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REITs on the rise in Portugal

Francisco Cabral Matos and Teresa Teixeira Mota of Vieira de Almeida explain how the rapid development of the market for REITs in Portugal has attracted a range of new real estate investors.

In 2019, the Portuguese government approved a new regime which created a new type of investment vehicle aimed at attracting foreign investment and boosting the real estate sector – the *Sociedades de Investimento e Gestão Imobiliária* (SIGI). The changes became effective as of February 1 2019. These new investment vehicles are the Portuguese version of real estate investment trusts (REITs) and benefit from a favourable tax regime to improve the country's attractiveness for real estate investors.

As the international interest in this new form of investment is picking up, there are already some SIGIs in the Portuguese real estate market, allowing and encouraging the diversification of investments in commercial real estate. The first SIGI to be incorporated was Olimpo Real Estate Portugal, sponsored by the Portuguese retail group Sonae Sierra and Bankinter. More recently, Merlin Properties has also decided to enter into the Portuguese SIGI market through a dual listing process. In fact, SIGIs may well become an investment entity for the general Iberian market, with target properties that may go beyond its Spanish competitor (the *SOCIMIs*). The Portuguese regime is more permissive as per the type of properties, including, for instance, non-urban plots, for instance creating opportunities in agribusiness.

Main aspects of the Portuguese SIGIs legal framework

SIGIs are real estate investment companies aiming at attracting real estate investments, including construction, rehabilitation, renting and other types of economic investments in real estate. SIGIs corporate purpose is limited to:

i) The acquisition of freehold rights, surface rights or other equivalent rights over property (*rights in rem*), for leasing or other forms of economic exploitation (including construction and urban rehabilitation projects, the use or rental of spaces in shopping centres and the use or rental of office spaces);

ii) The acquisition of shares in other SIGIs, or in companies having their head office in Portugal or another EU or EEA member state (bound by administrative cooperation in the field of taxation, provided that the requirements applicable to SIGIs (corporate purpose, composition of portfolio and profits distribution) are complied by all affiliates/subsidiaries; and

iii) The acquisition of units or shares of real estate UCITS governed by Portuguese law having profit distribution rules similar to those applicable to SIGIs, or of real estate investment companies specialised in residential letting.

The rights and shares/units referred above must be held for at least three years after their acquisition.

SIGIs must be incorporated as a public limited liability company registered in Portugal with a minimum share capital of €5,000,000, through:

a) A private placement or public offering; or

b) The conversion of other listed limited liability company or real estate investment funds/companies; or

c) The conversion of UCITS.

Moreover, 20% to 25% of the shares representing SIGIs' share capital must be held by investors which hold shareholdings corresponding to less than 2% of the voting rights in accordance with the Portuguese Securities Code.

SIGIs' assets shall be composed mainly of property rights (*rights in rem*), lease or other forms of economic exploitation, which must be detained for at least three years after acquisition, subject to the following cumulative limits:

a) The value of the rights over real estate and shareholdings shall represent at least 80% of the total value of SIGIs assets; and

b) The value of leased or other forms of economic property rights shall represent at least 75% of the total value of SIGIs' assets. SIGIs' assets must be detained.

SIGIs leverage may not exceed 60% of the SIGIs total assets. Within nine months after the end of each accounting period, SIGIs must distribute at least:

- 90% of its profits resulting from the payment of dividends deriving from holdings in other investment vehicles; and
- 75% of remaining profits.

At least 75% of the net income proceeding from the sale of assets under SIGIs corporate activity shall be reinvested in other assets within three years from said sale.

Portuguese SIGIs' tax regime

SIGIs are qualified as a sub-type of real estate investment companies, being subject to the tax regime applicable to UCITS (set forth in articles 22 and 22-A of the Portuguese Tax Benefits Code), which foresees a typical 'exit taxation' mechanism.

At the SIGI level, corporate income tax (CIT) will be applicable at the standard rate (21%) to SIGIs net profit, except to income derived from the real estate investment activity, including investment and rental income and capital gains. SIGIs will not be subject to municipal and state surcharges. This results in a quasi-exemption regime applicable to SIGIs which are resident for the purposes of the DTT. Additionally, SIGIs will be subject to a 0.0125% stamp duty on their global net asset value, due on a quarterly basis.

At the investors' level, personal income tax (PIT) or CIT may apply to the income distributed by SIGIs, depending on whether the investors are individuals or companies.

Resident investors will be subject to withholding tax at a rate of 28% (individuals) or 25% (companies). Non-resident investors (either corporate or individuals) will be subject to a flat 10% withholding tax rate.

Although it is not clear whether the participation exemption regime may apply to the distribution of dividends or the capital gains arising from the sale of shares, the fact is that SIGIs are subject to (and not exempted from) CIT and therefore could, in principle, claim the application of double tax treaties and EU tax directives. Time will clarify how tax authorities and tax courts apply the SIGI regime.

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