preventing the Artificial Avoidance of Permanent Establishment Status) and related discussion papers.

The reforms broaden the incidence of when an Agent PE arises while at the same time narrowing the scope of when the independent agent exception can apply.

Under the 2018 tax reform, the scope of what falls within an Agent PE was expanded by including an additional classification. An Agent PE may arise through the activities of a person in Japan who habitually acts in the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the foreign taxpayer, and these contracts are for the transfer of the ownership of assets owned by that foreign taxpayer, etc.

Under the 2018 tax reform, notwithstanding the existing criteria, a person is excluded from qualifying under the independent agent exception where that person acts exclusively or almost exclusively for one or more foreign taxpayer(s) to which it is closely related.

These amendments are applicable on or after January 1st 2019, for individual income tax and for the tax years beginning on or after January 1st 2019, for corporation tax.

Changes to determining when a real estate holding company arises

Capital gains derived by a non-resident, without a PE in Japan, from the transfer of shares in either a listed or unlisted corporation (including certain defined trusts) are subject to tax in Japan where the corporation predominantly holds real estate in Japan, and the non-resident (including, by aggregation, any special related persons) owns more than 5% of the shares (if the corporation is listed) or more than 2% of the shares (if a private corporation) at the prior fiscal year-end in which the shares are sold, unless relief applies under a double tax treaty.

Under current law, a corporation is treated as predominantly holding real estate if 50% or more of its assets consist of real estate in Japan (inclusive of land, buildings, shares in other corporations or specified trusts that predominantly hold real estate, etc.).

The 2018 tax reform expands the scope of when a real estate holding company is tested from the date of transfer to any day preceding one year from that date.

This amendment is applicable on or after January 1st 2019, for individual income tax and for the fiscal years beginning on or after April 1st 2018, for corporation tax.

Tax administration procedures – e-filing requirement

Large corporations need to file their corporate, consumption, and local tax returns electronically from fiscal years beginning on or after April 1st 2020.

A TMK (tokutei mokuteki kaisha) would be required to file tax returns electronically from fiscal years beginning on or after April 1st 2020, regardless of whether it is a large corporation or not.

Restrictions on interest deductions ('earnings stripping rule')

The current earnings stripping rule will be revised to align with BEPS Action 4, including:

1. Expansion of the scope of interest expense, to include interest paid to third parties, but exclude interest that is subject to Japanese income tax in the hands of the recipient.
2. Lowering of the benchmark fixed ratio from 50% to 20%.
3. Modification of the calculation of "adjusted income", on which non-deductible interest will be calculated, as well as the calculation of the non-deductible interest amount.
4. Lowering the threshold amount of interest expense for the application of the new rules.

The above amendments will be applied to the fiscal tax years beginning on or after April 1st 2020.

4 Korea

Securities transaction tax

Securities transaction tax rate cut for unlisted shares

Real estate transaction in Korea can be made through sale of shares of a company holding real estate. In such as case, securities transaction tax is imposed on the sale of shares of a real estate holding company currently at the rate of 0.5% for unlisted shares.

Starting from April 1st 2020, the securities transaction tax rate on unlisted shares would be lowered from 0.5% to 0.45%.

Property holdings taxes

A Korean Real Estate Fund (REF) is a common collective investment vehicle used for real estate investment in Korea. During the period of holding the real estate by REF, there are two types of property holdings taxes imposed annually on the REF; property tax and composite real estate.

Property tax: Lower single rate (0.24%) was applied to REF, but Starting from FY 2020, regular rates of 0.24%–0.48% will be applicable to private type REF. As for public type REF, the low rate (0.24%) will continue to apply.

Composite real estate tax: REFs are at present exempt from this tax, however, starting from FY 2020, it is going to be imposed on the private type REF at the regular rates of 0.6% to 0.84%. Public type REF will continue to enjoy the exemption.

5 New Zealand

Non-resident investment in New Zealand

Non-residents may invest in New Zealand (NZ) property directly or through a local company, non-resident company, trust or partnership.

Investments in NZ real property by a non-resident may require government approval in some cases. Overseas Investment Office (OIO) consent is required where an overseas person wishes to make an investment in significant business assets (securities, consideration or assets of more than NZ$100m) or to acquire an interest in sensitive land (rural land over five hectares, coastal land, seabed, areas adjacent to reserves or water and following a recent law change, residential land).

There are different consent requirements for different types of land. Broadly, when considering an application for consent, the OIO will assess the good character and the business experience of the overseas person, including its directors and ultimate beneficial owners. Where the investment is in sensitive land, the OIO will also need to identify the benefit the proposed overseas investment brings to NZ against a counterfactual scenario (the likely state of affairs if the overseas investment were to not proceed).

The NZ government is currently conducting a review of the application of NZ's foreign investment regime more broadly.

Real property taxation

Net rental income derived from NZ real property is taxable in NZ –
- At the owner's personal marginal tax rate if the owner is an individual (the highest marginal tax rate in NZ is currently 33%);
- At a flat rate of 33% if the owner is a trust (i.e., trustee tax rate) and the income is not distributed to beneficiaries within a specific tax year;
- At a flat rate of 28% if the owner is a company.

Expenses incurred in deriving rental income are generally deductible (subject to the anti-hybrid rules). These include property costs such as repairs and maintenance, insurance, rates, administration costs and depreciation. Interest on loans used to acquire the property is deductible subject to potential restrictions under any of the thin capitalisation, anti-hybrid or transfer pricing rules.

Capital expenditure in relation to the property is not deductible. Capital expenditure is able to be included in the cost base of the property and depreciated (provided it relates to depreciable property, see further details below).

NZ does not have a capital gains tax. As such, if the property is held on "capital" account, there will not be any taxable gain or loss on disposal (subject to recovery of depreciation deductions noted below). If the property is held on "revenue" account, then any gain or loss will be taxed in the same way as other income earned in relation to the property (outlined above). Generally, property acquired for long term investment for the purpose of earning investment income is held on "capital" accounts. There are some exceptions to this general rule such as where a property is acquired with a purpose or intention of disposal where a property is developed and where a property owner is associated with a builder or land developer.

Tax depreciation

The depreciation rate for buildings with an estimated useful life of 50 years or more is 0%. However, certain components of buildings held on "capital" account are able to be depreciated (such as fixtures and fittings, plant and equipment). Depreciable property such as internal non-load-bearing walls and wiring are depreciable at rates relevant to their estimated useful life (the specific rates are set by Inland Revenue). The components of a building that are able to be depreciated can be dependent on whether the building is residential or non-residential.

Where depreciated assets are sold at a value in excess of the depreciated value, there will be a taxable gain on sale in the year of sale (capped at the amount of depreciation previously deducted).

A tax loss can be claimed on disposal of depreciable property (e.g., fixtures and fittings). A taxpayer is only able to claim a tax deduction for a loss made on the disposal of a building in very limited circumstances.

As noted above, capital expenditure in relation to a building is not deductible. The criteria for capitalising costs for accounting purposes is not the same as the criteria for tax purposes. As a result, there are typically items that are expensed for accounting purposes that need to be capitalised for tax purposes (and, where appropriate, then depreciated for tax purposes over the useful life of the asset).

Transfer pricing

Cross-border related party transactions are subject to transfer pricing (TP) rules. NZ enacted legislation in 2018 that included significant changes to NZ's TP regime for income years starting on or after July 1st 2018. These changes align the NZ TP regime with the new OECD TP guidelines, with the effect of placing a greater focus on economic substance over legal form.

The onus of proof is now on the taxpayer to demonstrate that cross border arrangements are conducted on an "arm's length" basis, and the statute bar for TP matters has been extended from four to seven years. Inland Revenue is adopting a stricter approach to TP compliance. Contemporaneous NZ specific TP documentation will be critical moving forward, and will mitigate the risk of the "lack of reasonable care" penalty being applied if audited.

Cross-border related party financing is also typically subject to the "restricted transfer pricing" (RTP) rules. These rules significantly restrict the way cross-border related party borrowing of more than NZ$10m is priced for NZ income tax purposes.

There are currently no compulsory tax disclosure requirements in NZ relating to related party transactions. However, it is expected that some taxpayers will be required to disclose certain related party transactions as part of a new "BEPS disclosure" which is expected to be introduced by the Inland Revenue (this disclosure will also require information in relation to taxpayers' thin capitalisation and anti-hybrid positions where relevant).

Thin capitalisation rules

Inbound thin capitalisation rules apply to non-residents who invest in NZ to limit interest deductions where debt exceeds certain levels. Significant changes were introduced with respect to NZ's thin capitalisation regime in 2018, applying to income tax years starting on or after July 1st 2018.

A portion of a NZ taxpayer's interest expense will be disallowed where an entity's debt percentage (calculated as total debt/total 'net' assets) exceeds both of the following:

- 60% for "inbound" investment (i.e. non-NZ owned groups) (or 75% for "outbound" investment (i.e. NZ owned groups); and
- 110% of the worldwide group's debt percentage (or, where non-resident shareholders are considered to be acting together, 100% of the worldwide group's debt percentage).

For the purposes of calculating the debt percentage:

- interest bearing debt, fixed rate shares and stapled stock is included; and
- assets are reduced for non-debt liabilities to determine the "net" assets.

The use of a debt-to-asset percentage differs from many other jurisdictions' thin capitalisation regimes which tend to monitor an entity's debt-to-equity ratio.

There are special concessions for certain infrastructure projects which allow the debt percentage to exceed 60%.

Anti-hybrid rules

NZ introduced anti-hybrid rules for income tax years starting on or after July 1st 2018. The rules are aimed at eliminating tax benefits arising from hybrid mismatch arrangements.

Generally, hybrid mismatch arrangements are arrangements that take advantage of the differences in tax treatment of an instrument, entity or branch across different jurisdictions (mismatch situations). They can include a deduction where there is no inclusion by the recipient or where there is a deduction for the same expense (or portion thereof) in two jurisdictions.

The rules are extremely complex with the legislation and guidance with respect to these rules continuing to evolve.

Tax losses

Tax losses incurred by both resident and non-resident taxpayers can generally be carried forward and used to offset income in a future year. In the case of companies, trusts and partnerships, a tax loss can only be carried forward if there is at least a 49% shareholding continuity of the ultimate owners at all times from the year in which the tax loss was incurred to the year in which it is used to offset profits. Tax losses are not able to be carried back and offset against prior year tax profits.

In 2019 changes were introduced to "ring fence" tax losses arising from residential properties (e.g., rental losses). In certain circumstances taxpayers will only be able to offset residential rental property tax losses against other residential property related income (and not against other income such as salary or non-property related business income).

Goods and services tax (GST)

Goods and services tax (GST) registration is required if income from non-residential rental income is, or is expected to be, over NZ$60,000 for any 12 month period.

If GST registration is required, GST is payable on rental income derived from commercial (or industrial) property rental. However, there is no GST imposed on residential rental property.

Most sales of non-residential land (and buildings) between GST registered persons are zero-rated for GST purposes.

Depending on whether you or your NZ investment entity is registered for GST, and the past and intended use of the property (i.e., whether for a GST taxable activity or not), the purchase or sale of the property may or may not be subject to GST. It is important to seek GST advice from your advisor prior to any transaction.

Resource Management Act

The Resource Management Act 1991 (the RMA) has the potential to be a significant issue for businesses. The RMA aims to promote the sustainable management of NZ's physical and natural resources.

Resource consents under the RMA are required before undertaking certain activities that might impact on the natural character of the environment or where a use inconsistent with a site's underlying zoning is being sought. Depending on the nature of the consent required, this can be a public process (notified) or non-public process (non-notified). The consent authorities are empowered to impose conditions on the grant of consents. The conditions can range from financial contributions, to the need to obtain specific permits or submit to certain discharge restrictions.

The imposition of conditions is a complicated system and details are often embedded in the local authority plans and are specific to the proposed activity. For uses consistent with the underlying zoning, the consenting process is normally straight forward, albeit local authorities have a certain amount of power over whether or not they impose conditions.

6 Singapore

Treaty benefits/MLI will enter into force for Singapore on April 1st 2019

Historically, Mauritius and Luxembourg are jurisdictions that are commonly used to set up financing structure to provide interest-bearing shareholders' loans to property holding entities in Singapore as the treaties between Singapore and Mauritius / Luxembourg allow for withholding tax exemption on interest payments (as opposed to 15% under Singapore domestic law). With the increase scrutiny from the Inland Revenue Authority of Singapore (IRAS) on treaty shopping, due care and consideration needs to be given in implementing such financing structure.

On this note, Singapore has also deposited its instrument of ratification on December 21st 2018. As a result, the MLI has entered into force for Singapore on April 1st 2019. Under the MLI, the principal purpose test (PPT) will now apply to all Covered Tax Agreements under the MLI.

To this end, investors should conduct a review its existing structure to evaluate the impact of this provision and the sustainability of its existing investment structures (especially when Mauritius and Luxembourg entities are used to provide loans to the Singapore entities).

Specified income that qualify for tax exemption under the Tax Incentive Schemes for Funds Managed by Singapore-based Fund Managers will include Singapore sourced interest income with effect from February 19th 2019

Approved Funds under the Singapore Fund Exemption Scheme enjoy tax exemption on the specified income derived from designated investments.

As announced during Budget 2019, the definition of specified income has been enhanced to include Singapore-sourced interest (except where is loan is granted in respect of an immovable property situated in Singapore). Hence, approved Funds or investors looking at setting up Singapore funds should consider whether they are able take advantage of this enhancement for their existing and future investments.

7 Taiwan

Income Tax

The income tax regime in Taiwan is divided into the consolidated personal income tax regime for individuals, or individual income tax (IIT), and the profit-seeking enterprise income tax regime for business enterprises, or corporate income tax (CIT).

IIT

Individuals, irrespective of whether they are residents of Taiwan, are subject to income tax on Taiwan-sourced income defined in the Income Tax Act (ITA). The residence status determines how an individual will be taxed on Taiwan-sourced income and whether the Alternative Minimum Tax (AMT) will be applied. A resident individual is subject to marginal progressive rates (ranging from 5% to 40%), with entitlement to personal exemptions and deductions. Non-residents are generally subject to a flat tax rate on gross income received, and are not eligible for personal exemptions or deductions.

CIT

A resident company in Taiwan is subject to income tax on its worldwide income. The prevailing corporate income tax rate is 20% effective from FY 2018, assuming the taxable income is higher than TWD500,000. Current year after-tax earnings of a resident company which are not distributed within one year after fiscal year end are subject to 5% profit retention surtax. A company is deemed to be a resident corporation for income tax purposes if it is incorporated or established under Taiwan Company Act, regardless of whether it is owned by foreign or local investors, or jointly by both. Similarly, a resident foreign company generally refers to a company incorporated in a foreign jurisdiction that has a permanent establishment (PE), i.e. a fixed place of business or a business agent, in Taiwan. Resident foreign companies are subject to income tax on Taiwan-sourced income only, at the same rates as Taiwanese resident companies, and are also subject to AMT. Non-resident foreign companies are generally subject to withholding tax on Taiwan-sourced income, unless where separate tax filings are required.

Alternative Minimum Tax

The AMT applies to both resident enterprises and resident individual taxpayers. Under the Income Basic Tax Act (IBTA), taxpayers are required to calculate and report their alternative minimum taxable income (see below) calculated under the IBTA, together with their same year regular income calculated under the ITA. If the regular tax is greater or equal to the AMT, the regular tax must be paid. Conversely, if the regular tax is less than the AMT, the taxpayer pays the AMT instead.

AMT= (Alternative minimum taxable income ./. AMT exemption) x AMT rate		
	AMT rate %	**AMT exemption TWD**
Resident enterprises	12	500,000
Resident individuals	20	6,700,000

The AMT is designed to guarantee minimum taxes are paid. As such, income exempted from income tax assessment, such as capital gain from securities transaction etc., as regulated under the ITA or other laws, would need to be added back when calculating AMT. Notably, offshore income of resident individuals will be included in AMT calculations.

Rental income

Rental income is assessable and taxed at the CIT rate of 20% for companies. In addition, the rental income shall also be subject to a 5% value-added tax (VAT).

Respective marginal progressive income tax rates ranging from 5% to 40% are assessed on rental income received by resident individuals. The rental income of resident individuals are taxed on a deemed profit basis if the actual cost of such rental is difficult to establish.

Capital gains on sale of property

A new real property transfer tax (RPT) regime, which taxes actual gain realised from property transactions for both buildings and land, is applicable to all properties acquired on or after January 1st 2016, as well as those bought on or after January 2nd 2014 if held for less than two years.[5] The tax base is the market value of the properties reduced by related costs, expenses, and increase in government-assessed land value for land value incremental tax (LVIT) purposes. A rate of 20% will apply on Taiwanese corporate taxpayers and resident individuals are subject to 15%~45% tax rate, depending on the holding period (other preferential rates apply if certain criteria are met); whereas, a tax rate of 35% or 45% will apply on non-resident individuals and profit-seeking enterprises with foreign head offices located outside of Taiwan (i.e. using Taiwan branch structure), depending on whether the property is held for more than or less than one year.

LVIT will continue to be levied with the implementation of the new RPT regime. The total amount of land value increment calculated for LVIT purpose is deducted from real estate transaction gain to avoid double taxation.

[5] The old real property tax regime still applies to properties purchased prior to January 2nd 2014, or those purchased after January 2nd 2014 but before January 1st 2016, if held for more than two years. Under the old Real Property Tax regime, only gain from sale of buildings is subject to income tax assessment, and land value incremental tax (LVIT) applies to increment in government-assessed value of land, i.e. land is exempt from income tax assessment. Capital gain is consolidated into the tax return of the resident enterprise, Taiwan branch of a foreign enterprise, or resident individual selling the real property, and therefore is subject to corporate income tax rate of 20% for enterprises (including resident enterprise or foreign enterprise with a Taiwan branch), or progressive tax rates of 5% to 40% for resident individuals, respectively. For non-resident individuals and foreign enterprises without a Taiwan branch, capital gain is subject to 20% income tax rate.

The following is a summary of the new real property tax regime:

Item	Description
Taxation scope	Sales of any of the following after January 1st 2016 will be subject to the new RPT regime, except where various criteria are met (see section below on 'Exclusions'): • building; • building and land where the building is situated thereon; and • land eligible for being granted a construction permit. **Exclusions:** If the building or land is sold after January 1st 2016, and meets any of the following criteria, the sale will be subject to the old RPT regime instead: • building or land was acquired prior to January 2nd 2014; or • building or land was acquired on or after January 2nd 2014, but before January 1st 2016, and has been held for over two years.
Tax base	Proceed from sale of building and land minus: • costs; • expenses; and • the total amount of land value increment calculated based on the Land Tax Act, i.e. tax base of LVIT
Tax rate	For Taiwanese profit-seeking enterprises: 20% For resident individuals, building/land held for: • less than one year: 45% • more than one year but less than two years: 35% • more than two years but less than ten years: 20% • more than ten years: 15% For profit-seeking enterprises with foreign head-offices located outside of Taiwan, i.e. with Taiwan branch, and non-resident individuals, building/land held for: • less than one year: 45% • more than one year: 35%

For any profit-seeking enterprise having its head office outside of Taiwan who directly or indirectly owns more than 50% of an offshore company's shares, where at least 50% of the value of such company is comprised of building and land within Taiwan, income derived from transaction of such offshore company's shares shall be deemed as real property transaction gain, and income taxes shall be calculated and paid in accordance with guidance provided under new RPT regime.

Interest expense

Interest expense is allowed as deduction from rental income for corporate income tax purposes if interest expense incurred is related to the principal and ancillary operations of the company. The deduction of interest expense on related party loans is subject to Taiwan transfer pricing regulations.

Taiwan introduced the thin capitalisation rule in Article 43-2 of the ITA, where deductible interest expense on intercompany loans is capped at a prescribed intercompany debt-to-equity ratio of 3/1. The rule generally applies to profit-seeking enterprises, except banks, credit cooperatives, financial holding companies, bills finance companies, insurance companies and securities companies.

Certain interest cost must be capitalised. An example of such cost includes interest incurred on loans used to finance the construction of a building. Interest incurred for purchase of land before land title transfer is effected shall also be capitalised.

Further, based on Rules Governing Allocation of Costs, Expenses and Losses Related to Tax Exempt Income, interest expense relating to tax-exempt income may no longer be deductible from taxable income. For example, since the gain on sale of land is not subject to corporate income tax under the old RPT regime, interest expense in relation to sale of land is subject to restrictions for tax deduction purposes.

Payment of interest to resident individuals or profit-seeking enterprises on loans used to finance the construction of a building and acquisition of land is subject to withholding tax at a rate of 10%. A 20% withholding tax is applied on interest payment to non-resident individuals and profit-seeking enterprises having no fixed place of business in Taiwan, absent any tax treaty. No withholding tax is imposed on interest paid to local banks.

Depreciation

Depreciation of fixed assets is calculated based on useful lives prescribed in the Table of Service Lives of Fixed Assets. The methods of depreciation allowed under the current tax regulations are straight-line, sum-of-the-years-digit, fixed-percentage on diminishing book value, production unit or working-hour method.

Loss carryforward

Net operating losses can be carried forward for a maximum period of ten years by virtue of Article 39 of the ITA.

Land tax

Land is subject to annual land tax based on government-assessed value. The first rate is the regular progressive tax rate ranging from 1% to 5.5%, depending on the starting cumulative value (SCV) of the said land. The second rate is a special privileged rate applicable to various types of land ranging from 0.2% to 1%.

House tax

Buildings are subject to house tax imposed on the taxable present value announced by the government. The building tax rate for commercial properties is 3% to 5% of the taxable present value, and the rate for non-commercial properties is 1.2% to 3.6% of the taxable present value.

Deed tax

Deed tax is imposed on transactions that involve purchases and sales, acceptance of Diens, exchanges, bestowal or partition of, or on, immovable property, or acquisition of ownership of immovable property by virtue of possession. Immovable property refers to both land and land fixtures. However, if land is located in an area where LVIT is assessed, no deed tax shall be imposed, so deed tax is collectible, in effect, only on land fixtures such as buildings.

The applicable tax rates range from 2% to 6%, depending on the classification of each deed. Specifically, deed tax on activities in relation to sales and acquisitions is 6% on the government-assessed value of the property. In case of a sale, the deed tax shall be filed and paid by the purchaser.

Stamp tax

Stamp tax is imposed on deeds or contracts for sale, gratuitous transfer, partition or exchange of real estate or pledge of lien on real estate to be submitted to government agencies for registration. The current tax rate is 0.1% of the government-assessed present value of real estate.

LVIT

LVIT is levied on the increased published present value of land upon the transfer of legal title of land, and is borne by the seller. The tax liability is calculated based on the published present value promulgated annually by the government. The tax rates for LVIT are as follows if the land is held for less than 20 years:

For value increase of less than 100% of the previous published present value, LVIT shall apply at the rate of 20% on the increased value.

For value increase of more than 100% but less than 200% of the previous published present value, LVIT shall apply at the rate of 30% on the increased value falling within this range.

For value increase of more than 200% of the previous published present value, LVIT shall apply at the rate of 40% on the increased value falling within this range.

The present value of land is assessed and published annually, taking into consideration such factors as the development of each geographic district and inflation rate.

VAT on sale of property

VAT is exempt on the sale of land. A 5% VAT will be assessed on the sale of buildings.

Real Property Securitisation

The Real Property Securitisation Law (RPSL) was officially promulgated with a view to revitalise the real estate market, heighten the liquidity of real estate, and bring greater diversity to the securities market. The RPSL provides two possible methods to securitise real properties, namely “real estate investment trust” (REIT), and “real estate asset trust” (REAT). The RPSL also incorporates real estate development trust.

Income distributed to beneficiary certificate holder of REIT or REAT shall be subject to the following withholding tax treatment:

10% withholding tax for resident companies (interest income to be consolidated in corporate tax return) and 10% final withholding tax for resident individuals.

15% final withholding tax for non-resident companies and non-resident individuals.

Tax implications of repatriation of income

Corporate dividends distributed from after-tax profits to foreign investors are subject to withholding tax. The standard dividend withholding tax rate was increased from 20% to 21% as part of the 2018 income tax reform. The increased rate shall apply to dividends distributed to non-resident individuals and corporate shareholders from 2018 onwards. This withholding tax may be reduced if the foreign shareholder is a tax resident of a country which has a signed and effective tax treaty with Taiwan. Foreign investors that invest in Taiwanese real estate using Taiwan branch of a foreign corporation are not subject to Taiwan withholding tax on repatriation of after-tax profits to the foreign head office (i.e. there is no branch profit tax in Taiwan). With respect to taxes on capital gain from sale of property, please refer to the section “Capital gains on sale of property” above.

America

1 Argentina

Sale of Stock by non-residents and dividend distributions

Transfer of Argentine shares between non-residents is currently subject to non-resident capital gains tax (NRCGT). Thus, foreign beneficiaries are subject to a 13.5% effective income tax withholding rate on gross proceeds or, alternatively, a 15% income tax on the actual capital gain if the seller's cost basis can be duly documented for Argentine tax purposes.

In April 2018, the Argentine tax authorities issued Resolution No. 4227-E, establishing the mechanism for paying the capital gains due by non-residents.

Regulations now provide that the seller is responsible for paying the NRCGT for transactions made since January 2018.

Non-residents are exempt from NRCGT on the sale of shares of publicly-traded companies, but only to the extent that the shares are sold through the local Stock Exchange. Furthermore, non-residents are exempt from tax on capital gains from the sale of sovereign bonds and corporate bonds issued in an IPO. The yields from those bonds are also exempt from Argentine tax. In all cases, the exemption is conditioned on the foreign seller being a resident in a jurisdiction that has an exchange of information agreement with Argentina and that the funds come from these jurisdictions. Only yields and capital gains derived from specific securities issued by the Argentine Central Bank (so-called LEBACs) do not benefit from this exemption. In these cases, both the income and the capital gains are subject to a 5% tax. If the tax cost cannot be determined in the case of a sale, the tax is levied at a rate of 4.5% of the sales proceeds.

Indirect transfer of Argentine assets (including shares) are subject to indirect NRCGT provided that i) the value of the Argentine assets exceed 30% of the transaction's overall value and ii) the equity interest sold in the foreign entity exceeds 10%. The tax is due if any of these thresholds were met during the 12-month period prior to the sale. The indirect transfer of Argentine assets, however, is only subject to the tax to the extent those assets were acquired after January 1st 2018. Furthermore, indirect transfers of Argentine assets within the same economic group do not trigger taxation.

A withholding tax on dividend distributions has been established since 2018. The current withholding tax rate is 7% and it will be increased to 13% for profits generated in taxable years started on or after January 1st 2020.

In addition, a 35% "equalisation tax" applies to dividend distributions made out of earnings accumulated prior to January 1st 2018 that exceeded tax earnings as of the year-end prior to the relevant distribution.

Rollover of fixed assets

Income Tax Law establishes that in the event of disposal and replacement of fixed assets, the gain obtained from that disposal may be applied to the cost of the new fixed asset. Therefore, the result is charged in the following years, through the computation of lower amortisation and/or cost of a possible future sale of new goods.

In case of real estate, this procedure only takes place when the property was affected to the obtaining of taxable income (as fixed asset or was subject to lease) at least (two) years before its disposal.

It is important to consider the implications of applying of the roll-over mechanism in the income tax return.

The use of real estate trust

The use of real estate trusts is regulated by the Civil and Commercial Code, which provides a very flexible legal framework. It has been the preferred vehicle for real estate projects in Argentina and is commonly used in building construction, especially in structures where small and medium-sized investors are involved. There are no major taxation differences compared to other corporate entities.

A recently enacted law (Law 27,440) establishes tax reductions and reduced tax rates for trusts and investment funds constituted for real estate developments, to the extent that certain requirements are met. The main advantages are the following:
1. Revenue recognition for income tax purposes is deferred up to the moment the trust effectivity makes a profit distribution to its participants;
2. Certain real estate trusts with social-productive aims are benefited with a reduces 15% income tax rate.

Real estate investment trusts should be examined as an alternative to structure real estate projects in Argentina.

Transfer Pricing

All related-party cross-border payments have to comply with the arm’s length principle. Failure to present appropriate documentation to the tax administration may result in the non-acceptance of group charges and penalties for tax purposes.

The tax reform introduced a detailed definition of a permanent establishment (PE). The term “PE” comprises: a building site, a construction, assembly or installation job or supervision activities in connection therewith but only if such site, project or activities last more than six months in Argentina.

The arm’s length principle should be duly followed and documented. The existence of a PE should be analysed.

Tax prepayments

In the case of declining profits, an application can be made to reduce current tax prepayments.

Cash flow models and profit forecast should be checked in order to improve liquidity by applying for tax prepayment reductions and/or refunds.

Tax Treaty Network

Argentina has concluded tax treaties for the avoidance of double taxation with various countries, under which reduced withholding tax rates can generally be applied on dividends, interest, royalties and certain capital gains. Currently, there are more than 20 double tax treaties signed by Argentina.

Although pending to be ratified, Argentina has signed in 2018 the MLI (Multilateral Instrument), which may provide changes to the provisions of the existing treaty network which should be duly monitored.

It is strongly recommended to verify substance requirements to apply double tax treaty benefits.

Tax losses carried forward

Losses may be used to offset Argentinean profits arising in the same company. Any amount of tax losses that could not be used in the year in which they were incurred can be carried forward for five years. Tax losses cannot be carried back. Losses in transfers of shares generate specific tax loss carry-forwards and may only be used to compensate profits of the same origin.

It is important to monitor taxable profits and losses during the project and when you intend to reorganise your investment structure.

Thin capitalisation rule

The deduction on interest expense and foreign exchange losses with local and foreign related parties is limited to the higher amount between:

a. 30% of the taxpayer's taxable income before interest, foreign exchange losses and depreciation;
b. The amount fixed by the Regulatory Decree (AR$1m).

The taxpayer is entitled to carry forward excess non-deductible interest for five years and unutilised deduction capacity for three years.

It is important to monitor this subject.

Foreign exchange control regulations

As from September 1st 2019, the National Executive Branch and the Argentine Central Bank issued a number of regulations which determined the restoration of the Foreign Exchange Control Regime.

In this sense, regarding incoming flows of currency in concept of financial loans, it was established that they must be brought into and negotiated in the Free Foreign Exchange Market (MLC). The fulfilment of this obligation will have to be demonstrated in order to access the MLC to pay capital and interests of financial loans. Likewise, the MLC can be accessed to pre cancel capital or interest instalments for a maximum of three business days before the corresponding due date A prior pre cancelation will require BCRA approval.

There is no obligation to bring into the country the foreign currency of capital contributions received from non-resident entities. However, non-residents who intend to access the MLC in order to purchase and or transfer abroad foreign currency (for instance for a repatriation of direct investments) for amounts greater than the equivalent to $1,000 per month, shall have prior approval of the BCRA (with exception of International Organisations and other official agencies with functions in the country).

Another topic that has been significantly modified relates to the option granted to residents –individuals and legal entities- to form foreign assets. It should be mentioned that prior to the introduction of the new set of regulations this was an alternative for both kind of subjects. Nowadays, only individuals may access the MLC to form external assets abroad or locally for an amount of up to $10,000 per month. To access the MLC for higher amounts, prior BCRA approval will be required.

Legal entities, local governments, mutual funds, trusts and other universalities established in the country shall count with prior consent of the BCRA to access the MLC for the formation of external assets abroad or locally.

Access to the MLC by residents to pay debts and other obligations in foreign currency contracted with other residents and agreed as of September 1st 2019 onwards is prohibited, unless such obligations have been implemented through public records or deeds by August 30th 2019. In the latter case, residents will be able to access the MLC on the date in which the debt is due.

As to payments of debts arising from imports of goods and services, they can only be paid at its maturity, while pre-cancelation of the mentioned debts will be subject to prior approval of the BCRA. For the payment of financial or commercial debts abroad in general, it was also established that it must be demonstrated that the transactions has been reported in the last due filing of the Survey of Assets and External Liabilities.

In addition, the requirement of prior approval of the BCRA will also be necessary to perform payments originated in imports of services to foreign related companies, except for certain specific concepts.

Foreign currency derived from export of goods, export of services and the sale of non-financial non-produced assets must be brought into and settled in the MLC within the terms specified for each type of these transactions.

The Exchange Control Regime gains once again extreme importance, having the BCRA emphasised that all operations that do not comply with the provisions of the exchange regulations are reached by the Foreign Exchange Regime. Consequently, in each project a careful analysis should be performed.

Corporate Law Impacts

In case the purchaser of land is a foreign company, the purchase of real estate may either be treated as either an "isolated act" or as an act evidencing some degree of continuous presence in Argentina. Recent administrative precedents and judicial case law tend to treat the purchase of real estate property by foreign companies under the second view and, hence, a permanent representation of the company in the country (e.g., a subsidiary or a branch) may be required by the local Office of Corporations.

A local presence in the country may be needed in other to acquire real estate property.

Rural land ownership law

Pursuant to Law 26737, enacted in December 2011, foreigners shall not hold more than 15% of the total amount of land in the whole country, or in any province or municipality. An additional restriction prevents foreigners of a unique nationality from owning more than 30% within the previously referred cap of 15%. The law specifically prevents any foreigner from owning more than 1,000 hectares (approx. 2,500 acres) of rural land in the Argentine “zona núcleo”, or an equivalent area determined in view of its location; and from owning rural lands containing or bordering significant and permanent water bodies, such as seas, rivers, streams, lakes and glaciers.

Decree 820/2016 introduced certain interpretation criteria in order to not over restrict foreign investment in rural land.

According to Section 3 of Law 26737, the following persons will be considered as foreigners:
- individuals with foreign nationality, despite of having their domicile in Argentina or abroad;
- legal persons with 51% of foreigner holding or being entitled with enough votes to control corporate will, or
- legal persons with 25% of indirect foreigner holding or having enough votes to control corporate will.

Said regulation does not affect those rights acquired before the above-mentioned Law 26737 came into force.

Finally, any person acquiring frontier land (either local or foreigner) must obtain the corresponding governmental authorisation.

It is necessary to review hypothetical effects of this law in real estate investment with foreign investors.

Surface Right in the new Civil and Commercial Code

A surface right involves a temporary property right on real property not personally owned, which allows its holder to use, enjoy and dispose the property subject to the right to build (or the right on what is built) in relation to the said real property. The maximum legal term for this surface right is 70 years.

The surface right holder is entitled to build, and be the owner of the proceeds. In turn, the landowner has the right of ownership provided that he does not intervene on the right of the surface right holder.

The surface right terminates upon completion of the established term (or by operation of law), or by express resignation, occurrence of a condition, consolidation, or upon ten years from the last use in cases of construction.

The landowner owns what is built by the surface right holder and thus, the landowner must compensate the surface right holder unless otherwise provided by agreement.

It is worth noting that this new legal mechanism is available for real estate projects in Argentina.

Simplified Companies

Law 27349 provide different new tools for developing entrepreneurial capital. Among other legal mechanisms a trust for developing and financing such capital (FONDCE) has been created, as well as a new legal corporate type: Simplified Companies. The referred Simplified Companies has been created for providing every entrepreneur the possibility of incorporating a company, obtaining it tax code and a bank account in a short period and with a much more flexible structure than the one in force for other legal types provided by Argentine Law 19550. Also, any existing company incorporated in Argentina under any of such existing legal types is entitled to amend its by-laws in order to adopt the Simplified Companies legal type.

It is worth noting that this new legal mechanism is available for any kind of projects in Argentina.

Limits to the Property Right in the new Civil and Commercial Code

The new Civil and Commercial Code establishes that the exercise of individual rights over goods must be compatible with the Collective influence rights. Such exercise must meet national and local administrative laws passed upon the public interest and must affect neither the performance nor the sustainability of flora and fauna ecosystems, biodiversity, water, cultural values, landscape, among others, according to the criteria foreseen in the particular legislation. This broad limitation over the exercise of property rights in Argentina is still to be interpreted and applied by local courts.

This a current legal concern when exercising property rights.

2 Brazil

Investment in Brazilian property

Corporate and individual investors (mainly foreign investors that could apply for certain tax benefits) have different options for better structuring their investments in Brazil.

The choice of the best alternative for structuring investments in the property sector will depend on the characteristics of the investment to be proceeded.

Acquisition of urban/rural real property

Non-residents may invest in property through direct ownership from abroad, or through resident companies or partnerships.

The acquisition of real property by foreign individuals or companies observes the same procedures imposed on Brazilian citizens. Therefore, the acquisition must be formalised through a contract of purchase and sale, as well as through a public deed.

According to Brazilian law, foreign individuals resident in Brazil and foreign companies may invest in rural properties, but there are several restrictions regarding the size of the area to be acquired and the interest to be held by the investors (i.e., there might be limitation to control in the rural real property by foreign investors). There are few alternatives to invest via Investment Funds regarding this restriction of holding control.

Rural properties acquired by foreign companies must be destined for the implementation of agricultural, industrial or settlement projects and these activities must be related to the companies' purposes.

Rental income

Brazilian income tax is a federal tax levied on income and proceeds of any nature received by individuals or corporations. The taxable event is considered to be the acquisition of the right to dispose, economically or legally, of either, both or one of the following:

- Income, derived from capital, labour or a combination of both.
- Proceeds of any nature (not included in the above), which imply an increase in the individual's net equity.

According to Brazilian legislation, payment of income tax may be required from whoever is legally or economically entitled to dispose of it, including rental income.

Individual taxation

Individual taxation in Brazil varies according to the taxpayer's status (resident or non-resident). Resident taxpayers include Brazilian natural citizens, naturalised foreigners and others under specific conditions.

Brazilian-resident taxpayers are taxed on their worldwide income, being subject to a progressive rate, ranging from 0% to 27.5%.

Non-resident individuals are taxed as per the general rules of non-resident investors.

Corporate Taxation

Brazilian tax legislation considers all legal entities, including branches, agencies or representatives associated with companies headquartered abroad, as subject to taxation.

Gains arising from real estate will be subject to income taxes, namely Corporate Income Tax (*Imposto sobre a Renda da Pessoa Jurídica* – IRPJ), a federal tax levied at 25% rate, and the Social Contribution on Net Income, or *Contribuição Social sobre o Lucro Líquido* (CSLL), a social contribution levied at 9% rate.

Additionally, revenues of legal entities are subject to PIS (Employees' Profit Participation Program or *Programa de Integração Social* (PIS) and COFINS (Contribuition for Social Security Financing or *Contribuição para o Financiamento da Seguridade Social* (COFINS) at a 1.65% and 7.6% rate, respectively, being allowed offsetting credits from certain inputs.

Depending on certain conditions, such as the total company revenues and the corporate tax regime elected, the PIS and COFINS rates can be reduced to 0.65% and 3% over gross proceeds (this will bring impacts on corporate income taxes, which will vary from 2.88% to 10.88% over gross proceeds). In this case, no deductions are allowed.

Non-residents

Non-resident taxpayers (both individuals and corporations) are subject to tax on their Brazilian-source income at a rate of varying from 15% to 25%. Brazilian-source income is considered all income paid by Brazilian-sourced payers, regardless of the nature, or which period it relates to.

Note that "Portfolio Investment", investments made in the Brazilian financial and capital markets, which are regulated by Resolution 4373/14 of National Monetary Council (CMN), could trigger different taxation.

Capital gains on the sale of property

Individuals

Capital gains arising from the disposal of real estate property by Brazilian individuals is subject to a progressive 15% to 22.5% rate, based on the amount on the total capital gains received.

Capital gain earned by a resident individual on the sale of residential real estate is exempt of such tax, provided the seller, within 180 days from the sale, uses the earnings to buy a new house in the country. This rule is only applicable for determined individuals after a gap of five years between the transactions.

Corporations

Capital gains arising from the sale or exchange of fixed assets are treated as ordinary income and taxed at the regular rates (i.e., IRPJ and CSLL rate 34%) plus PIS and COFINS at a combined 9.25% rate (3.65% if the taxpayer is under the cumulative method) if the real estate is a non-fixed asset.

Real estate developers may apply for a special taxation regime (Regime Especial Tributário – RET). Under this regime, the taxes IRPJ, CSLL, PIS and COFINS are paid at a unified tax rate of 4% of the received revenues.

Non-residents

Disposal of real estate properties by non-resident individuals is subject to withholding tax at a rate of 15% to 22.5%, based on the amount of capital gain received.

If the disposal is made by a beneficiary domiciled in a tax haven country/territory, capital gains will be subject to 25% withholding tax.

Capital gains realised by non-residents is generally determined as being the difference between the sales price and the cost basis of the asset or right sold.

Note that “Portfolio Investment”, investments made in the Brazilian financial and capital markets, which are regulated by Resolution 4373/14 of National Monetary Council (CMN), could trigger different taxation.

Real estate transfer tax (ITBI)

Transference of real estate property and/or related rights are usually subject to the Real Estate Transfer Tax (*Imposto sobre Transmissão Intervivos de Bens Imóveis*- ITBI), based on the value of the sale or transfer.

Each municipality imposes its own ITBI rates, usually ranging from 2% to 4%.

Certain transferences (e.g., capital contribution with real estate assets) may be tax exempt, provided certain conditions are met.

Other relevant taxes – IOF, IPTU, ITR and ITCMD

Inflow and outflow of resources related to Foreign Direct Investment (e.g., direct acquisition of real estate or incorporation of a Brazilian company) is subject to IOF at 0.38% rate.

Foreigner investors, whenever investing through Resolution CMN 4,373, for assets traded in financial and capital markets (e.g., Real Estate Investment Funds), will be taxed by IOF at 0% on the inflows and outflow of resources in the country.

A municipal tax called Real Estate Tax, (*Imposto sobre a Propriedade Predial e Territorial Urbana* – IPTU) is imposed on the holding of the real estate. The tax is calculated on an appraised value of the property (not necessarily the fair market value), and rates vary from one municipality to another (on average of 0.3% to 2.8% per year), limited to 15% per year.

The same rules pertinent to the taxable basis, taxable event and the taxpayer also apply to the Rural Land Tax (ITR), or *Imposto sobre a Propriedade Territorial Rural*, which is a federal tax levied on the ownership or possession of rural property. The tax rate is determined considering the area size and how much the area is used (ranging from 0.03% to 20%).

The State Tax ITCMD, or *Imposto sobre a Transmissão "Causa Mortis" e Doação de Bens e Direitos* it is a state tax levied on inheritances and donations of real estate properties and their rights. The rates may vary from state to state, from 2% to 8%.

Other real estate investment structures

Other alternatives for investing into real estate assets or real estate companies are also available for both, local and non-resident investors.

Certain alternatives, such as Investing into Real Estate Funds (*Fundo de Investimento Imobiliário* – FII) or Private Equity Funds (*Fundo de Investimento em Participações* – FIP) may provide for a more tax efficient scenario, especially for non-resident investors.

For instance, gains arising from the disposal of FIP quotas, provided certain conditions are met, may be tax exempt. A case by case analysis should be carried to verify the most tax efficient scenario.

3 Canada

Investment structures

Foreign investors may invest in property in Canada using a Canadian legal entity (corporation, partnership or trust) or may acquire property directly.

Corporations resident in Canada are subject to Canadian tax on worldwide income. Non-resident corporations are subject to tax on income derived from carrying on a business in Canada (generally through a permanent establishment located in Canada) and on capital gains from the disposition of taxable Canadian property.

Partnership income is determined at the partnership level and the partners are taxed on their share of the partnership income, whether or not such income is distributed.

Income of a trust resident in Canada that is paid or payable to a beneficiary is generally deductible in computing the trust's taxable income and is included in the beneficiary's taxable income.

Compare the various structures that can be used to invest in property in Canada.

Corporate income tax rates

The combined federal and provincial/territorial income tax rates for the 2019 taxation year range from 26.0% to 31.0%, depending on the province or territory. The combined rates include the 15% federal rate plus the provincial or territorial rate which is applied when income is earned in one of Canada's ten provinces and three territories.

Corporate income tax rates have been stable, except for the provinces of Alberta and Quebec. In Alberta, the corporate income tax rate decreased from 12.0% to 11.0% effective July 1st 2019. The rate is expected to be reduced to 10.0%, 9.0%, and 8.0% effective January 1st 2020, 2021, and 2022 respectively. Corporate income tax rates for the province of Quebec were reduced from 11.7% to 11.6% effective January 1st 2019, with a further expected reduction of 0.1% to reach 11.5% in 2020.

Compare corporate income tax rates for different jurisdictions.

Capital cost allowance (tax depreciation)

Capital cost allowance (CCA) may be claimed on buildings and other structures at rates which range from 4% to 10% depending on the age and use of the property (i.e. commercial, residential, manufacturing, etc.). Enhancements have been made to the CCA rates for newly constructed assets acquired after March 18th 2007, generally resulting in a 6% CCA rate for non-residential buildings. Additionally, certain capital property acquired after November 20th 2018 may be eligible for an enhanced first-year allowance.

CCA is calculated on a pool basis, with separate tax classes provided for various types of property. The deduction for CCA is calculated on the tax cost of the entire pool. Most rental properties (i.e. buildings costing more than C$50,000) are required to have separate tax pools so that CCA is claimed on a property by property basis and not on a combined pool of properties.

CCA is a discretionary deduction and cannot be claimed on a rental property to create or increase a tax loss unless the CCA claim is being made by a corporation, the principal business of which is the leasing, rental, development or sale of real property, or a partnership, the partners of which are all such corporations.

Ensure additions to a CCA class include the original acquisition price plus related transaction costs incurred to acquire the asset.

Thin capitalisation rules

The Canadian thin capitalisation rules may apply when the lender to a Canadian corporation is a non-resident person who alone or with other related persons owns more than 25% of the Canadian corporation's shares, and interest expense on the loan would otherwise be deductible to the Canadian corporation. If the ratio of these debts to equity exceeds 1.5/1, the interest on the excess is not deductible.

The thin capitalisation rules will apply to debts owed by a partnership in which a Canadian-resident corporation is a member, as well as to Canadian-resident trusts and to non-resident corporations and trusts that operate in Canada, including when these entities are members of partnerships.

Disallowed interest under the thin capitalisation rules will be deemed to be a dividend for Canadian withholding tax purposes that will be subject to dividend withholding tax of 25%, which may be reduced under a tax treaty.

Recent changes to the Canadian thin capitalisation rules can apply in respect of certain situations that involve secured guarantee arrangements in respect of third-party debts that would otherwise not be subject to the thin capitalisation limitations. In general terms, the changes apply where a non-resident person that does not deal at arm's length i) pledges property to secure the debt, and the lender has at that time the right to use, invest or dispose of the property ii) holds limited recourse debt of the third party lender; or iii) makes a loan to the third party lender on condition that the loan be made to a Canadian corporation or trust.

The new legislation relies on the use of various defined terms and may create significant uncertainty due to many interpretive issues. Careful consideration of all financing arrangements is required.

Consider whether the thin capitalisation rules limit the deduction of interest on debt and trigger a withholding tax liability.

Disposition of property by non-residents

A non-resident that disposes of taxable Canadian property (TCP) that is held as capital property is subject to Canadian tax on any resulting taxable capital gain, i.e. 50% of the gain (proceeds of disposition less capital cost of the property). TCP generally includes real property situated in Canada. TCP also includes shares of the capital stock of an unlisted corporation, an interest in a partnership or trust, if at any time during the previous 60-month period, more than 50% of the value of the share or interest was derived real property situated in Canada.

In addition, to the extent that the proceeds of disposition of Canadian situs depreciable property (i.e. a building) exceed the property's undepreciated capital cost, the excess (up to the property's capital cost) is taxable to the non-resident as recaptured depreciation, at the tax rate that would apply if the non-resident were a resident of Canada.

Generally, a non-resident vendor must report the disposition to the Canada Revenue Agency (CRA) and obtain a clearance certificate in respect of the disposition. If no certificate is obtained, the purchaser is required to withhold and remit to the CRA either 25% (in the case of sale of land that is capital property) or 50% (in the case of land that is not capital property, a building or other depreciable property) of the gross sales proceeds. Relief from the reporting and withholding requirements may be available in certain cases.

In addition to the federal reporting and withholding obligations noted above, a non-resident vendor must separately report the disposition of real property to the provincial authorities where the real property is situated in the province of Quebec. If no certificate is obtained from Revenu Quebec, the purchaser is required to withhold and remit 12.875% of the gross sales proceeds. Non-residents must obtain a certificate even if the transaction results in a capital loss. Relief from the reporting and withholding requirements may be available in certain cases.

When the disposition is on income account rather than on capital account, i.e. inventory, the non-resident will be taxed at full tax rates on the resulting profit less applicable expenses, subject to possible relief by tax treaty.

Ensure the tax consequences of property dispositions are calculated properly and any withholding and reporting requirements are met.

Losses carried forward

Losses incurred in a taxation year from a business carried on in Canada are deductible from income, other than income from property. If these losses are not used in the year they are incurred, they can be carried back three years and forward 20 years. However, losses of a non-resident from a business carried on outside Canada are not deductible in Canada.

Capital losses, resulting from the disposition of taxable Canadian property of a capital nature, can be carried back three years, and forward indefinitely, to reduce taxable capital gains realised on the disposition of taxable Canadian property in those years.

Ensure a loss utilisation plan is in place for losses set to expire.

Withholding tax

Certain payments by a Canadian resident entity to non-residents are subject to withholding tax of 25% of the gross amount of the payment. These payments may include interest paid to related parties, dividends, rents, or royalties. The withholding tax rate may be lower when the payment is made to a resident of a country with which Canada has a tax treaty.

Interest paid to arm's length non-resident lenders is generally exempt from Canadian withholding tax, unless paid in respect of a participating debt arrangement.

Planning may be available to minimise withholding taxes.

Transfer pricing

Canadian transfer pricing legislation and administrative guidelines are generally consistent with OECD Guidelines, and require that transactions between related parties be carried out under arm's-length terms and conditions.

Penalties may be imposed when contemporaneous documentation requirements are not met.

Ensure all transfer-pricing documentation meets the requirements imposed by the Canadian transfer-pricing rules and by the rules of the foreign country.

Land transfer tax, registration fees, and property tax

All provinces and territories and some Canadian municipalities levy a land transfer tax or registrations fees on the purchaser of real property (land and building) within their boundaries. The tax is expressed as a percentage, usually on a sliding scale, of the sales price or the assessed value of the property purchased.

Rates may be up to 5% of the property value depending on the city in Canada and depending on whether the property is residential or non-residential. The tax is generally payable at the time the legal title of the property is registered or on the transfer of a beneficial interest.

To address issues of unaffordability of residential housing in Toronto and Vancouver, local governments have implemented additional transfer taxes where non-residents of Canada acquire residential property. Foreign entities and certain taxable trustees that purchase residential property may be subject to additional property transfer tax (in addition to the provincial and municipal land transfer tax). If the property transfer is registered on or before February 20th 2018 in the Greater Vancouver Regional District in the Province of British Columbia and on or before April 21st 2017 in the Greater Golden Horseshoe in the province of Ontario, the tax amount is 15% of the property value. If the property is registered on or after February 21st 2018 and is within specified areas in the Province of British Columbia, the tax amount is 20% of the property value.

In addition to the above noted transfer tax, the City of Vancouver has also introduced a vacancy tax. A residential property which is not either i) used as a principal residence, ii) rented out for more than six months out of a calendar year, or iii) meets certain exemptions, will be subject to an additional 1% tax based on the property's value.

On October 16th 2018, the Province of British Columbia introduced a Speculation and Vacancy Tax (SVT), which is separate from the City of Vancouver vacancy tax. The SVT will apply in certain regions in the Province of British Columbia (including, but not limited to, the City of Vancouver), and for 2019 and subsequent years, the tax will be levied at 2% of a property's assessed value for foreign owners or satellite families (a satellite family is an individual or spousal unit where the majority of their total worldwide income for the year is not reported on a Canadian tax return).

In addition, most cities and towns impose an annual realty and/or business tax on real property. These taxes are based on the assessed value of the property at rates that are set each year by the various municipalities.

Take into account the land transfer tax and additional tax costs when acquiring real property.

Principal Residence Exemption

Historically, a gain realised on the sale of an individual's "principal residence" has been exempt from tax in most instances. In certain circumstances, non-residents have structured their investments in Canada to take advantage of the principal residence exemption.

A change in CRA's administrative position means that if an individual sells their principal residence in 2016 or later years, they will be required to report the sale, and the principal residence exemption on their income tax return to claim the full principal residence exemption (this was previously not a requirement).

Furthermore, the Department of Finance has issued new rules for taxation years beginning after 2016 that limits the type of trusts that can claim the principal residence exemption and extends the period during which CRA can assess taxpayers that do not report the sale of real or immovable property. The new rules also have implications for non-residents who acquire residential properties, and may limit the availability of the principal residence exemption to non-residents.

Be aware of the legislative changes and administrative changes to the principal residence exemption and consider any impacts.

Sales tax

The 5% federal Goods and Services Tax (GST) will apply on the purchase of real property and on certain expenses incurred in connection with the operation of the property, although the GST paid is usually recoverable (subject to significant restrictions in respect of residential rental properties). In most cases, a landlord is required to collect and remit GST on commercial rents received. However, a non resident vendor of real property is not generally required to collect GST on the sale of real property.

In addition, some provinces have harmonised their sales taxes with the GST. The harmonised sales taxes function as the GST, described above.

If a non-resident owns a property in a province that imposes a sales tax that is not harmonised with the GST, the non-harmonised sales tax will be a non-recoverable additional cost on certain expenses incurred in connection with the operation of the property.

Take into account sales tax when acquiring or collecting rents on real property.

4 Mexico

Tax Reform

In Mexico, an initiative of tax reform was proposed by the Mexican Branch of the Mexican government that would introduce relevant changes in the Mexican tax environment. This proposal is expected that would be discussed and approved no later than October 31st 2019 and be applicable starting from 2020 fiscal year.

We summarise the most relevant changes proposed by the Executive branch of the Mexican government that may have impact to Real Estate industry in Mexico in the 2020 fiscal year:
- Limitation of interest deductibility up to a 30% of the Mexican entity's adjusted income (three years carry forward allowance);
- Modifications to the definition of Permanent Establishment (PE) that would be aligned with the definition included in the Multilateral Agreement and action number 7 of BEPS;
- Non-deductibility for tax purposes of payments made to related parties or unrelated parties through a "structured arrangement' subject to a Preferred Tax Regime in the case if an unrelated party is interposed (some exemptions would apply to this rule);
- Non-deductibility for tax purposes of payments where the same expense is deductible by another entity of the same group or the same entity where it is a resident in other jurisdiction (except in some cases when the income in Mexico is also considered as taxable income in the jurisdiction that allows the tax deduction);
- New proposed provisions would not allow to look-through transparent entities or vehicles to determine their tax implications form its income obtained from Mexico (even if their owners are considering such income as taxable on its residence jurisdictions), except otherwise is stated under a tax treaty. This rule may apply to transparent entities investing in Mexico as public or private funds;
- Transparent entities or vehicles that its effective place of management is located in Mexican territory would be considered as Mexican residents for tax purposes;
- New proposed provisions would introduce a General Anti-Avoidance Rule that is intended to prevent the abuse of tax provisions on benefits obtained when the legal acts have a lack of business reasons.

It is important to mention that even though the provisions mentioned before have not been enacted to be applicable in the 2020 fiscal year, it is expected that the majority of the proposed changes would pass through the legislative process and be in force starting from January 1st 2019.

Books vs. tax depreciation

For book purposes, assets can be depreciated using different methods. For income tax purposes, fixed assets are depreciated on a straight-line basis applying the rates established by law. In addition, tax depreciation is adjusted for inflation, resulting in differences with the amount of the book depreciation.

Review book and tax depreciation, including the adjustment for inflation in the latter, and determine whether the tax depreciation rates are the highest allowed. For taxpayers in a tax loss position, a decrease in the depreciation rates could be analysed.

Alternative minimum tax

There is not an alternative minimum tax in Mexico.

Asset impairment

Impairments are allowed under Mexican GAAP. However, impairments are not deductible for income tax purposes.

Check that no tax deduction from impairment of the assets is being taken by the company. Furthermore, confirm that impairment adjustments are not from obsolescence of fixed assets, because a tax deduction may be included.

Goodwill

Any amount paid in excess of the fair market value of the real estate is considered as goodwill, which is non-deductible for Mexican tax purposes. In addition to the amount being not deductible, the depreciation as well as any interest related to the goodwill will also become non-deductible.

Check if there is an amount related to goodwill, if such amount is being deducted, and whether the related amounts to depreciation and interest are being deducted.

Classification of real estate acquisition

Real estate must be classified for both book and tax purposes as inventory or fixed assets, depending on whether it is acquired for subsequent sale or for development. This will impact the way in which the real estate is deducted: as cost of goods sold (inventory) or via depreciation (fixed assets).

Review how the real estate is classified and determine how it must be deducted and whether this classification makes sense with respect to the business.

Thin capitalisation rules

Interest derived from debts granted by foreign related parties of the taxpayer that exceed three times its shareholders equity will not be deductible (several special rules apply).

Review the thin capitalisation position of the company and also the computation to determine the non-deductible interest, if this is the case.

Informative returns

Taxpayers are obliged to file informative returns related to several different matters. In general, the deadline to file said informative returns is February 15th of the following year, except for the informative return of transactions with related parties, which is filed together with the annual tax return. All taxpayers are subject to reporting relevant transactions on a quarterly basis. Relevant transactions are defined as share acquisitions or dispositions, extraordinary transactions with related parties, and corporate reorganisations, among others on form 76.

Prepare the documentation and ensure that the informative returns are duly filed, as it is a deductibility requirement for expenses and acquisitions made.

Transfer pricing

Mexican income tax regulations require that taxpayers conducting transactions with related parties i) determine the price or value of such transactions at arm's length conditions and, ii) secure the corresponding contemporaneous documentation. Otherwise, the tax authorities may determine the price or value that would have been used by independent parties in comparable transactions.

In connection with BEPS Action 13 (Country by Country reporting), local legislation aimed to comply with such reporting obligations has entered into force. In this regard, Mexican local entities with taxable income of MXN$755,898,920 (i.e. approximately US$40m) are obliged to file Local and Master Files, and Country-by-Country filing if worldwide consolidated revenues are equal or greater than MXN$12 billion (i.e. US$640m) on December 31st of the following year in which the obligation is triggered. Penalty for non-filing is MXN$220,400 and may lead to disqualification from entering into contracts with Mexican public sector and cancelation of the taxpayer importer registry. Note that 2018 filing obligations must be complied with at the latest on December 31st of the current year.

Prepare a transfer pricing study covering each transaction carried out with related parties, including the country by country reporting requirements.

Analyse if the mark up currently used can be adjusted based on the transfer pricing study.

Pension fund exemption

Mexican tax law establishes a tax exempt regime for foreign pension and retirement funds investing in Mexican real estate. Such tax exempt regime on interest, leasing income and capital gains, if certain rules are complied with. Please note that income tax exemptions for foreign pension funds in connection with the sale of real estate or shares (which value is comprised in more than 50% of immovable property located in Mexico), should be available to the extent the real estate property was leased for at least a minimum period of four years before the transaction takes place.

Specific analysis of the structures involving foreign pension funds should be carried out in order to apply the tax exemption granted by the Mexican Income Tax Law. Moreover, documentation to support the exemptions is required so it is strongly recommended to secure it on a contemporaneous fashion.

Mexican REITs

A special tax regime is granted for Mexican REITs providing certain advantages, such as the no obligation to file monthly advanced income tax payments (among other tax benefits). In addition, the Mexican tax rules enacted a new type of REIT for developing hydrocarbon related activities in Mexico (known as REIT-E) that also provides tax benefits.

Review the applicable tax benefits for Mexican REITs.

Creditable VAT for specific business transactions

VAT paid on costs and expenses should only be creditable when the taxpayer carries out taxable activities. For VAT purposes, for example, the sale of land, houses and dwellings is VAT-exempt. Therefore, VAT may be a cost for those real estate companies performing VAT-exempt activities.

Specific review of VAT-able and non-VAT-able activities of Mexican real estate companies should be carried out.

Tax incentive for real estate developers

Taxpayers engaged in construction and sale of immovable property projects may elect to take a deduction for income tax purposes on the acquisition cost of land in the fiscal year that the land is acquired to the extent that this option is applied for a minimum period of five years for all the land being part of its inventory.

Review all requirements for the exercise of this option.

5 United States of America

U.S. Economy and 2019 Outlook

The U.S. economy had real GDP growth of 2.9% in 2018 despite $1.5 trillion in tax cuts and increased government spending. The U.S. economy has expanded at a pace well above the long-term average. The U.S. economy in 2019 is forecasted to grow at a slower pace than it did in 2018, though still above the long-run trend. Interest rates are declining, business investment is predicted to moderate in 2019, while the housing sector is projected to improve this year. The unemployment rate is expected to stay low, at 3.7%, through the end of 2019, and inflation is predicted to move down slightly to 2.3%.

Benefit of U.S. Blocker Corporations

The 2017 tax reform act changed the corporate tax rate from a graduated tax rate with a maximum rate of 35% to a flat 21%, resulting in increased return rates overnight for real estate investments held through US blockers. Due to the rate reduction, investing in U.S. real estate through a U.S. blocker corporation has become a more favourable fund structure for both U.S. and non-U.S. investors. The 21% corporate level tax may be further reduced or eliminated with the use of debt and certain non-U.S. investors may also benefit from a reduced treaty rate on dividend distributions.

Non-Traditional REITs

Most property REITs hold traditional rental real estate assets in the office, retail, residential and industrial sectors. In recent years, increased attention has been given to real estate investment opportunities available from the non-traditional real estate sectors such as infrastructure, fiber, self-storage, healthcare, timber and other specialty real estate classes. Such non-traditional REITs have gained market share due to the increased need for private sector investment in such assets. Investing in privatised projects through REITs open the doors to investors looking to participate in a new category of attractive long-term and stable investments.

IRC Section 163(j)

On November 26th 2018, Treasury released proposed regulations concerning the Section 163(j) interest expense limitation rules. The 2017 tax reform act revised and broadened the existing interest expense limitation rules which limits business interest expense deductions to the sum of business interest income plus 30% of adjusted taxable income. These regulations brought much more complexity than was expected, especially in the asset management industry that has many tiered partnership structures.

Open Ended Funds

Increased focus has been given to open ended funds as the structure allows investors the flexibility to enter and exit the fund at periodic times versus set dates, which often resulted in investors needing to reinvest sales proceeds at inopportune market times. Open-end funds also have no specific term (unless otherwise required by the state law of the state in which the fund is formed) which allows for continuous solicitation of additional capital and also the ability for investors to contribute property without having to sell within a certain timeframe.

QFPF Proposed Regulations

Treasury and the Internal Revenue Service released proposed regulations on June 6th 2019 addressing qualified foreign pension funds (QFPFs) under Section 897(l). The proposed regulations provide guidance regarding the definition of a QFPF, the application of entities owned foreign pension funds and certain transactions that Treasury and the Internal Revenue Service view as potentially abusive.

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