MAZARS INTERNATIONAL TAX CONFERENCE 2019

REAL ESTATE
1. INTRODUCTION
2. PHASE 1: ACQUISITION
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INTRODUCTION

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Tax and Financing considerations during the acquisition of real estate
PHASE 1: ACQUISITION

- Tax Due Diligence
- Tax Structuring
- Purchase Agreement
- Final Purchase Price Calculation
(1) Tax Due Diligence: Areas of typical Tax Risks

- **Transactions with related parties**
  - Compliance with arm’s length principle
  - In particular in cross-border groups
  - Foreign Tax Act/ Constructive dividends

- **Tax balance sheet treatment**
  - Purchase price allocation
  - Capitalization of expenses
  - Depreciation schedule (incl. extraordinary write-offs)

- **Tax impacts from past re-structurings**
  - Latent gains
  - Forfeiture of tax losses
  - Triggering of real estate transfer tax
  - Tax groups

- **VAT related risks**
  - Deduction of input VAT (mixed-use properties; formal requirements)
  - Reverse charge

- **Building Withholding Tax**
## Phase 1: Acquisition

### (2) Tax Structuring: Critical Aspects

<table>
<thead>
<tr>
<th>Asset Deal</th>
<th>Share Deal</th>
</tr>
</thead>
<tbody>
<tr>
<td>▪ Taxation of disposal profit by the seller</td>
<td>▪ Forfeiture of tax losses at the level of the target entity</td>
</tr>
<tr>
<td>▪ Triggering of real estate transfer tax</td>
<td>▪ Real estate transfer tax might be avoided</td>
</tr>
<tr>
<td>▪ Take-over of input VAT corrections in case of a qualification as a transfer of going concern</td>
<td>▪ Deductibility of interest expenses in the future (e.g. through debt-push-down or tax group)</td>
</tr>
<tr>
<td>▪ Withholding taxes on future dividends</td>
<td>▪ Exit taxation</td>
</tr>
</tbody>
</table>

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Complemented by:
- Legal advisory
- Financial advisory
PHASE 1: ACQUISITION

(3) Purchase Agreement: Tax Related Issues

- **Tax guarantees**
  - General tax compliance
- **Tax indemnities**
  - Coverage of all taxes and ancillary costs up until Closing
  - Alignment with purchase price calculation
  - Restriction of exceptions
  - Avoid reference to general limitations (cap, de minimis, knowledge, time)
  - Rights and obligations in tax proceedings
- **Purchase price determination**
  - True-up vs. locked-box
  - Relevant closing date
  - Consideration/ assessment of assets and liabilities
  - Preparation, review and agreement procedures
(4) Final Purchase Price Calculation: Typical Review Items

- Recoverability of receivables
- Operating costs
- Provisions (tax and others)
- Incoming invoices received post closing date
- Prepaid expenses and deferred income
Phase 1: Acquisition

Financing instruments

- Real Estate project finance structuring, e.g. asset deal or share deal structure
- Loan and Equity and LTV considerations, mix of Equity, Mezzanine and Debt
- Derivatives, e.g. interest rate swaps
- Collateralization of Loans

Financing Considerations

- Financial structuring, e.g. mix of financing instruments (e.g. bank loan, debt fund as loan providers)
- Net operating income vs. yield expectations
- Interest rate related instruments (fixed or floating rates, derivatives such as swaps, caps)
- Investment horizon and term of financing (implications on amortization period)

Transaction Advisory and Valuation as well as Structuring
PHASE 2: OPERATIONS AND MAINTENANCE

Tax and Financing considerations during the ownership of real estate
POTENTIAL OWNERSHIP STRUCTURE AND TAX CONSIDERATIONS IN OPERATIONAL PHASE

- Third party/connected party tenants
- Tenant inducements – capital vs revenue
- Capital appreciation
- Inter-company lending – Anti-hybrids and other rules
- Third party financing (and refinancings)
- BEPS Action Point 4
- Capital Expenditure and Tax Depreciation
- Withholding Taxes
- VAT
- Corporate Income Tax filings
- Transfer Pricing
- IFRS 16? Limited impact for landlords (but may affect intra-group tenants!)
Phase 2: Maintenance

Financing Considerations

- Change in interest rate environment may have implications on financing structure
  - refinancing of loan
  - restructuring of financial structure

- Covenant breach
  - financial restructuring
  - collateralization

- Cash-out of Equity
  - excess cash outflow

- Additional financing for maintenance and/or modernization of property to increase value

- Real estate valuation on property level or portfolio level, calculation of lending value and market value for financiers

Transaction Advisory and Valuation as well as Structuring
PHASE 3: EXIT OF INVESTMENT

General considerations - main issues to have in mind
TAKing the right decisions in the framework of an acquisition

Questions at the date of an exit for the seller:
- Tax leakage on capital gain
- Tax economy / transfer of the tax losses
- Tax leakage on registration duties (in France, buyer's liability)

Best option: asset deal or share deal?

Questions at the date of an acquisition for the buyer:
- Future tax leakage on latent capital gain (in case of a share deal)
- Tax economy / transfer of the tax losses
- Tax leakage on registration duties

Best option: asset deal or share deal?

How to deal with opposed interests?

Finding a convenient solution for both parties
Criteria 1 Valuation
Is the company a RE tainted company?

Criteria 2 Nature of the asset or the shares

Criteria 3
- Pre or post-transaction restructuration impact
- Maintain of the activity
- Impact of a change of ownership

Exit
Registration duties
Capital gains?
- On which asset?
- Where is the capital gain taxable?
- Upon which taxation regime?

Asset deal
- On RE properties
- On business corporate
- Participation exemption (2 years)
- Exception for RE tainted shares

Share deal
- Transfer to buyer
- Kept by the seller

Tax losses if any (only in share deal)
- Registration duties
- Capital gains?
The qualification of RE tainted company will mostly depend on the valuation of the different assets of the company.

Consequence of the valuation / RE tainted qualification:
- Location of taxation place
- Capital gain taxation
- Registration duties

Most common valuation issues:
- Date of realization
- Trustworthiness and on the edge valuation
- Modification of the Target’s asset / Pre-closing restructuring
- Reliance on the valuation
### French example:

<table>
<thead>
<tr>
<th>Share deal</th>
<th>Asset deal</th>
</tr>
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<tbody>
<tr>
<td>SA, SAS</td>
<td>RE Property</td>
</tr>
<tr>
<td>SARL</td>
<td>Business corporate</td>
</tr>
<tr>
<td>RE tainted company (*)</td>
<td></td>
</tr>
</tbody>
</table>

**Rate**
- 0.1%
- 3%
- 5%
- 5.8%
- 5%

**Basis**
- Fair market value

(“) Determination of the RE tainted qualification depends on the valuation (see before)
TRANSFER OF TAX LOSSES

Pre / post transaction restructuring

• Split of a Company (e.g. OpCo /PropCo)
• Origin of the tax losses (activity) - holding activity
• Tax group before the Operation
• Necessary tax ruling

Continuity of the activity

Change of control / ownership

In France, no impact
### DEALING WITH OPPOSED INTERESTS

<table>
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<tr>
<th>Share deal</th>
<th>VS</th>
<th>Asset deal</th>
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<tr>
<td><strong>Seller</strong></td>
<td><strong>Buyer</strong></td>
<td><strong>Seller</strong></td>
</tr>
<tr>
<td>• Latent capital gain on shares value</td>
<td></td>
<td>• Latent capital gain on the asset</td>
</tr>
<tr>
<td>• Participation exemption régime possible (in France, not for RE Tainted companies)</td>
<td></td>
<td></td>
</tr>
</tbody>
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Open issue: tax saving: CIT rate

#### Potential solution

- Asset deal / Share deal: split of the tax economy between the parties
- Timing of reorganization:
  - pre transaction restructuring to isolate the business /RE property to be sold and
  - post acquisition restructuring to ensure tax efficiency

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### Seller's interest

- Share deal rather than asset deal
- Reorganization post transaction

### Buyer’s interest

- Asset deal rather than a share deal
- Reorganization pre transaction
Phase 3: Exit/Sale

Financing Considerations

- Change of control may have implications on financing structure
  - restructuring of financial structure / transfer of loan

- Earlier as planned exits/sales may have implications on derivatives (swaps)
  - market value of swap depends on interest rate environment at time of exit

- Early repayment of financing structure may result in prepayment penalty (e.g. GER)

- Challenging or even distressed RE assets have implications on financial structure at exit (e.g. as a result of value driven portfolio analysis)
  - NPL assets vs performing assets / carve out portfolio transactions

Transaction Advisory and Valuation as well as Structuring