

LISTED CORPORATIONS FOR INVESTMENT IN THE REAL ESTATE MARKET (SOCIMIS)

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I. DEFINITION

According to Act 11/2009, of 26 October, the legal form of Listed Real Estate Investment Stock Companies (SOCIMIs, its acronym in Spanish) was introduced, and along with it, the legal regime of a REIT (Real Estate Investment Trust), a long-standing investment vehicle in the English-speaking world. The main business activity of this type of company is the direct or indirect investment in urban real estate assets – including, *inter alia*, residential property, commercial premises, residences (student or retirement), hotels, garages and offices – for the purpose of letting.

II. LEGAL REGIME

Act 16/2012 has changed certain aspects of the special tax regime applicable to Spanish Real Estate Investment Trusts (in Spanish, *Sociedades Anónimas Cotizadas de Inversión en el Mercado Inmobiliario* or "SOCIMI"), taking effect for tax years beginning on (or after) January 1, 2013.

The purpose of the reform is to facilitate the application of this regime by reducing the applicable requirements because, as stated in the preamble of the law (section XIII), very few SOCIMI have been incorporated so far.

Among the changes that this statute made to the special regime of SOCIMIs, of note are those related to the possibility of trading on a multilateral trading facility, such as the Spanish Alternative Securities Market (MAB), or the removal of restrictions on third-party funding (the 70% limit of external financing is removed), though without relinquishing the structural elements of these companies, bringing them into the line with the REITs (Real Estate Investment Trusts) existing in Spain's neighbouring countries¹.

The main development introduced by Act 16/2012 (notwithstanding the importance of some of the substantive changes) resides in the tax rate – 0% on profit from carrying out the corporate objects – applied to these companies.

III. BASIC REQUIREMENTS OF SOCIMIS

III.1 COMMERCIAL LAW REQUIREMENTS FOR SOCIMIS

III.1.1 Corporate form

- SOCIMIs must be listed "SA" corporationsⁱⁱ. The minimum share capital for SOCIMI is five million euroⁱⁱⁱ; they can have only one class of shares; and they must include in their corporate name the maker "*Sociedad Cotizada de Inversión en el Mercado Inmobiliario, Sociedad Anónima*", or its abbreviation, "SOCIMI, S.A.". The share capital can be subscribed using non-monetary contributions (i.e. by contributing properties to the SOCIMI), meaning that it is not necessary make a monetary disbursement.
- Any non-monetary contributions of real estate for the formation or increase in capital of a SOCIMI must be appraised by one of the approved companies in the mortgage market legislation and their appraisal will be made in accordance with corporate/commercial legislation. This obligation affects contributions made both to SOCIMIs and to the unlisted entities in which they invest.

- A minimum of only one property is required to incorporate a SOCIMI, thus they can be created in real estate projects where the existence of a company per project (and one asset per company) is essential for the purposes of liability, management, risks and licenses. It is not necessary for the property to be located in Spain.
- Mandatory trading on regulated markets (such as the four Spanish Stock Exchanges) or multi-lateral trading systems (such as the Alternative Securities Market, in Spanish: *Mercado Alternativo Bursátil* or the MAB) either in Spain or another jurisdiction within the European Union or the European Economic Area or in any other country with which there is an effective exchange of tax information (uninterruptedly throughout the entire tax period).
- Without prejudice to the above mentioned, it is worth noting that in addition to SOCIMIs, the special tax regime can also be taken for companies known as unlisted SOCIMIs, as was already the case under the former regime. Unlisted SOCIMIs are Spanish-resident companies that are wholly owned by SOCIMIs or foreign REITs (i.e. by non-resident companies listed on European markets that have the same corporate purpose as SOCIMIs and have a similar regime concerning a compulsory policy, by statute or in their bylaws, under which they have to distribute their income)^{iv}.
- The shares of all SOCIMIs must be registered shares, which applies also to the non-resident REITs that have invested in "unlisted SOCIMIs"^v.

III.1.2 Corporate Purpose

Their corporate purpose must consist of acquiring and developing urban real estate to lease, whether directly or through entities which meet certain requirements. They can also carry on ancillary activities so long as the total income from those activities accounts for less than 20 per cent of their income in each tax period.

SOCIMIs may carry on the following activities:

- Acquiring and developing urban real estate for lease, including renovating buildings^{vi}.
- Holding shares in other SOCIMIs or in other non-resident REITs.
- Holding shares in unlisted SOCIMIs or in unlisted non-resident companies^{vii}, provided that one and the other have as their corporate purpose the acquisition of urban real estate for lease, have a similar income distribution policy and are wholly owned by SOCIMIs or non-resident REITs^{viii}.
- Investing in shares or units of the real estate collective investment vehicles (mutual funds and real estate investment companies) governed by Collective Investment Vehicle Law 35/2003.

The investments and activities that may be undertaken by unlisted SOCIMIs, the shares of which must also be registered, are confined to the acquisition of urban real estate to lease and, as a new addition, to the performance of development activities. They cannot, however, own shares in any type of entity (i.e. SOCIMIs can invest in real estate through just one tier of corporate vehicles).

Identical restrictions apply to non-resident entities with properties for rent in which a SOCIMI may invest.

III.1.3 Distribution of dividends

A mandatory distribution of dividends in a given proportion (within six months after the closing term) depending on the origin of the profits obtained^{ix}:

- 80 per cent of overall earnings, including the earnings derived from the lease of properties;
- 50 per cent of the capital gains obtained from the transfer of assets (properties and shares) eligible for the application of the special tax regime (properties used for lease and shares in entities whose corporate object in the foregoing activities). The remaining 50 per cent will be reinvested in eligible assets within three years of the transfer. Failing that, said benefit must be distributed in its entirety together with the rest of the benefits; and
- 100 per cent of the profits coming from entities in which SOCIMI hold a stake.

IV. INVESTMENT REQUIREMENTS FOR SOCIMIS

IV.1 ASSET REQUIREMENT

SOCIMIs must invest^x at least 80% of the value of their assets in the following elements:

- Urban real estate to be leased out.
- Land for developing the real estate referred to above provided that the development in commenced within three years after it is acquired.
- Investments in the capital or in the equity of the entities indicated in the above section (i.e. SOCIMIs or non-resident REITs, unlisted SOCIMIs, unlisted non-resident entities wholly owned by SOCIMIs, REITs or collective investment vehicles).

IV.2 INCOME REQUIREMENT

At least 80 per cent of the earnings (excluding any income arising from the sale of qualifying assets) must come from lease or dividends distributed by any subsidiary SOCIMI.

IV.3 ASSET HOLDING PERIOD REQUIREMENT

Property assets must be leased for a minimum three-year term (one-year availability for lease will be computable for this purpose). Regarding the interpretation of this requirement, the Tax Authorities consider that, in those cases where we find complex property (such as a shopping centre in which the horizontal division has not been declared) it is not necessary that the term for lease is fulfilled for all the promises individually, but the overall degree of compliance will be analysed, without prejudice to any premise not having been leased.

V. BORROWINGS OF SOCIMIS

Not debt restrictions will be apply.

VI. TAX REGIME FOR SOCIMIS

The main purpose is to bring the tax regime for SOCIMs into line with that of the REITs existing in Spain's neighbouring countries (such as French SIFCs, Dutch FBIs or German G-REITs). SOCIMs will be subject to CIT at a zero per cent rate, which make them very attractive for any kind of investor, whether resident or non-resident in Spain.

Just as a general introduction to taxation for the investors, we may face three different scenarios:

- Spanish CIT taxpayers (or non-residents with a permanent establishment in Spain) will include the dividend in their CIT base without entitlement to double taxation relief, although these investors may still take advantage of the SOCIM's regime;
- Spanish individuals will include the dividend in the taxable base subject to flat rates up to a maximum of 21 per cent (temporarily increased up to 27 per cent); and
- Non-residents without a permanent establishment in Spain will be subject to a withholding tax of 19 per cent (temporarily increased up to 21 per cent), unless an exemption (parent-subsiary) or reduced treaty rate is applicable.

In this regard, investors non-residing in Spain (e.g. funds investing in shopping centres, hotel buildings or any other property to be leased), in particular residents within the European Union, may maximize the efficiency of their investments in Spanish real estate for leases down to zero per cent on the Spanish CIT, and also to zero per cent on Spanish withholding taxes under the parent-subsiary directive, then receive return on the investment without tax leakage.

However, all that glitters is not gold and, since the rule of taxation is zero excepted if dividends are distributed to a shareholder holding five per cent or more of the share capital of the SOCIM, and such dividends, in the hands of such shareholder, are either exempt or subject to a tax rate under ten per cent, in which case the application of a special levy to the SOCIM has been foreseen because the latter is required to pay tax at a rate of 19 per cent - which will be treated as corporate income tax payable - on the amount of dividends paid to the shareholders who meet the referred requirements^{xi} (participation equal to or greater than five per cent or the share capital and taxation below ten per cent).

This special levy will typically be triggered in case of non-resident investors who are resident in either a tax haven territory or in a jurisdiction (even within the European Union) where the dividends collected by the relevant investor are entitled to a participation exemption regime. Note that most investment in Spanish real estate by non-resident investors has been done through Luxembourg or Dutch entities. Therefore a review of the structures currently in place may be needed in order to determine whether the SOCIM's tax regime (as amended in 2012) provides additional efficiencies and how to adapt the existing investing structures to be able to apply the new regime.

Last but not least, SOCIMI are entitled to a 95 per cent reduction on the Transfer Tax triggered on the acquisition of real estate assets if they are residential properties to be leased or land for the promotion of residential properties to be leased, to the extent that the holding period requirement of three years is met.

VI.1 SPECIAL TAX REGIME OF SHAREHOLDERS

To determine the tax regime applicable to shareholders, it should be distinguished primarily if it is natural person or legal entity, whether or not if it is considered a tax resident in Spain, and the type of income to be received. It is shown below, in the following chart, the existing treatment to dividends paid against profits or reserves to which the Act's special tax regime has applied and capital gains or losses on the sale or redemption of shares in the capital of companies that have opted for this regime, as detailed:

Taxpayers	Dividends	Capital Gains
Personal Income Tax on Residents	Taxed without application of the annual one thousand five hundred euro (€ 1,500) exemption (Article 10.1.b) of Act 16/2012)	Taxed according to general calculation rules (Article 10.2.b) of Act 16/2012)
Corporate Tax: Resident legal persons/Permanent Establishments	Taxed without application of domestic double taxation relief (Article 10.1.a) of Act 16/2012)	
Personal Income Tax on Non-Residents (without Permanent Establishment)	Taxed without application of the annual one thousand five hundred euro (€ 1,500) exemption (Article 10.1.c) of Act 16/2012)	Taxed without application of the exemption on holdings in investment funds (Article 10.2.c) of Act 16/2012)

VII. SOCIMIS ON THE SPANISH MAB (ALTERNATIVE MARKET)

SOCIMI can opt for trading on regulated markets (thus accessing to a more flexible trading), generally subject to tighter regulatory demands, or on multi-lateral trading systems (such as the MAB), subject to more flexible regulation and less regulatory requirements, located not only in Spain but also in any other European Union Economic Area jurisdiction.

VIII. CREATION OF A SPECIFIC MAB SEGMENT FOR SOCIMI

From 2012 the MAB is a market suitable for SOCIMI so that they can comply with the listing requirement in that market.

The MAB has created an "ad hoc" segment for them, alongside its other three segments (SICAVs, Venture Capital Companies and Growth Companies) and subject to a specific regulation contained in the Circular of the MAB 2/2013 of 15 February (the "Circular 2/2013").

Circular 2/2013 enables both Spanish SOCIMI and foreign companies whose corporate purpose and investment regime are comparable to those established for SOCIMI to join this segment of the MAB.

IX. NECESSARY AGENTS FOR THE ADMISSION OF A SOCIMI ON THE MAB

Admission on the MAB requires the SOCIMI to designate a registered advisor to liaise with the supervisory authorities both at the time of inclusion and later on once it is listed. Its main task is to assess the suitability of SOCIMI interested in joining the MAB segment and to advise them in regard to the regime applicable to the trading of their securities, as well as in preparing and submitting financial and corporate information required for operating in that segment.

In order to boost the liquidity and trading of shares in SOCIMI the MAB requires SOCIMI or their core shareholders to sign a liquidity agreement with a liquidity provider, which may be an investment services company or a credit institution. The main purposes of this agreement are to boost liquidity in transactions affecting SOCIMI's shares, to achieve adequate trading frequency and to reduce price fluctuation not caused by the overall market trend.

The MAB, in the Circular 2/2013, requires that, at the time of admission, SOCIMI submit a valuation report of the company prepared by an independent expert in accordance with international valuation standards (copy of this report shall be attached to the relevant document for admission to trading). Said valuation shall not be necessary if, in the six months prior to the application for admission, SOCIMI have conducted a share placement or financial operation to determine the initial listing price of their shares.

Public float or Free float^{xii}

In order to ensure the adequate operation of this segment and to facilitate share liquidity, the MAB requires a minimum free float at the time of their inclusion on the MAB. Circular 2/2013 requires SOCIMIs to reach the requirement to have shareholders with shareholdings of less than 5 per cent of share capital, representing the lesser an estimated market value of two million euro or 25 per cent of the shares issued by the company. In case of not accessing to the settings at the time of the admission, it is sufficient if a mandate is granted to the Liquidity Provider to achieve this ownership.

Notwithstanding the foreign, as detailed in section 3 of the First paragraph of the Circular, the candidate SOCIMI listed on the MAB that cannot comply the requirement mentioned above, will only require to issue a mandate to the Liquidity Provider (Investment Firms or Credit Institution). Thus, the MAB opens the door to those SOCIMIs that cannot comply with this free float, to reach them establishing that contract/mandate.

X. DOCUMENTS AND DEADLINES IN ORDER TO INCLUDE A SOCIMI ON THE MAB

To be listed on the MAB, SOCIMIs must present an application for admission to trading, along with a prospectus called "information document for inclusion on the MAB", which must contain information regarding the real estate assets and their management, as well as financial and corporate information. For illustration purposes, the aforesaid "information document for inclusion on the MAB" shall include the following information:

- (i) Description of the real estate assets, situation and condition, depreciation periods.
- (ii) Potential cost of the same being put into use due to a change in lessee.
- (iii) Tax information.
- (iv) Description of the policy for investment and replacement of the assets,
- (v) Valuation report by an independent expert in accordance with internationally accepted criteria, unless within six months prior to the application a share placement is made or a financial transaction that are relevant for determining a first reference price for the start of trading of the shares of the company.
- (vi) Number of shareholders, with details on the number of the shares and percentage of major capital.

The financial information provided to the MAB must be prepared in accordance with International Financial Reporting Standards (IFRS) or national accounting standards, unless the issuing company was incorporated outside the European Economic Area, in which case it may choose to apply Generally Accepted Accounting Principles used in the United States (US GAAP).

The procedure for admission to trading on the MAB takes between two and four months. In any event, it all depends on various factors, such as whether or not it is necessary to restructure the company or its group beforehand, the type of financial information to be included in the "information document for inclusion on the MAB" or the conducting of a public offering for the sale or subscription of shares. However, unlike other segments of the MAB or our Spanish Stock Exchanges, in this SOCIMI segment, issuers or their shareholders will not be obliged to conduct an offering, whether public or private, for the sale or subscription of shares prior to their inclusion on the MAB in order to comply with the minimum free float requirement, since the Circular 2/2013 allows SOCIMI or their core shareholders to place at the disposal of the liquidity provider all or part of the shares necessary to reach the free float threshold.

Once the SOCIMI's shares have been listed on the MAB, Circular 2/2013 prohibits their core shareholders and key executives from selling shares or performing transactions equivalent to selling shares during the first year following their listing on the MAB, except those placed at the disposal of the liquidity provider.

Lock-up

Once the shares are listed on the MAB, Circular 2/2013, prohibits its reference shareholders and key executives to sell shares or perform equivalent operations to sales of shares within one year of its admission on the MAB, except those available to the liquidity provider.

XI. DISCLOSURE AND TRANSPARENCY REQUIREMENTS OF SOCIMIS LISTED ON THE MAB

Once their shares have been listed on the MAB, SOCIMI must provide the MAB with information on a regular basis. In its regulations, the MAB has sought to strike a balance between two principles: the principle of sufficient information, as investors must have available a reasonable amount of information to enable them to make trading decisions, and the principle of simplicity, inherent to the MAB, which, as a multilateral trading system, is subject to more flexible requirements than those required for trading on a regulated market.

Once its shares are admitted to trading on the MAB, the issuer shall be obliged to make available to MAB the following information:

- Periodic information:
 - Every six months: summarized unaudited annual accounts, including a reference to important events occurred and a list of shareholders with a position equal to or higher than 5% of which it is aware
 - On an annual basis: the audited annual accounts
- Other information, including communications on significant shareholdings, transactions by directors and executives and the signing, renewal or termination of shareholders' agreements that restrict the transfer of shares or affect shareholders' voting rights and other information that must be deemed relevant or of interest to investors.

Finally, it should be highlighted that SOCIMI must have a website including all the public information relating to the process of inclusion of their shares on the MAB as well as any further information that they submit to the MAB from time to time.

ⁱ Such as the French “*Société d’Investissements Immobiliers Côtée*” (SIIC), the “*Fiscale Beleggingsinstelling*” (FBI) in the Netherlands, or the “*G-REITs*” in Germany.

ⁱⁱ They will be governed by the provisions of corporate/commercial law, as well as by the special provisions of Act 11/2009 on SOCIMIs (including the reform brought in by the Tax Measures Law – Law 16/2012, of December 27, 2012).

ⁱⁱⁱ The minimum capital stock that these entities must have (formerly, €15 M) has therefore been reduced under the new regime.

^{iv} Any references in this newsletter to SOCIMIs should also be deemed to include unlisted SOCIMIs unless indicated otherwise.

^v The requirement that the shares of listed companies must be registered already applies in Spain in industries such as the banking and airline industries.

^{vi} On the terms established in the value added tax legislation.

^{vii} Provided that they reside in a country or territory with which there is an effective Exchange of tax information.

^{viii} We mean non-resident companies that are subject to the same listing requirements, have the same corporate purpose as SOCIMIs, are subject to a similar income distribution policy, and reside in countries or territories with which there is an effective Exchange of tax information.

^{ix} We consider that the lawmakers intended to extend this requirement to all income obtained by the SOCIMI

^x This minimum investment requirement will be computed by reference to the following rules: (i) The 80% will be calculated by reference to the consolidated balance sheet; (ii) The real estate must be acquired for ownership; (iii) Neither the special-feature assets under article 8 of the Cadaster Law (in Spanish: *Ley del Catastro*), such as motorways, ports or airports, nor the assets provided to third parties under finance lease agreements qualify for the purposes of this calculation; (iv) Real estate located abroad must have equivalent characteristics to the real estate located in Spain and there must be an effective exchange of tax information with the country or territory in which they are located.

^{xi} The especial 19% charge will be applied to the income for accounting purposes that is distributed by the SOCIMI in the form of dividends, and not to the proportional part of the tax base relating to that income (e.g., this would mean, that even if the special 19% charge applied, it would not be affected by any tax adjustments that might be made to the entity's income for accounting purposes, such as those relating to the deductibility of finance costs).

^{xii} Public float or free float represents the portion of shares of a corporation that are in the hands of public investors as opposed to locked-in stock held by promoters, company officers, controlling-interest investors, or government. This number is sometimes seen as a better way of calculating market capitalization because it provides a more accurate reflection rather than the entire market capitalization. In this context, the float may refer to the entire market capitalization of the company or all the shares outstanding that can be publicly traded.

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