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BUDGET BILL FOR 2009: REAL ESTATE INVESTMENT FUNDS FOR RENTAL PURPOSES

As a result of the worldwide financial crisis, the Portuguese government proposed in the budget bill for 2009 an incentive that will benefit banks by allowing them to clean their balance sheets, and for homeowners by allowing them to pay less for their loans. This incentive introduces two new legal concepts: real estate investment funds for rental purposes ("FIIAH," the Portuguese abbreviation) and real estate investment companies for rental purposes. These funds will be subject to the general rules applicable to other real estate investment funds but will also benefit from special tax incentives.

Generally, anyone who has a mortgage may sell his dwelling to a FIIAH, while maintaining the right to live in it by negotiating a lease agreement with the fund's managing entity, and receive a call option to buy the dwelling back prior to December 31, 2020. This option is not negotiable and is transmittable

only to one's heirs. In the meantime, the seller pays monthly rent to the fund, which the government expects to be lower than the amount paid for the bank's loan because there will be no amortization of the capital lent by the bank. However, individuals interested in selling their dwellings to a FIIAH must consider two aspects: (1) the means through which the government intends to keep the rents lower than the amounts being paid to the banks remain, for now, unknown; and (2) the call option expires if the rent is not paid for more than three months.

What Characterizes a FIIAH?

FIIAHs must be closed-end funds of public subscription. After the first year of activity, the total value of a FIIAH's

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assets must be at least ten million euros, and the fund must have a minimum of 100 participants whose individual participation units must not exceed 20% of the fund's assets. At least 75% of the FIIAH's assets must be immovable property located in Portugal that is designated for rental housing purposes. FIIAHs must distribute no less than 85% of their net profits.

Tax Incentives

In general, transactions on immovable property are subject to several Portuguese taxes. The sale of a house subjects the seller to capital gains taxable as personal income tax and the buyer is subject to municipal tax and stamp duty. The owner of a household (landlord or proprietor) on December 31 of each year is subject to municipal tax on immovable property.

The main incentive to advance the creation of FIIAHs is tax relief. In short, the fund and its participants may be almost totally exempt from taxes. First, capital gains derived from the sale of households to a FIIAH are exempt from Portuguese personal income tax as long as the previous owner enters into a lease agreement with the fund's managing entity. Also, taxpayers may credit against their final

personal income tax liability 30% of qualifying expenses incurred under the lease, with a limit that can go up to 879 euros for taxpayers with lower income (7,142 euros) and up to 644 euros for taxpayers with income up to 41,021 euros. For taxpayers with higher income, the limit is 586 euros. If a tenant exercises the call option, the purchase is exempt from municipal tax on the transfer of immovable property (IMT) and stamp duty.

With respect to taxation of the fund, any income obtained by FIIAHs between January 1, 2009, and December 31, 2014, is exempt from corporate income tax. Further, the fund is exempt from IMT and stamp duty on the acquisition of houses for rental purposes, as well as from the municipal tax on immovable property (IMI) on houses that constitute FIIAH's assets. FIIAH's managing entities are exempt from all supervision charges in connection with managing activity related to these funds.

For individual and corporate holders of participation units, the law grants an exemption from Portuguese personal and corporate income tax on any income received or made available. However, this exemption is not extended to capital gains derived from the sale of the units.

State Aid

As FIIAHs benefit from several tax incentives, the EU's framework for state aid must be considered. In accordance with the state aid regime, the Commission must be notified of any plans to grant new aid, and these plans should not be put into effect before the Commission has authorized them ("standstill clause"). The member state must provide all information necessary to enable the Commission to make a decision on whether the aid under analysis distorts or may distort competition affecting trade between member countries.

Since member states are subject to the standstill clause, no specific deadline was established for notifying the Commission. Therefore, notification must be timely, meaning that the member state must inform the Commission in advance of the date chosen for the aid to be put into effect.

Conclusion

Publication in the Official Gazette is the last step before a new law enters into force. Before publication, however, the budget law must be ratified by the President of the Republic. At press time, there were rumors that the President was not willing to ratify the budget, so entry into force was still uncertain. ●