LEXOLOGY
Getting The Deal Through

REAL ESTATE INVESTMENT TRUSTS 2024

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Quick reference guide enabling side-by-side comparison of local insights, including into the definition, advantages and disadvantages of REITS, and market climate; organisational and governance considerations; key regulatory requirements, including for publicly traded REITS; categories of REIT and relevant property sectors; eligible investors; and recent trends.

Generated on: October 30, 2023

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Luxembourg

Frank van Kuijk, **Tom Hamen**
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Summary

PRELIMINARY CONSIDERATIONS

Definition

1 | What constitutes a real estate investment trust (REIT) in your jurisdiction?

A real estate investment trust (REIT) is an entity that is dedicated to investments in domestic or foreign real property and benefits from a set of advantageous tax rules. The tax rules generally provide for *quasi-tax neutrality* at the REIT level combined with mandatory distributions of the real estate-related income subject to a withholding tax in the country in which the REIT is established. Luxembourg law does not, unfortunately, provide for a REIT regime.

Despite the absence of a bespoke regime, Luxembourg offers a wide range of other legal products to initiators, promoters or sponsors in the real estate investment business. Even though these rules are not specifically tailored to real estate investments, they are suitable for the purposes of acquiring, developing and holding Luxembourgian or foreign real estate property.

For a number of commercial reasons, foreign REITs often opt for Luxembourgian acquisition or holding vehicles that then acquire real estate assets. These acquisition vehicles are typically organised as unregulated private limited liability companies which are regular taxpayers in Luxembourg. When properly structured, they should however not be subject to a material tax burden in Luxembourg.

In specific cases foreign REITs prefer to own real property assets through a Luxembourg specialised investment fund (SIF). A SIF is subject to approval by the Luxembourg financial regulator (CSSF). As the approval process of a SIF is time consuming, entities are frequently launched under the reserved alternative investment fund (RAIF) regime and adopt the SIF regime at a later stage. This considerably speeds up the launching process. A RAIF is not subject to approval by the CSSF. The CSSF oversees only the manager of the RAIF. That manager should qualify as a European Union (EU)/European Economic Area (EEA) authorised alternative investment fund manager (AIFM). The SIF and the RAIF can be organised as capital companies, limited partnerships or contractual funds. They are subject to risk diversification rules. With the exception of certain exemptions, they shall not invest more than 30 per cent of their assets or commitments in securities of the same kind issued by the same issuer. Under the default tax regime applicable to SIFs and RAIFs, a mere 1 basis point subscription tax is levied at the entity level on the basis of its assets.

A SIF and a RAIF can also be used as an investor-facing real estate fund. Luxembourgian investor-facing real estate funds can, but do not typically, adopt the SIF or RAIF regimes. By default, they are organised as an unregulated special limited partnership (SCSp). Such special limited partnerships generally qualify as alternative investment funds (AIFs). AIFs generally appoint an EU/EEA-based (host) AIFM to ease fundraising efforts or boost their commercial credibility. To avoid the burden of engaging with a host AIFM, non-EU/EEA fund sponsors may also manage a Luxembourg fund directly out of their home jurisdiction. This strategy may complicate or invalidate fundraising efforts in certain EU/EEA jurisdictions. In practice, however, it is relied upon, as certain key EU/EEA investor jurisdictions do accommodate this strategy.

As Luxembourg does not provide for a REIT regime, while being a key jurisdiction for real estate fund initiators, the questions below are, as much as possible, answered with that profile in mind and only address the key attention points of a default investment structure.

Pros and cons of REITs

2 Why were REITs created in your jurisdiction? What are the advantages and disadvantages of using REIT structures in your jurisdiction?

This question is not relevant, as Luxembourgian legislation does not provide for a real estate investment trust (REIT) regime.

Market climate

3 How would you describe the state of the REIT market in your jurisdiction? How common are REITs in practice?

Despite not having a REIT regime, Luxembourg is a key jurisdiction for initiators that seek to set up European-based private real estate funds. Luxembourgian fund structures can rely on a high reputation among international investors. The diversity in legal forms and fund regimes allows Luxembourgian investment structures to accommodate legal, tax and regulatory concerns arising in the jurisdictions where the real estate is situated.

ORGANISATION

Choice of entity and organisational requirements

4 What forms of entity are used for REITs and what basic organisational requirements apply?

Luxembourgian real estate funds are typically organised as limited partnerships. The Luxembourgian special limited partnership is the default legal form for real estate funds. Special limited partnerships closely resemble Anglo-Saxon style limited partnerships and benefit from a wide recognition by international investors and fund managers. The special limited partnership can be formed under a private seal and requires a Luxembourgian general partner. In practice, the general partner is organised as a private limited liability company and must be established in front of a notary who, among others, verifies whether the minimum capital amount (€12,000 or the equivalent in another currency) was funded. The incorporation deed – or an excerpt thereof for the special limited partnership – will thereafter be filed with the Luxembourg Register of Commerce and Companies (RCS) and published in the Luxembourg official electronic platform of central publication in respect of companies and associations (RESA). The RCS excerpt of the special limited partnership will not provide details on the investor base.

Partnerships as subsidiaries

5 | Are REITs permitted to have partnerships as subsidiaries in your jurisdiction?

Luxembourg real estate investment vehicles can generally have Luxembourg or foreign partnerships as subsidiaries. Specialised investment funds (SIFs) and reserved alternative investment funds (RAIFs) must generally abide by specific risk diversification criteria (ie, they should not invest more than 30 per cent of their assets or commitments in securities of the same kind issued by the same issuer). These diversification rules are generally applied on a look through basis.

REITs as subsidiaries

6 | Are partnerships permitted to have REITs as subsidiaries in your jurisdiction?

This question is not relevant, as Luxembourgian legislation does not provide for a real estate investment trust (REIT) regime. Luxembourg and foreign limited partnerships are generally eligible to invest in any sort of Luxembourg vehicle that invests in Luxembourg or foreign real estate.

Governance

7 | What governance issues should the boards of REITs in your jurisdiction be aware of? How are these issues navigated in practice?

Luxembourgian real estate funds are by default organised as special limited partnerships, which typically qualify as alternative investment funds (AIFs). An AIF can generally be defined as a collective investment vehicle that raises capital from a number of investors with a view to investing it in accordance with a defined investment policy. An AIF shall appoint an internal or external fund manager. In order to accommodate distribution and credibility, most sizable AIFs appoint a European Economic Area-based authorised fund manager.

The fund manager is a third-party service provider referred to as a 'host AIFM'. It enters into an agreement with the fund's initiator to delegate portfolio management or obtain real estate investment advice. Fund managers are most inclined towards delegation since it allows higher levels of control and is generally more efficient. Whether that model is possible depends on the jurisdiction of residence of the initiator and the type of regulatory oversight that applies at the level of the initiator.

KEY REGULATORY REQUIREMENTS

Sources of income

8 What are the basic source-of-income requirements for a REIT?

Contrary to classic real estate investment trust (REIT) regimes, Luxembourgian real estate funds are not subject to source-of-income requirements other than the risk diversification rules applicable for reserved alternative investment funds (RAIFs) and specialised investment funds (SIFs) (ie, exemptions, they shall not invest more than 30 per cent of their assets or commitments in securities of the same kind issued by the same issuer). To assess the diversification requirement, a look through approach applies.

Asset composition

9 | What are the basic asset composition requirements for a REIT?

Luxembourgian real estate funds are not subject to asset composition requirements other than the risk diversification rules applicable for RAIFs and SIFs only (ie, exemptions, they shall not invest more than 30 per cent of their assets or commitments in securities of the same kind issued by the same issuer). To assess the diversification requirement, a look through approach applies.

Distributions

10 | What are the basic distribution requirements for a REIT?

SIFs, RAIFs and alternative investment funds (AIFs) used in Luxembourg for real estate funds are not subject to distribution requirements. Distribution, but also recycling requirements, can be agreed contractually, which is typically the case in open-ended and evergreen real estate fund structures.

Consequences of non-compliance

11 | What happens if a REIT fails to meet the basic regulatory requirements? Is relief available if a company fails to meet any of these requirements?

This question is not relevant, as Luxembourg does not provide for a REIT regime.

Compliance best practices

12 | What best practices should be considered to ensure compliance with the key regulatory requirements for REITs in your jurisdiction?

Luxembourgian real estate funds should have their central administration in Luxembourg and should generally be able to demonstrate that their board is fit and proper while having sufficient Luxembourg footprint.

Most real estate funds are managed by an external ‘host AIFM’. A Luxembourg AIFM is subject to a thorough authorisation process, which, among others, focuses on the team, and the size thereof, effectively conducting the business. As the fund initiator generally hires the ‘host AIFM’ and given that authorisation from Luxembourg’s financial regulator (CSSF) and oversight are focused on the Luxembourgian AIFM, the fund initiator is in most cases not directly impacted.

The AIFM is, among others, in charge of the annual reporting process and disclosures to investors.

Public REITs – regulatory treatment

13 Are the requirements for a publicly traded REIT raising capital different from those imposed on private REITs or public non-REIT companies?

This question is not relevant, as Luxembourg does not provide for a real estate investment trust (REIT) regime.

Public REITs – ongoing requirements

14 What are the ongoing securities and disclosure requirements for publicly traded REITs?

This question is not relevant, as Luxembourg does not provide for a real estate investment trust (REIT) regime.

Public REITs – listing rules

15 Do the stock exchanges in your jurisdiction have any special rules that do not apply to unlisted or private REITs?

This question is not relevant, as Luxembourg does not provide for a real estate investment trust (REIT) regime.

SCOPE OF ACTIVITIES AND INVESTMENTS

Categories of REIT and relevant property sectors

16 What kinds of REIT are available in your jurisdiction? In which real property sectors are REITs used?

The Luxembourg entity toolbox allows initiators to invest in all real estate asset classes and categories, without being limited by a specific legal or tax regime. The entities and regimes described here above are tailored to invest in all types of real property sectors, be it residential, office, retail, logistic or student housing.

Special rules

17 | Are there any special rules for different types of REIT?

This question is not relevant, as Luxembourg does not provide for a real estate investment trust (REIT) regime.

Eligible investment property

18 | What assets are treated as qualifying real property under the REIT rules in your jurisdiction? Can REITs located within your jurisdiction invest in real property outside your jurisdiction?

For purposes of the entities used to form Luxembourgian real estate funds (ie, specialised investment funds (SIFs), reserved alternative investment funds (RAIFs), etc) the notion of qualifying real property does not exist. Moreover, these entities and regime are well suited to invest both in Luxembourg-based and foreign real property. This being said, the Luxembourg Budget Bill 2021 has made investments into Luxembourg-based real property more onerous for certain specific Luxembourgian fund vehicles. In fact, certain tax-exempt investment vehicles will be subject to a new real estate tax, levied at a flat rate of 20 per cent, on income and gains derived from real estate assets situated in Luxembourg.

Permitted activities

19 | Are REITs in your jurisdiction allowed to engage in any ancillary non-investment activities, such as real property management and development?

Since no specific REIT regime exists, the possibility for ancillary non-investment activities to be performed is to be examined under the laws applicable to the investment vehicle chosen for a real estate fund. However, there are no limitations applicable to Luxembourgian investment vehicles. Property management and development activities are carried out through special purpose entities, which may or may not be controlled by the investment vehicle.

Depending on the nature of the ancillary non-investment activity, specific licensing requirements either in Luxembourg or abroad may apply.

Eligible investors

20 | Who may invest in REITs in your jurisdiction? What types of investor do they typically attract? Are there any restrictions on foreign investors?

Luxembourgian real estate investment vehicles, whether they are formed as regulated or non-regulated vehicles, generally obtain their funding from institutional, professional or sophisticated private investors. The SIF and RAIF legislations restrict the offering of an interest in a SIF or RAIF to 'well-informed investors'. Those investors are deemed to be able to adequately assess the risks associated with an investment in this type of vehicle. Investors that invest a minimum amount of €125,000 qualify, subject to self-adherence, as 'well-informed'. For SIFs and RAIFs, these conditions apply neither to the general partners of limited partnerships and of partnerships limited by shares, nor to their managers or any other persons involved in their management. In addition, the distribution of Luxembourg-based alternative investment funds managed by an EU/EEU alternative investment fund manager is in principle restricted to professional investors in the sense of Annex II of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on Markets in Financial Instruments (MiFID II).

Transactions with non-REITs

21 | Are there any special considerations when REITs negotiate purchases and sales or leases of investment real estate with non-REITs?

There are no such special considerations from a Luxembourgian perspective.

Acquiring non-REIT corporations

22 | Are there any special considerations when REITs acquire non-REIT corporations?

There are no such special considerations from a Luxembourgian perspective.

UPDATE AND TRENDS

Recent developments

23 | What have been the most noteworthy recent developments affecting REITs in your jurisdiction, including any significant legal or regulatory changes and commercial trends?

On 27 March 2023, the Ministry of Finance submitted to the Luxembourg Parliament its Bill of Law No. 8183 (the Bill), bringing substantial improvements to the Luxembourg toolbox for investment funds and their managers by proposing amendments to the SICAR Law, the SIF Law, the UCI Law, the RAIF Law (collectively, the Product Laws) and the AIFM Law. Noteworthy changes include, among others:

- extension of legal corporate forms available for Part II UCIs to partnerships limited by shares (SCA), common and special limited partnerships (SCS/SCSp), private limited liability companies (SARL) and cooperatives organised as public companies limited by shares (SCoSA);

- lowering the eligibility threshold for 'well-informed investors' from €125,000 to €100,000;
- doubling the timeframe for reaching the minimum regulatory capital from 12 months to 24 months for SICARs, SIFs and RAIFs and from 6 to 12 months for Part II funds;
- confirmation that RAIFs can be marketed to non-professional investors in Luxembourg; and
- finally, the Bill also intends to amend certain rules related to AIFMs and management companies (notably on their liquidation).

Parliament voted on the Bill on 11 July 2023. The Law entered into force on 29 July 2023.

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