DG TAXUD
Submitted electronically

Brussels, 19 January 2024

SUBJECT:

Public consultation – Directive on Business in Europe: Framework for Income Taxation (BEFIT)

The European Public Real Estate Association (EPRA) welcomes the opportunity to provide feedback on the BEFIT proposal. EPRA is the voice of Europe's listed real estate companies and with more than 290 members (companies, investors, and their suppliers), EPRA represents over 840 billion EUR of real estate assets (European companies only) and 95% of the market capitalisation of the FTSE EPRA Nareit Europe Index.

KEY HIGHLIGHTS AND RECOMMENDATIONS

EPRA is concerned about the prospect of making the rules mandatory for certain large companies. Specifically, enforcing BEFIT rules on real estate investment trusts (REITs) falling within the scope could introduce more complexity and uncertainty, potentially disrupting the current European REIT regime's landscape.

- Specific tax mechanisms ensuring REITs' tax exemption vary from country to country, which can lead to an uneven application of BEFIT rules;
- Due to the notion of 'subject to tax' outlined in the Directive and the variety of tax mechanisms for achieving exemptions in different European REIT regimes, this may result in varied interpretations among member states, increasing uncertainty and uneven application of the rules;
- The thresholds set out in the Directive to be part of the BEFIT group would impose additional burdens and complexities;
- The unique nature of the REITs regime and their importance within the real estate markets are crucial considerations for policymakers. This uniqueness has led real estate investment vehicles to benefit from recent carve-outs at OECD level to avoid disruption;
- Instead of mandatory adherence**, EPRA suggests that REITs falling within the scope should have the option to voluntarily adhere to these rules;**
- Alternatively, for REITs falling within the scope of the Directive, **EPRA would see merit in granting member states the possibility to exclude companies under a special tax regime.**

BACKGROUND

EPRA understands the policy goals at the core of the BEFIT proposal. The directive aims to simplify corporate tax procedures for businesses, decrease the necessary compliance administration, thereby enhancing the competitiveness of the single market.

While EPRA sees benefits in some of the measures, we are concerned about making the rules mandatory for certain large companies. Specifically, the mandatory application to real estate investment trusts (REITs) falling within the scope can lead to unintended consequences.

This paper aims to outline the specific characteristics of REIT regimes in Europe and the potential unintended consequences of the mandatory application of the BEFIT rules, emphasising the necessity to provide flexibility for REITs when applying them.

EXPLAINING THE REIT REGIME CONCEPT IN EUROPE

REITs are guardians of our cities' high-quality assets, covering all types of real estate assets, from offices to retail, and increasingly healthcare and retirement facilities.[1] They help communities grow, thrive, and revitalise and provide an investment opportunity that makes it possible for everyday citizens as well as large institutional investors to benefit from valuable real estate, dividend-based income, and total returns. As societies in Europe are facing challenges to provide for their rapidly greying populations, REITs play a crucial part in providing retirement security to millions of people, by offering long-time investors like pension funds and insurers stable and highly competitive assets to invest in. Furthermore, they are great contributors to GDP and society as they represent hundreds of thousands of jobs in our continent. Currently established in 13 EU Member States, the introduction of REIT legislation by national governments has always been seen as an opportunity to attract new sources of capital into the local real estate market in a more open, transparent, liquid, and advantageous form of investment.

Real Estate Investment Trust (REIT) can be defined as *''a widely held company, trust or contractual or fiduciary arrangement that derives its income primarily from long-term investment in immovable property (real estate}, distributes most of that income annually and does not pay income tax on income related to immovable property that is so distributed.''* [2]

The fact the REIT vehicle does not pay tax on that income is the result of tax rules that provide for a single level of taxation in the hands of the investors in the REIT (with corresponding withholding tax obligations imposed on the REIT with respect to its distributions to foreign investors).

Tax status of REITs in Europe

Despite these common features, there may be differences between countries as regards how REITs are structured and how the tax exemption of the income is provided. In some countries, REITs were developed using the tax rules generally applicable to trusts and companies; in others, a specific REIT tax regime has been adopted.

The specific tax mechanisms that ensure REITs are tax-exempt can vary from country to country and can include, for example, rules that allow the deduction of REIT dividends or distributions; tax exemption of only the part of the REIT's income distributed within a specific period; tax exemption of a REIT that meets certain conditions or rules that allocate income to investors rather than to the REIT itself. In addition, REITs are increasingly investing cross-border, including in jurisdictions that do not recognise a REIT status, resulting in full tax liability there.

The structural nuances and tax exemptions associated with REITs exhibit considerable diversity. The divergence in how various member states integrate REITs into their tax frameworks, underscores the complex global landscape, in such a way that the determination of whether a REIT is subject to BEFIT rules may give rise to different interpretations and presents a risk of not being uniform across all EU member states.

Carve-out from Pillar Two agreement

As the BEFIT proposal builds on the OECD/G20 international tax agreement on a global minimum level of taxation, and the Pillar Two Directive adopted at the end of 2022, EPRA would like to recall the discussions with the OECD which have underlined the uniqueness of real estate investment vehicles and the necessity to provide a carve-out for this specific sector. This has led to the exclusion of real estate investment vehicles from the scope of the Pillar

[1] You can find more on the Impact of European REITs in this report: https://www.epra.com/download_file/2505/187.

[2] OECD's definition of a REIT used for the purpose of the OECD Model Tax Convention.

Two agreement approved on 14 December 2021 by the OECD/G20 Inclusive Framework on BEPS, and to the subsequent Directive adopted by the Council.[3]

EPRA aims to underscore the absence of a comprehensive impact assessment specifically conducted for the real estate sector in the Commission's proposal. This has raised concerns among some of our members regarding the potential disruption these rules might cause to the current European REIT regime's landscape.

UNCERTAINTIES SURROUNDING THE APPLICATION OF BEFIT RULES TO REITS

(1) Tax status and scope of the Directive

The existing ambiguity in the wording of Article 2 has prompted numerous stakeholders to question its precise scope. Under this article, the rules of the Directive are to be applied to a company, along with its permanent establishments in other member states, which are *"subject to one of the corporate taxes listed in Annex II or to a similar tax subsequently introduced."* The notion of being "subject to tax" introduces uncertainty. The international bureau of fiscal documentation (IBFD), in their comprehensive report on the BEFIT Directive[4], points out that it is unclear whether this should encompass companies that are tax-exempt or have the option to be. In contrast, other corporate tax Directives, such as the parent-subsidiary Directive or the interest and royalty Directive, explicitly include wording to cover companies "without the possibility of an option or of being exempt"[5] or companies that are not exempted.[6]

As mentioned earlier, the methods by which REITs achieve tax exemption vary. While some operate under a tax transparency regime, others may be subject to corporate income tax with a de facto zero or near-zero taxable basis on real estate results. Adding to the complexity, cross-border investments made by REITs, extending into jurisdictions that do not acknowledge REIT status, expose these entities to full tax liability there.

The current uncertainty permits various interpretations, making it challenging to anticipate the potential impact of the proposed rules on business operations and real estate markets in EU member states for REITs falling within the revenue threshold.

(2) Unclear consolidation within a BEFIT group

In addition to the BEFIT proposal's ambiguity regarding the notion of "subject to tax," the various rules pertaining to the formation of a BEFIT group add complexity. The BEFIT group is indeed confined to the European subset of entities that meet the 75% threshold, as outlined in Article 5. Consequently, it is unclear how the consolidation of BEFIT rules can be executed when applying rules that do not encompass all the companies forming a group.

Despite the BEFIT proposal's intention to simplify corporate tax procedures, the ambiguity surrounding the definition of "subject to tax" and the requirement for EU entities to meet a 75% threshold, as outlined in Article 5 of the proposal, could lead to an unreasonably complex outcome for REITs.

EPRA'S RECOMMENDATIONS

EPRA raises concerns about the potential unintended consequences of automatically applying the rules of the BEFIT proposal to REITs falling within the scope. While EPRA acknowledges the merits of certain measures contained in the proposal, we believe that, due to the reasons exposed in this paper, **REITs should have the option to voluntarily adhere to these rules rather than be mandated to do so.**

Alternatively, EPRA would see merit in **granting the possibility for member states to exclude companies under a special regime from the scope**. Member states, possessing a more profound understanding of their national tax systems and REIT structures, would be in the best position to determine whether these entities should fall within the scope of the BEFIT Directive. Member states would also be best placed to assess whether a similar outcome could be achieved through the prerogatives granted by Article 48, par. 2 of the BEFIT proposal.

This would ensure that REITs are treated fairly and appropriately under the Directive, mitigating the risk of unintended consequences.

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[3] Council Directive (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union.

[4] https://www.ibfd.org/sites/default/files/2023-10/2023.10.12-befit_an-initial-assessment-vf.pdf.

[5] Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, art. 2(a)(iii).

[6] Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, art. 3(a)(iii).

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We trust that our feedback will aid in fostering productive debates and in reaching an agreement on the Directive proposal. We remain entirely at your disposal to discuss these issues in greater detail. Should you need any other information, we are at your disposal: publicaffairs@epra.com

About EPRA

For 20 years, the European Public Real Estate Association (EPRA) has been the voice of Europe's listed real estate companies, investors, and their suppliers. EPRA achieves this through providing better information to investors and stakeholders, active involvement in the public and political debate, promotion of best practices, and the cohesion and strengthening of the industry. With more than 290 members (companies, investors, and their suppliers), EPRA represents over 840 billion EUR of real estate assets (European companies only) and 95% of the market capitalisation of the FTSE EPRA Nareit Europe Index. Find out more about our activities on www.epra.com.

EU Transparency Register no. **09307393718-06**