EU and OECD continue work at high speed

> Both at OECD and EU level, the drafting of systematic changes in tax rules continues at high speed, with potential severe impact on after-tax returns of INREV funds.

> At OECD level, INREV continues its active work on engaging with the OECD BEPS project, underlining the (special) nature of real estate investment funds.

> At EU level, INREV continues monitoring the Anti-Tax Avoidance Package initiated by the European Commission, which contains a number of elements that are likely to have far-reaching consequences for national corporation tax systems in the near future.

Introduction

The internationally coordinated political effort to combat tax avoidance has led to a multitude of (proposed) measures at the global, regional and national level.

The OECD and European Union are progressing with important changes to critical tax rules, including the access to tax treaty benefits, the use of participation exemption regimes and the tax deductibility of interest payments. At OECD level, work on the BEPS project recently saw another public consultation on Action Plan 6 – dealing with the granting of tax treaty benefits to non-listed funds. At EU level, several initiatives are and have been undertaken to prevent aggressive tax planning and to increase tax transparency in Europe. Especially the far-reaching attempt to harmonize national anti-tax avoidance legislation by means of a European Anti-Tax Avoidance Directive stands out.

Although in the perception of some these measures primarily concern multinational enterprises, in reality the measures are likely to result in higher effective tax burdens and costs for the non-listed real estate funds industry as well, potentially putting pressure on investors’ returns and managers’ fees.

1. OECD level:
BEPS Action Plan 6 consultation

- In connection with Action Plan 6 of the OECD BEPS project, following recommendations for denying tax treaty benefits in inappropriate circumstances, the OECD asked for further information building on earlier consultations. In its latest consultation published on 24 March, the OECD sought public input in order to find appropriate solutions for non-listed investment funds (‘non-CIVs’), to ensure that these are not being caught up in their recommendations. Such funds arguably include non-listed real estate fund structures.

- In its consultation, the OECD expressed two main concerns about granting tax treaty benefits to non-CIVs that make finding an appropriate solution challenging:
  - Some non-CIVs may be used to provide treaty benefits to investors that are not themselves entitled to treaty benefits, and
  - Investors may defer recognition of income on which treaty benefits have been granted.

- In a submission filed in late April, INREV addressed the concerns raised and answered specific questions relevant for non-listed real estate funds.

- On the first issue, INREV argued that a specific carve-out for non-listed real estate funds is justified, based on the unique tax profile of real estate. Whereas the granting of tax treaty benefits to non-CIVs typically concerns withholding taxes, real estate taxation is about profit tax – not withholding tax. Given this unique tax profile, the concerns raised by the OECD in relation...
to granting tax treaty benefits to non-CIVs should not be relevant to non-listed real estate funds. Hence, we argued that the concerns expressed by the OECD do not normally arise in non-listed real estate funds and a specific carve-out for non-listed real estate funds is justified.

- On the second issue, INREV referred again to the unique tax profile of real estate. Source states typically secure immediate real estate income taxation by means of levying profit taxes. Hence, non-listed real estate funds cannot be used for deferral of taxation.

- Further, INREV argued that non-listed real estate funds should pass the PPT (Principal Purpose Test), once more referring to the unique tax profile of real estate whereby property countries secure immediate real estate income taxation by levying profit taxes. Given this fact, non-listed real estate funds cannot be used for treaty shopping and/or tax deferral.

- INREV’s response to the OECD’s consultation was developed in consultation with a large number of other real estate associations, although in some ways it took a different approach.

2. EU level:

- After the introduction in 2014 of a number of anti-avoidance measures relating to the European parent-subsidiary directive, the EU has continued to work on further-reaching legislative initiatives to combat tax avoidance. This led to the proposed Anti-Tax Avoidance Package by the European Commission in February 2016 containing several measures to tackle aggressive tax planning in Europe.

  - On 20 June 2016 the EU Council reached political agreement on the Anti-Tax Avoidance Directive (ATAD). The main goal of the ATAD is to ensure a coordinated and coherent implementation at EU level of some of the OECD’s BEPS recommendations and to add certain anti-tax avoidance measures which are not part of the OECD BEPS project.

  - The ATAD lays down rules against tax avoidance in five specific fields: (i) deductibility of interest, (ii) exit taxation, (iii) general anti-abuse rule (GAAR), (ii) controlled foreign company (CFC) rules; and (v) hybrid mismatches. The rules of the ATAD merely set the minimum required standards: Member States may apply additional or more stringent provisions aimed at BEPS practices.

  - The expected impact from the ATAD is significant, as EU directives constitute “hard law”. The Member States have to implement all measures into their local legislation as of 1 January 2019, except for the exit taxation provision and the interest deduction limitation provision. The exit taxation provision must be implemented by 1 January 2020. The implementation of the interest deduction limitation provision can be postponed until 1 January 2024, subject to certain conditions.

  - The implementation of the ATAD will in some Member States require significant changes to currently existing corporate income tax rules, such as interest deduction limitations, but will also require the introduction of completely new sets of rules like for CFCs (in brief: taxation at the level of EU companies of certain types of non-distributed “low-taxed” income of (in)directly held subsidiaries or establishments) and hybrid mismatches in many Member States. Real estate income is excluded from the types of “low taxed” income covered by the CFC rule.

  - Further, in an effort to increase tax transparency, the European Union continues to expand the automatic exchange of information between Member States. A significant increase in reporting obligations and exchange of information under national law should therefore be expected. Already, many jurisdictions have implemented the “master/local file” and country-by-country reporting obligations, as well as additional exchange of information provisions, for example with respect to tax rulings.