



REAL ESTATE INVESTMENT GUIDE PORTUGAL

Prima Carta | 2018

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INTRODUCTION

In recent years, Portugal has become an attractive market for investment in real estate. The market has seen a huge growth in volume of transactions during that time, particularly in Lisbon. This has been facilitated by the Golden Visa program, which allows citizens of non-EU Member States to apply for a residency permit, subject to certain conditions

The last two years (from January 2016 to December 2017) were responsible for 48% of total residence permits for investors (ARI) were issued out of all such permits issued since they were created in 2012.

Furthermore, in 2015 significant changes in the tax treatment of collective investment entities, including Real Estate Investment Funds incorporated either as corporate funds or as contractual funds, came into force and this has served as a further boost to the market.

The stability of the real estate market along with a large inclination among market players to embrace foreign investment has placed Portugal, and particularly Lisbon, as an attractive place in which to invest.

Investors around the world want to have a clear idea of the acquisition process and the relevant tax implications arising in connection with these transactions and ongoing ownership. Accordingly, we have prepared this real estate investment guide to allow investors to assess the regime and to obtain an overview of the legal issues involved with property acquisitions in Portugal. For any further questions, please contact our office or visit us at www.prima-carta.pt

A low-angle, upward-looking shot of a modern skyscraper with a grid-like facade of windows and balconies. The image has a strong blue color cast. A white square frame is centered on the page, containing the title text.

Economic Overview

1. - ECONOMIC OVERVIEW

The Portuguese economy has been recovering at a very healthy pace after a 3-year recession period, between 2011 and 2013, during which the country was under an Economic Adjustment Programme agreed with the European Commission, the European Bank and the International Monetary Fund ("troika"), having exited in May 2013.

Portugal began to show signs of economic recovery at the end of 2013 and has been experiencing an annual gross domestic product (GDP) growth since 2014. Increase in household consumption, exports (especially in tourism) and, recently, investment (namely in the construction sector), are the main drivers. Tourism has been increasing successively over the past 8 years, with the number of overnight stays rising 7% y-o-y in 2017.

GDP is estimated to have grown 2.7% in 2017, according to Oxford Economics.

The labour market is likewise proceeding very positively. After reaching an all-time high of 17.4% in early 2013, the unemployment rate has since been decreasing, to around 9.2% in 2017.


Consumer Price Index (CPI) was below 1% between 2013 and 2016 (inclusively with deflation in 2014) but increased in the region of 1.4% in 2017.

Main confidence indicators have been improving since 2012 and in 2017 reached record highs levels.

After exceeding 16% in early 2012, and decreasing sharply from then onwards, the 10-year bond yield once again showed an upward trend in 2015 and 2016, rising above 4% at the beginning of 2017. However, the rate fell over the first six months of 2016, standing below 2% at the end of 2017. Simultaneously, and following a fiscal deficit of 2% of GDP in 2016, well below the 2.5% EU target, the European Commission, in May, recommend Portugal's exit from the Excessive Deficit Procedure. In addition, at the end of 2017 both Fitch and S&P raised Portugal's credit rating to investment grade.




2,7%
GDP



2,3%
Consumption



1,4%
CPI



9,2%
Unemployment

An aerial photograph of a city, likely Lisbon, Portugal, showing a dense urban landscape with numerous buildings featuring red-tiled roofs. In the background, a prominent clock tower (Torre do Relógio) is visible, and the city extends to the waterfront where a ship can be seen. The image is overlaid with a semi-transparent dark rectangle containing the title text.

Territorial Division & Demographics

2. - TERRITORIAL DIVISION & DEMOGRAPHICS

Portugal is made up of the mainland and the archipelagos of Madeira and Azores located in the Atlantic Ocean. Portuguese territory comprises 9.2 million ha and is administratively divided into 18 districts and the two autonomous regions of Madeira and Azores, which together integrate 308 councils. The councils are subdivided into parishes ("freguesias"). In 2013, after an administrative restructure the number of parishes has decreased, to the current 3,092.

Statistically Portugal is divided in 7 different regions: North, Centre, Lisbon, Alentejo and Algarve, in the mainland, as well as Madeira Autonomous Region and Azores Autonomous Region. These are then subdivided in 30 subregions.

According to the last census carried out in 2011, Portugal had 10.5 million inhabitants reflecting a 1.4% demographic growth in that decade. However, 2016 estimate point now to only 10.3 million inhabitants, a decrease that results mainly from emigration and the sharp decline in birth rate.

The Greater Lisbon sub-region concentrates circa one fifth of the Portuguese population with 2.8 million inhabitants, while 1.7 million people live in the Greater Porto sub-region. The most populated councils are Lisbon, Sintra and Vila Nova de Gaia.

9.2
million ha

7
regions

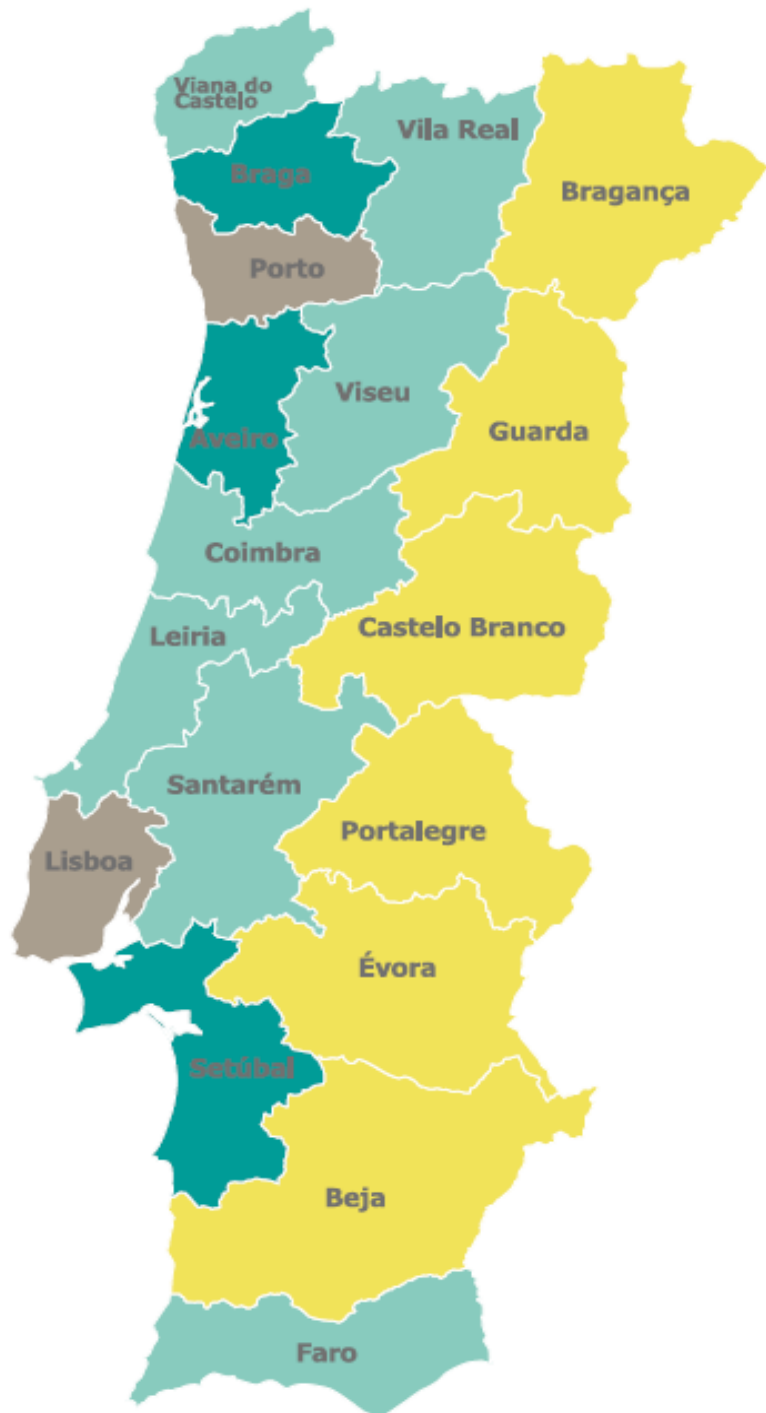
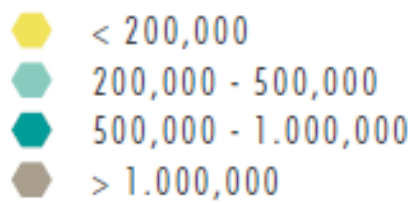
18
districts

308
councils



TERRITORIAL DIVISION & DEMOGRAPHICS

POPULATION
PER
DISTRICT



A photograph of a modern city skyline featuring several tall glass skyscrapers. The buildings have a grid-like facade of windows. In the foreground, there is a paved plaza with some trees and the silhouettes of people walking. The sky is a clear, deep blue. A white rectangular frame is centered over the image, containing the title text.

Investment Market Overview

3. - INVESTMENT MARKET OVERVIEW

The Real Estate Investment market has completely changed over the last decade, with regards to volume, type of investors, origin of the capital, and is currently at a new stage.

Up until 2002 institutional investment turnover in Portugal was low and limited to Portuguese funds and a reduced number of foreign investors. It was only after 2002, with the entry of the Euro, that the commercial property investment market became more dynamic with the arrival of several international players.

The strong growth at this stage was associated mainly to the renowned quality of Portuguese shopping centers that stimulated strong interest from foreign investors. Other factors that contributed to this growth were the reduction of IMT (property transfer tax) in 2004, from 10% to 6.5% making the acquisition of Portuguese assets more attractive, together with the change introduced in 2005, in the Property Investment Funds regulation, which meant that closed ended funds were then able to leverage without restrictions.

2007 registered a historic record high in investment activity in Portugal, fuelled by the easy access to credit from which investors benefited during that period.

The world economic crisis that was felt since 2008, became even more critical in Portugal with the acknowledgement of the Portuguese public debt crisis in 2010. Surprisingly, property investment volumes still increased in 2010, but this was driven by a couple of shopping centre transactions that could almost be considered as internal reorganization exercises.

In 2011 and 2012 the market suffered a severe contraction. It was only in the second half of 2013, with the risk of Portugal leaving the Eurozone set aside and the prospects for eventual economic growth, that the first signs of investment in the commercial property market appeared, with international players showing increasing interest.

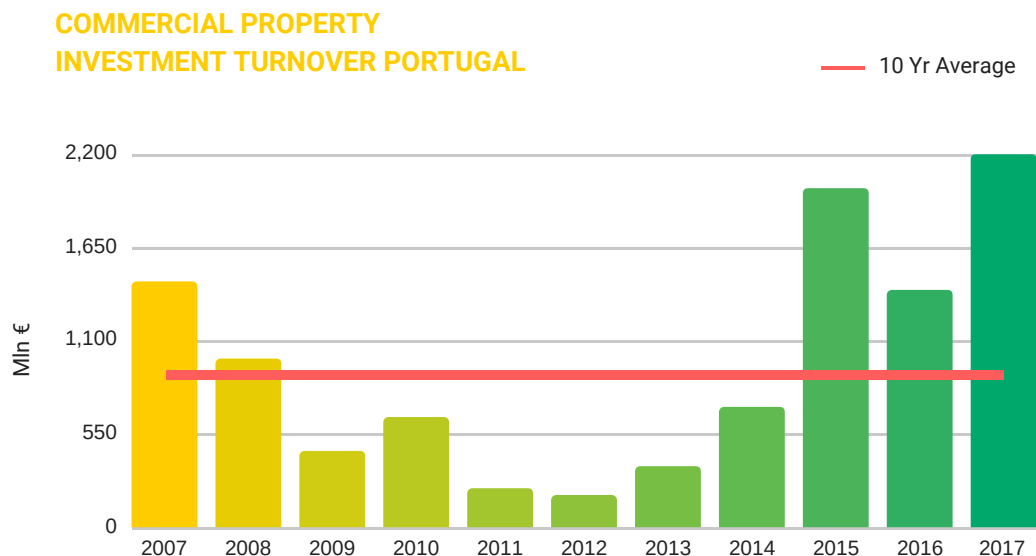
2014 was the year of investment recovery in Portugal and in 2015 a new historic record high of €2.1 billion euros was achieved.

INVESTMENT MARKET OVERVIEW

The 10-year average investment turnover (between 2008 and 2017) was €910 million (against €1 billion on the 2003 to 2007 previous peak). However, in 2017 investment once again surpassed the 2 billion Euros threshold achieving a new high of 2.2. The 2017 turnover was leveraged by the sale of two multinational companies with several assets in Portugal, Logisor and Empark, both purchased by international institutional investors, which represented 20% of the total investment volume.

In this 10-year period the retail sector recorded the highest share in investment volume, followed by offices, with 47% and 31% respectively of the total inflow. Portuguese shopping centres have attracted a considerable number of international investors, although in the last couple of years the investment in the office sector has exceeded that of retail. Despite representing a lower share in the total investment turnover over the past 10 years, with a quota of 12%, the logistics sector saw a very strong activity driven by the Logisor acquisitions. Furthermore, we have been observing over the last years an increasing interest in the hotel sector supported on the strong tourism growth and price increase.

The shape of investment origin and profile has changed significantly from the previous cycle of the market. While in 2007 more than a half of the acquisitions volume was driven by Portuguese investors (closed-end and open ended funds) and the United Kingdom was the more relevant foreign investment market; in 2015 capital inflow was dominated by the USA market. Investment origin has been much more diversified in 2016 and 2017 and new players are continuously entering the market. Nevertheless, while in 2015 and 2016 Portuguese investment has represented only 10% of total turnover, in 2017 this share has more than doubled to 22%.



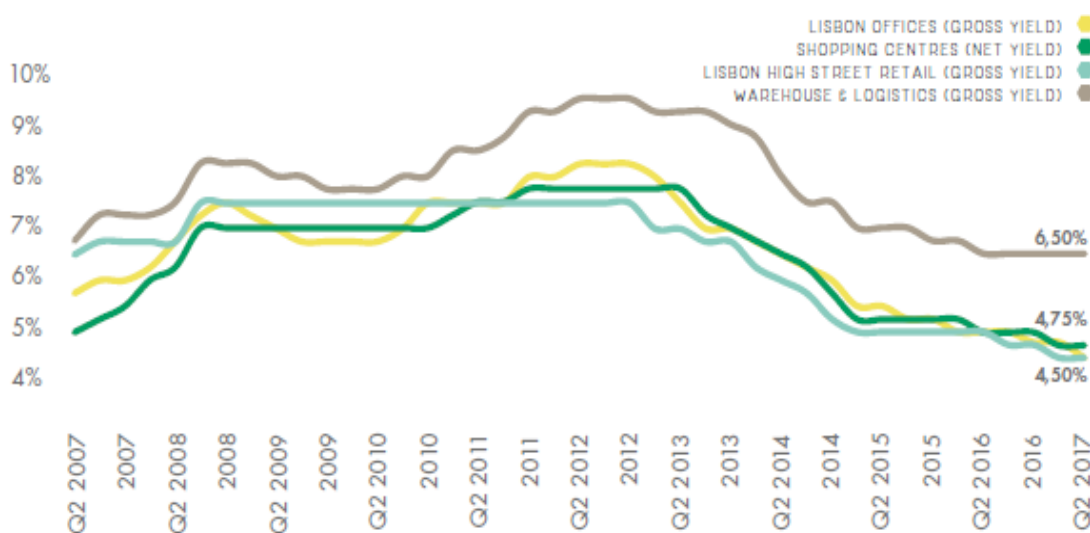
INVESTMENT MARKET OVERVIEW

Yields dropped consecutively since the beginning of the decade and up until 2007. The international financial crisis and, thereafter, the Portuguese public debt crisis, resulted in several increases in prime yields, which only began to compress in the second half of 2013. The prime yields are now lower than those of 2007 in all sectors, except in the retail park format: -25 basis points (b.p.) in prime shopping centres and logistics assets, -125 b.p. in the office sector and -200 b.p. in high street retail. This market was the most resilient to the crisis and has been showing strong dynamics driven by robust tourism growth and the renovation of several buildings in the city centre.

In recent years, investment in real estate in Portugal has not been limited to commercial property. Since 2014 we have witnessed a strong trend towards the acquisition of buildings for redevelopment in the Lisbon and Porto historic centres, from institutional foreign investors traditionally more risk adverse. Effectively, in a context of high liquidity and very low interest rates, property development, particularly that of residential renovation, emerged as a high return investment, in a moment where the commercial risk is mitigated with an increased number of sales off-plan.

An additional market trend has been the entry of small private investors in the residential sector, with the acquisition of units for lease, both in the short term rental market (tourism) or in the traditional residential market. In a general way, these small scale operations allow yields above 3.5%, providing an interesting upside when compared to the interest of traditional financial alternatives; the advantage of this type of investment is supported by an increasing rental growth.

EVOLUTION OF PRIME YIELD



Looking for Investment Opportunities in Portugal?

A man in a dark suit stands with his back to the camera on a balcony with a glass railing. He is looking out over a dense city skyline with many skyscrapers under a clear sky. The balcony floor is highly reflective, showing the man's reflection.

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or

Email us info@prima-carta.pt



Property Ownership & Taxes

4. - PROPERTY OWNERSHIP & TAXES

Full Ownership

“Full Ownership” (Direito de Propriedade) is the most common and the strongest form of ownership title over real estate in Portugal. The full owner of a property is entitled, within the limits of the law, to exclusive rights of use, fruition and disposal of the property, such ownership being unlimited in time (full ownership would be equivalent to a “freehold” in common law systems and to the French concept of “droit de propriété”).

A real estate property can be held individually or by more than one person or entity (co-owners), which is less common. Co-owners jointly exercise the rights deriving from the ownership title, and they participate proportionally (by reference to their quotas in the ownership) in the benefits and encumbrances of the property.

Surface Right

“Surface Right” (Direito de Superfície) entitles the respective titleholders to build or maintain a construction, perpetually or temporarily, on or below a land owned by a third party. It is a right in rem (and not only a contractual arrangement) that can be transferred and may also be used as collateral.

In case the Surface Right is granted on a temporary basis, the construction built over the land shall revert to the land owner upon expiration of the Surface Right. In such case, unless otherwise agreed, the surface right holder is entitled to receive a compensation corresponding to the value added to the land as a result of the construction.

The parties may agree that the remuneration due for the surface right is payable through a single payment or through periodic payments.

Condominium

The “Condominium Regime” (Propriedade Horizontal) allows the segregation of buildings (or groups of buildings that are functionally interconnected) into different and independent units, resulting in a condominium structure whereby each unit can be separately owned by a different individual or entity.

The condominium regime confers to unit owners a full ownership right over one or more units and a co-ownership right over the common areas of the building (such as the lobbies, hallways and stairs). Both rights are indivisible as they cannot be transferred separately.

PROPERTY OWNERSHIP & TAXES

A condominium is normally established by means of a notary deed and is registered with the Land Registry. A Condominium can only be set if the relevant units (frações autónomas) are independent and isolated from one another, and have separate exits to a common area of the building or directly to a public road.

Co-owners bear all costs emerging from the management, maintenance and works of the common areas by means of a contribution charged and collected by the condominium, determined on a proportional basis taking into account the weight of each unit in the building (each unit has a relative value expressed by a percentage or per mileage mandatorily determined in the condominium constitutional deed).

Whenever commercial lease agreements are entered into regarding a condominium unit, condominium costs may be transferred to the tenants.

Municipal Property Tax

Municipal Property Tax (known in Portugal as “IMI”), is a municipal tax which focuses on the ownership of a property located in Portuguese territory. Municipal Property Tax is due by the registered owner of the property as at December 31st, according with the Property Tax Value (known in Portugal as “VPT”).

The Property Tax Value is determined according to a formula foreseen in the Property Transfer Tax Code which takes into consideration the nature and characteristics of each type of property. Property Transfer Tax is applicable according to the following tax rates:

- Urban Properties: 0,3% to 0,45% (variable according to each municipality);
- Rural Properties: 0,8%;
- Properties owned by entities resident in blacklisted jurisdictions (as detailed on the Ministerial Order 150/2004, of 13 February, as amended): 7,5%.

Additional to Municipal Property Tax

Pursuant to the State Budget Law for 2017, a new tax, the Additional to Municipal Property Tax (known in Portugal as “AIMI”), was enacted and is effective as from January 2017 onwards. The new tax replaces the Stamp Duty (known in Portugal as “Imposto de Selo”), previously applicable to properties with a Property Tax Value greater than €1 Million.

PROPERTY OWNERSHIP & TAXES

Additional to Municipal Property Tax is levied only on urban properties for residential purposes and plots for construction located in Portugal. Urban properties classified for “trade, industry, or services” or as “other types of property” are excluded from Additional to Municipal Property Tax.

The taxable amount corresponds to the sum of the Property Tax Value of the urban properties and construction plots held by each taxpayer reported on January 1st of each year.

Deductions/Exemptions

In the case of individuals and undivided estates, a deduction of €600,000 is applied to the taxable amount, prior to the application of the Additional to Municipal Property Tax; Married taxpayers or taxpayers under a civil union (união de facto) are entitled to a deduction of €1.2 Million on the sum of the Property Tax Value of the properties owned; The Property Tax Value of the properties that are exempt of, or not subject to, Municipal Property Tax in the previous year is excluded from the taxable amount subject to Additional to Municipal Property Tax.

Applicable Tax Rates

- For corporations, the Additional to Municipal Property Tax rate is 0.4% of the taxable amount.
- For individuals the Additional to Municipal Property Tax rate is 0.7% of the taxable amount after the abovementioned deductions (€600,000 or €1,2 Million);
- For taxable amounts in excess of €1 million, the marginal rate is 1%;
- For properties owned by entities resident in a blacklisted jurisdiction (as detailed on the Ministerial Order 150/2004, of 13 February, as amended), the rate is 7.5%.

Recovery or Deductibility for Corporate Income Tax purposes

The Additional to Municipal Property Tax may be deducted in the computation of the Corporate Income Tax (known in Portugal as “IRC”). Taxpayers may elect either to deduct the Additional to Municipal Property Tax as a general deductible expenditure or as a specific deduction against the Corporate Income Tax due. In the latter case, the deduction is limited to the portion of the Corporate Income Tax directly linked with income generated from properties used for leasing or accommodation activities and insofar as such properties are subject to Additional to Municipal Property Tax.



Real Estate Transactions

5. - REAL ESTATE TRANSACTIONS

Asset Deals

The transfer of real estate assets in Portugal (asset deal), may be performed by means of (I) a public deed, or (II) a private document certified by a notary, a solicitor, a lawyer or a chamber of commerce and industry. The transfer of title must be registered with the Land Registry Office within 30 days as from the date of the transaction.

Land Registry Offices are the entities in charge of keeping public records reflecting the description of properties and their current status, including ownership and encumbrances. Land Registry is guided under the principle of the registry's priority.

Any foreign or non-resident investor is allowed to acquire a property, without any restrictions, although investors need to comply with certain tax formalities (including obtaining a Portuguese taxpayer number).

Prior to acquiring a real estate property, investors typically perform a due diligence review (both legal and technical).

The legal due diligence scope normally includes amongst other aspects, confirmation of title, verification of existing encumbrances, confirmation that there are no property taxes in debt, and confirmation of the existence of a valid municipal use permit (a valid use permit is a requirement for the use of the property and it is mandatory to allow the transfer of a real estate asset through an asset deal).

In asset deals, the parties usually enter into a promissory sale and purchase agreement that precedes the definitive agreement of conveyance of the property. Under the promissory sale and purchase agreement the parties undertake to acquire /sell a real estate property at a certain moment in the future, under certain agreed terms and conditions.

REAL ESTATE TRANSACTIONS

A promissory sale and purchase agreement may include conditions precedent that need to be fulfilled prior to the execution of the definitive sale and purchase agreement. Conditions precedent are usually foreseen when the property is affected by irregularities and /or licensing issues that must be settled by the seller in order to conclude the transaction.

Upon signature of the promissory sale and purchase agreement, the promissory purchaser usually pays to the promissory seller a down payment ranging between 10% and 25% of the purchase price.

Under Portuguese Law, unless otherwise agreed between the parties, a breach of the Promissory Sale and Purchase Agreement entails the following consequences:

- Vendor's breach: the promissory purchaser may claim twice the amount of the down payment;
- Purchaser's breach: the promissory vendor may keep the amount received as a down payment.

As an alternative to the above, in case of breach, the non-breaching party may, in certain circumstances, apply in court for the specific performance of the promissory purchase and sale agreement, with the purposes of obtaining a court decision that shall enforce the execution of the transaction.

After entering into a promissory sale and purchase agreement, the promissory purchaser is entitled to submit a provisional registration for the acquisition of the property. Under the principle of the registry's priority, such provisional registration may provide security towards subsequent liens and/or encumbrances that could possibly be registered against the property. Upon completion of the sale and purchase agreement, the provisional registration becomes definitive upon request filed by the purchaser.

Share Deals

Alternatively to asset deals, the acquisition of real estate properties in Portugal may be performed indirectly, by means of the acquisition of shares in the property holding company (share deal). The transfer of shares may be affected by means of a private agreement between the parties.

There are no restrictions to the acquisition of an interest in Portuguese Companies by foreign or non-resident investors, although the investors may have to comply with certain tax formalities, including obtaining a Portuguese taxpayer number.



REAL ESTATE TRANSACTIONS

In case of a share deal, in addition to a due diligence review of the property, the purchaser typically also conducts a due diligence to the company encompassing the customary aspects involved in the acquisition of companies (corporate status, financing status, tax aspects, debts, employment agreements, etc.).

The acquisition of shares in public limited liability companies (sociedades anónimas) must, in certain cases, be notified to the company (notably for the registration of the shares on behalf of the purchaser) and to public authorities (tax authorities and regulatory entities). The acquisition of a stake in a private limited liability company (sociedade por quotas), must be registered with the Portuguese Companies Registry.

optimus

20

Taxes on Real Estate Transaction

6. - TAXES ON REAL ESTATE TRANSACTION

Asset Deals

Property Transfer Tax ("IMT") and Stamp Duty (Imposto de Selo)

Property Transfer Tax is a municipal tax levied on the transfer of real estate located in the Portuguese territory. Property Transfer Tax is levied on the higher of (I) the declared acquisition value and (II) the Property Tax Value.

The applicable tax rates are as follows:

- Urban property used exclusively as primary residence: 6% (maximum progressive rate, according with the Property Tax Value¹);
- Rural property: 5%;
- Urban property not intended for residential purposes: 6.5%;
- Property purchased by entities resident in a blacklisted jurisdiction (as detailed on the Ministerial Order 150/2004, of 13 February, as amended): 10%.

In addition the acquisition of real estate is also subject to Stamp Duty at a rate of 0.8%. Stamp Duty is levied on the higher of (I) the declared acquisition value and (II) the Property Tax Value.

Notary and registration fees

Notary and registration fees are payable by the purchaser upon the execution of the public deed of transfer and the respective registration with the Land Registry. The value of these fees is normally negligible.

VAT

The transfer of property in Portugal is exempt of VAT. However, such exemption may be waived, provided that the purchaser uses the acquired real estate for activities subject to VAT and that give the right to deduct VAT.

If the transaction is subject to VAT, the standard rate (currently, 23%) will be applicable and levied on the purchase price. The VAT is self-assessed by the purchaser, meaning that it is assessed and deducted in the same periodical VAT return.

It is relevant to note that, if the property is later used for non-VAT taxable activities, the VAT initially deducted must be adjusted. This restriction binds the taxpayer for a 20-year period.

TAXES ON REAL ESTATE TRANSACTION

Share Deals

Property Transfer Tax (“IMT”) and Stamp Duty (Imposto de Selo)

Acquisition of properties by means of share deals are, as a general rule, not subject to Property Transfer Tax nor to Stamp Duty. As way of exception Property Transfer Tax is triggered by the acquisition of more than 75% of the share capital of a private limited liability company (sociedade por quotas), as well as of the units of a privately placed closed-end real estate investment fund (fundo de investimento imobiliário fechado de subscrição particular), which own real estate located in Portugal.

Notary and registration fees

No notary or registration fees are payable in a share deal, except in case of acquisition of an interest in a limited liability company (“sociedade por quotas”), where registration with the Portuguese Companies Registry is required and, consequently, the payment of the respective registration fees is due. The value of these fees is negligible.

In light of the above, an indirect acquisition of real estate, through the acquisition of the share capital of a limited liability company by shares (“sociedade anónima”) owning such real estate property, is normally considered the most efficient way to invest in the Portuguese market. Nonetheless, a final decision on the transaction structure should be taken on a case-by-case basis.





Financing

7. - FINANCING

Legal

Real estate investors typically finance their real estate projects through a mix of bank debt and own funds.

Third Party Financing is usually secured against property (through a mortgage) and/or the shares of the company owning the property and/or property generated income.

A mortgage is an in rem guarantee that grants the creditor, in the event of default of the secured obligation, the right to be paid, with preference over the borrower's non-secured creditors, from the proceeds of the sale of real estate properties (provided other creditors do not benefit from special privileges, which would be the case, for instance, of the tax authorities with regard to property taxes). Mortgages are the most common security provided in real estate acquisitions in Portugal.

Mortgages are created by means of a notarial deed executed before a notary, or in a private document signed before, and certified by, a lawyer, solicitor or chamber of commerce and industry. The notarial deed must set forth the maximum amount secured. The mortgage may also secure interests of up to three years and also a certain amount for recovery expenses.

Mortgages follow the changes affecting the asset thus, and without prejudice to the rights of third parties, a mortgage shall be automatically extended to all improvements and constructions carried out on the secured real estate property.

Mortgages must be registered with the Land Registry as a condition for being valid and enforceable. Typically mortgages are enforced by means of a judicial process in the course of which the property is sold and the creditor is paid with the proceeds of the sale. Alternatively, depending on the legal procedure, the creditor may in certain circumstances apply for the award of the asset as payment in kind.

Pledges over shares and pledges over receivables (rents, deposits, indemnities, etc.) are commonly used in Portugal.

FINANCING

Taxes

Stamp Duty (Imposto de Selo)

Generally, both loans and guarantees are subject to Stamp Duty, at a variable rate depending on the maturity of the loan and/or guarantee, as follows:

- Loans – 0.04% (monthly), 0.5% or 0.6% applicable on credit granted for less than one year, one year or more, or five years or more, respectively;
- Credit used in the form of a current account, bank overdraft or any other form in which the term of use is not determined or determinable, on the monthly average obtained by summing up the outstanding amounts, calculated on a daily basis, during the month divided by 30 – 0.04 %;
- Interest paid to financial institutions – 4%;
- Any fees or commissions paid for financial services – 4% (except for commissions for guarantees provided, applying a rate of 3%).

At the level of Stamp Duty, some exemptions are available:

Shareholder loans – loans granted by the direct shareholder of the borrower for a minimum term of 1 year may benefit from a Stamp Duty exemption, (I) provided that the shareholder directly holds a minimum participation in the capital of the borrower of 10% and (II) provided that this holding is kept for a minimum period of one year prior to the execution of the shareholder loan. If the borrower was incorporated by the lender, the one year holding period may be complied with after the granting of the loan;

Short-term (up to one year) loans granted to cover treasury needs by a holding company to its subsidiary or viceversa or by a parent company to its subsidiary (where a minimum 10% stake is held uninterruptedly for at least one year);

Guarantees that are ancillary to the financing transaction (granting of loans) are exempt from Stamp Duty, provided that the guarantee is granted simultaneously with the secured loan, even if in a different instrument or title.

FINANCING

Withholding Tax

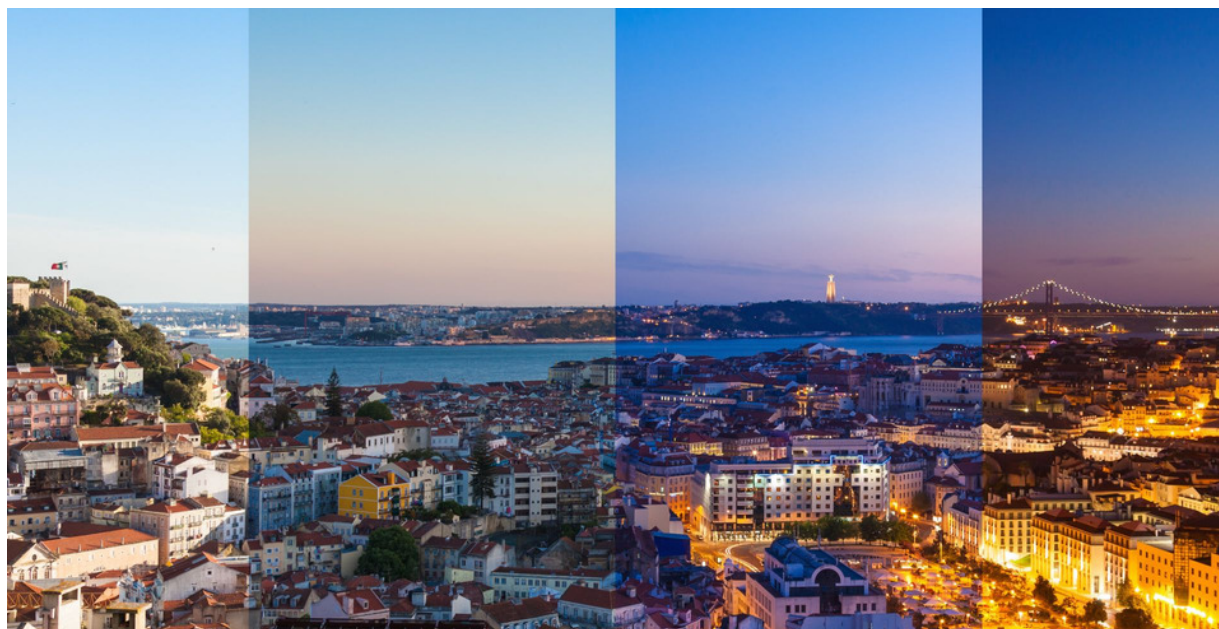
A withholding tax of 25% applies on interest paid by a Portuguese entity to a non-resident lender (other than a nonresident financial institution). The withholding tax may be reduced or fully eliminated pursuant to a double tax treaty, provided certain conditions are complied with.

In addition, no withholding tax is applicable under the Interest and Royalties Directive, if the lender is able to claim the benefits of the directive. The withholding tax exemption applies provided that the lender has a direct holding of at least 25% of the share capital or voting rights of the borrower for at least two consecutive years, or vice-versa. The withholding tax exemption also applies if both the borrower and the lender are directly held by a common shareholder holding at least 25% of the share capital or voting rights of each company, for a minimum period of two consecutive years.

Limits on The Deductibility of Net Financing Expenses

Portugal does not have thin capitalization rules. However, the Corporate Income Tax Code foresees an interest barrier rule, which sets the limits for the deductibility of net financing expenses. In 2018, the net financing expenses are deductible up to the greater of the following limits:

- €1 Million or
- 30% of EBITDA (Earnings before Interest, Taxes, Depreciations and Amortizations, with some tax adjustments).





Planning & Licensing

8. - PLANNING & LICENSING

Planning

In Portugal, the building code of each Municipality is specified in the town and country planning instruments, notably, the general plan (Plano Director Municipal), the master plans (Planos de Urbanização) and the (more detailed) detail plans (Planos de Pormenor).

The development of a real estate property may entail several types of urbanistic operations, which must always abide by the applicable town and country planning instruments, including but not limited to (I) plotting (“loteamento”), (II) infrastructure works (“obras de urbanização”) and (III) construction works (“obras de construção”), each of these operations requiring the respective administrative approval (being that plotting and infrastructure works are normally encompassed within the same procedure).

Licensing

The administrative approval of the urbanistic operations referred above, may follow several approval procedures as detailed below.

1) PIP

Prior to filing a licensing request, it is possible, although not mandatory, to file a previous information request (“PIP”) in order to obtain further certitude regarding the feasibility of the intended project.

A PIP consists of a request addressed to the competent Municipality, asking for the same to pronounce on the possibility of executing a certain project under the applicable town and country planning instruments.

When a Municipality issues a favourable decision, the PIP becomes binding to the Municipality, to the extent that, if a licensing abiding by the exact same terms under which the PIP was approved is filed within one year counted as of the approval of the PIP, the Municipality is bound to approve it. The Municipality may also extend the PIP for an additional period of one year, upon request.

According to the law, the conclusion of a PIP procedure should take 40 to 50 days (including the consultation of External Entities). However, in practical terms and according to our experience, said conclusion may take 3 to 6 months (or more, depending on the complexity of the project and depending on the Municipality in question). In any case, deadlines may vary from Municipality to Municipality and, therefore, confirmation of each Municipalities practice is recommended.

PLANNING & LICENSING

2) Construction License & Previous Communication

The applicable law currently foresees two types of administrative procedure entitling the execution of urbanistic operations (including: plotting and infra-structuring, construction of new buildings and modification of existing buildings):

License - is the standard procedure applicable whenever the law does not establish specifically that the operation in question may be exempted of such procedure or subject to the mere Previous Communication.

Previous Communication - consists of a mere prior communication to the Municipality before initiating the urbanistic operation

The specific situations where a Previous Communication is admissible by law, are situations in respect of which the degree of control by the Municipality may be lower.

Notably, the Previous Communication is allowed in situations where the parameters and requisites applicable to the urbanistic operation were previously established and approved by the Municipality with a high degree of detail (e.g. infrastructing or construction in areas covered by a plotting approval or by a detail plan, works in consolidated urban areas compliant with the Municipal plans and that do not exceed certain limits, or works complying with the exact terms of a PIP that has been approved).

The Previous Communication is filled with declarations signed by the architects and technicians responsible for the technical projects attesting that the urbanistic operation fully complies with the applicable rules, such declaration implying personal liability from the signatories.

Although the Previous Communication is foreseen in law as a mere communication upon which the developer may almost immediately start the works, the practice is often different because upon submitting the Previous Communication, Municipalities may require additional information to validate the admissibility of the Previous Communication or review the projects and make enquiries, which in practice may imply additional delay, rather than being immediate. Therefore, confirmation of each Municipalities practice is recommended.

PLANNING & LICENSING

Municipal Use Permit

In Portugal, the use of any real estate asset is generally subject to obtaining a Municipal Use Permit, which is the document attesting that a certain construction was built in accordance with the approved construction license and stating the respective authorized use.

The existence of an appropriate valid Municipal Use Permit in respect of each property is also a requirement for the execution of any agreements implying the transfer of any such properties (asset deal).

The need for Municipal Use Permit is exempted for constructions built before Decree-Law no. 38 382, dated of 7 August, 1951, came into force in the respective Municipality.

The Municipal Use Permit attests that a certain construction was built in accordance with the approved construction license and states the respective authorized use.





Renovation Regime

RENOVATION REGIME

LEGAL

Urban renovation regime

Aiming to simplify and stimulate urban renovation, Law no. 32/2012, dated of August 14, has changed the legal frame applicable to urban renovation, notably (a) allowing more flexibility in the procedures for the creation of urban renovation areas; (b) creating simplified procedures for the approval of urban renovation projects and (c) creating the concept of “individual urban renovation projects”, applicable to projects that may be located outside of urban renovation areas for construction built more than 30 years ago.

This simplification of procedures provided a significant contribution to urban renovation, which became more reliant on the initiative of private developers and less dependent on the initiative of the municipalities and other public entities.

Within the creation and simplification of procedures for the approval of urban renovation projects, a simplified licensing procedure, based on a swift Previous Communication (comunicação prévia) may be appointed as one of the most decisive changes enacted by the referred law.

This simplified procedure may be applicable, on the one hand, to projects located in urban renovation areas in accordance with approved urban renovation detail plans and, on the other hand, to the new concept of “individual urban renovation projects”.

Works on Leased Properties

Under the same legislative initiative, the Portuguese Government also enacted Law no. 30/2012, dated August 14, 2012, amending the legal framework for the execution of works in leased properties, focused on simplifying the execution of construction works by landlords on leased buildings, based on simpler and easier requirements for the termination of old lease agreements.

This regime was recently subject to new amendments, approved by Law no. 43/2017, dated of June 14, which introduced some additional requisites that limit substantially the possibilities whereby landlords may terminate old lease agreements for conducting renovation works.

RENOVATION REGIME

TAX

Tax Incentives

The Portuguese tax system has a wide range of benefits applicable to urban renovation, as follows:

In terms of VAT, the urban renovation construction contracts are subject to a reduced rate of 6%

The renovation of immovable property directly contracted with the National Fund for Urban Renovation (“Fundo Nacional de Reabilitação do Edificado”) by its management company is also subject to the reduced rate of 6%

In terms of Municipal Property Tax there are two applicable exemptions:

- Exemption for buildings or units (in buildings) built more than 30 years ago;
- Exemption for buildings or units (in buildings) located in urban renovation areas.

For the application of this type of exemptions, the following cumulative requirements must be met: (i) the buildings or units are subject to renovation according to the concept of “renovation of buildings” provided for in the Urban Renovation Legal Regime (“Regime Jurídico da Reabilitação Urbana”); and (ii) as a consequence of this intervention, the conservation status goes up two levels in relation to the conservation status before the renovation, with a minimum level of “good” (certified by the Municipality) and complies with applicable energy efficiency and thermal quality requirements.

The above exemptions are valid for a period of three years; counting from the year the renovation works were completed, which may be renewed upon request, for an additional five years period (only in the case of properties used for personal and permanent residence or residential long term lease).

At the Property Transfer Tax level there are also exemptions for urban renovation, in the same periods referred to Municipal Property Tax:

- Exemption for the purchase of property to be renovated, provided that the purchaser starts the renovation work within three years from its purchase;
- Exemption applicable to the first acquisition of the property after the conclusion of the renovation works, provided the acquirer is an individual that will use the property for personal and permanent residence, when located in an urban renovation area.

For the application of these exemptions, the cumulative requirements concerning Municipal Property Tax must also be verified.

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Foreign Investment

10. - FOREIGN INVESTMENT

DIRECT INVESTMENT

Portuguese government has enacted several legal and political programs in order to attract foreign investment and, as formerly referred there are no restrictions to foreign direct investment in real estate in Portugal.

Holding title over real estate properties should not directly imply the existence of a permanent establishment in Portugal for tax purposes. Nevertheless, investors must fulfill a few formalities, including, but not limited to, obtaining a Portuguese taxpayer number and investors with tax residence in a non-EU country must appoint a Portuguese legal representative (either individual or legal entity) to act on behalf of the investor before the Portuguese tax authorities.

Lease Income

Income derived by foreign investors from the leasing of properties located in Portugal is subject to Corporate Income Tax (known in Portugal as “IRC”), at a rate of 25%, except if the investor has a permanent establishment located in Portugal to which the rental income is attributable. The Corporate Income Tax may need to be withheld by the tenant provided the latter is a corporate entity or an individual subject to organized accounting rules.

For the computation of the taxable income, foreign investors have a very limited ability to deduct costs incurred. Maintenance costs, Municipal Property Tax and Stamp Duty are generally deductible, but there is no deductibility of financial expenditure, nor depreciation charges.

Capital Gains

Capital gains realized by a foreign investor on the sale of properties located in Portugal are subject to Corporate Income Tax at a rate of 25%.

For Corporate Income Tax purposes, taxable capital gains correspond to the difference between the sale price and the acquisition cost. The acquisition cost is updated pursuant to the specific rates foreseen in the tax legislation. Moreover, certain costs incurred by the property owner may also be added to the acquisition cost, such as the costs incurred with construction works performed on the previous five years and the costs necessary for the acquisition and/or sale of the property.

According to the State Budget for 2018, capital gains shall be liable to taxation in Portugal, whenever they result from the transfer of share capital or similar rights in any entity (non-resident in Portuguese territory), when at any time during the 365 days preceding the alienation, the securities derived more than 50 per cent of their value directly or indirectly from immovable property located in the Portuguese territory.

At this level, capital gains will not be liable to taxation when related to agricultural, industrial and commercial activity, except for the sale and purchase of immovable property.

FOREIGN INVESTMENT

INVESTMENT THROUGH A PORTUGUESE COMPANY

Foreign investors also structure their investments in Portuguese real estate by acquiring a Portuguese company (e.g. a special purpose vehicle, or “SPV”) that owns the target real estate asset(s), or by incorporating an SPV (to acquire the target real estate asset(s)).

In addition to the different transactional tax costs of the alternatives of acquiring the asset directly (asset deal) or through an indirect acquisition (share deal), as outlined above, the tax treatment applicable to a Portuguese resident entity owning real estate should be noted, as follows:

Lease Income

Lease income generated by a Portuguese company forms part of the taxable profits and is subject to Corporate Income Tax at a rate of 21%.

In addition to the Corporate Income Tax, there is also a municipal surtax ranging between 0% and 1.5% on the annual taxable profit (applicable before tax loss deduction).

Moreover, for taxable profits exceeding certain values, there is still a state surcharge:

- 3% for taxable profits exceeding €1,500,000 and up to €7,500,000;
- 5% for taxable profits exceeding €7,500,000 up to €35,000,000;
- 9% for taxable profits exceeding €35,000,000, according to the recent amendment promoted by the State Budget for 2018 (previously the applicable rate was 7%).

All expenses relating to the lease activity – i.e. not only maintenance and repair expenses and Municipal Property Tax, but also depreciation charges plus financial costs – are generally tax deductible with certain limitations (please refer to “real estate financing” section).

Portuguese permanent establishments and companies are entitled to certain tax credits, and to carry forward tax losses (currently through a period of 5 years, but limited to 70% of the annual taxable profits for losses originated).

According to the State Budget for 2018, it is expressly foreseen that there cannot be any kind of deductions to the total amount of autonomous taxation, even if those deductions are foreseen in special legislation. Autonomous taxation applies at different rates on certain expenses incurred by entities subject to Corporate Income Tax. It is self-assessed in addition to Corporate Income Tax (even if no Corporate Income Tax is due), at variable rates.

FOREIGN INVESTMENT

Capital Gains

Capital gains realized upon the sale of property by a Portuguese resident company are subject to Corporate Income Tax at a rate of 21% (plus the aforementioned surtaxes, where applicable).

Upon the sale of the Portuguese SPV, capital gains realized by the non-resident investor (shareholder) are subject to income tax (Personal Income Tax or Corporate Income Tax depending on the investor being a natural or legal person). Such capital gains will be subject to Corporate Income Tax at a rate of 25% (or to Personal Income Tax at a rate of 28%). The taxation of the capital gains may be eliminated pursuant to a domestic exemption foreseen in the Tax Benefits Code or pursuant to a double tax treaty, subject to certain conditions and formalities. However, provided that more than 50% of the Portuguese SPV's assets are real estate properties located in Portugal, the domestic exemption and the majority of the double tax treaties executed by Portugal foresee that the capital gains remain taxable in Portugal.

Dividends

Dividends distributed by a Portuguese SPV to the respective shareholder(s) are generally subject to income tax. Nonetheless, pursuant to the "participation exemption" regime, a Corporate Income Tax exemption is granted provided certain requirements are complied with. The main requirements are the following:

- a) The recipient of the dividend distributions holds at least 10% of the share capital or voting rights over the Portuguese SPV;
- b) The said shareholding was held for at least 1 year prior to the dividend distribution;
- c) The shareholder is a company resident in Portugal, in another EU or EEA member state, or a third country with a double tax treaty in force with Portugal and is subject to Corporate Income Tax at a rate higher than 60% of the Portuguese Corporate Income Tax rate (i.e. 12.6%).

A photograph of the Golden Gate Bridge in San Francisco, viewed from a high vantage point on a hill. The bridge's red towers and suspension cables are prominent against a hazy, blue-tinted sky and water. The city skyline is visible in the background. A white rectangular frame is superimposed over the center of the image, containing the text "Golden Visa".

Golden Visa

11. - GOLDEN VISA

TEMPORARY RESIDENCE PERMIT

The Golden Visa Program corresponds to a special legal regime that allows third-country nationals that intend to invest in Portugal to apply for a temporary residence permit ("Temporary Residence Permit for Investment" or "ARI"). In case the investment performed by third-country nationals fulfills the minimum requirements set forth under applicable law and the temporary permit is granted, investors may:

- freely travel within Schengen Area;
- apply for family reunification;
- live and work in Portugal;
- obtain permanent residence (after 5 years and in the terms and conditions set out by the legislation in force);
- acquire Portuguese citizenship (after 6 years and in the terms and conditions set out by the legislation in force).

Any third-country nationals can apply for Golden Visa, provided they are holders of a valid Schengen Visa (or being exempt from it) or legalize their permanence in Portugal within 90 days as of their first entry into national territory.

The Golden Visa's application shall be subject to the analysis and approval of the Regional Directorate and Regional Delegations of the Immigration and Borders Service ("SEF") in Portugal.

The minimum quantitative requirement is deemed fulfilled if one of the following conditions is met:

- capital transfer with a value equal to or above 1 million Euros;
- the creation of at least 10 jobs;
- the purchase of real estate property for a value equal or above 500 thousand Euros;
- the purchase of real estate property regarding buildings older than 30 years or located in urban renovation areas, destined to renovation, for a total value equal to or above 350 thousand Euros;
- capital transfer with a value equal to or above 350 thousand Euros for investing in research activities conducted by public or private scientific research institutions involved in the national scientific or technologic system;
- capital transfer with a value equal to or above 250 thousand Euros for investing in artistic output or supporting the arts, for reconstruction or renovation of the national heritage;
- capital transfer with a value equal to or above 500 thousand Euros, for purchasing shares in investment funds or in venture capital geared to capitalize small and medium companies;
- capital transfer of the amount of 350 thousand Euros, or higher, for constitution of a commercial society with head office in the national territory, combined with the creation of five permanent working jobs, or for the reinforcement of the share capital of a commercial society with head office in national territory, already existing, with the creation or keeping of working jobs, with a minimum of five permanent jobs, and for a minimum period of three years.

GOLDEN VISA

The real estate property acquired for Golden Visa purposes can be leased for commercial, agricultural or tourism purposes and can be acquired in co-ownership. The acquisition can be made directly by an individual or by a company based in Portugal or in another EU country with a permanent establishment in Portugal (as long as the investor shows evidence attesting he is the unique shareholder of the company). It is also possible to apply for the Golden Visa before the acquisition deed, if the applicant has entered into a promissory sale and purchase agreement and delivered to the promissory seller a deposit equal or higher than the minimum quantitative requirement as down payment.

The Golden Visa investor must stay in Portugal for a period of, at least, 7 days during the first year, and 14 or more days, in the subsequent 2 year periods.

The application for the Golden Visa implies the payment of an initial fee of 520.40 Euros and a permit issuance fee of 5,202.60 Euros. Later on, a renewal fee of 2,601.30 Euros will also be due per renewal. The Golden Visa is valid for 1 year and renewable for 2 year periods.

PERMANENT RESIDENCE PERMIT

In order to apply for a permanent residence permit, applicants must hold a temporary residence permit in Portugal (including Golden Visa) for at least 5 years.

The granting of the permanent residence permit is subject to certain requirements, notably the applicant shall: (I) have not been convicted in Portugal during the last 5 years for a crime punishable with deprivation of liberty exceeding 1 year, (II) have financial resources to live in Portugal, (III) have a place to live in Portugal and (IV) show evidence of basic Portuguese language commands (to be proven through a written test).

PORTUGUESE CITIZENSHIP

In order to apply for Portuguese citizenship applicants must legally live in Portugal for at least 6 years.

The granting of Portuguese citizenship is subject to certain requirements, notably the applicant shall (I) be of legal age under the Portuguese law (parents may also apply for the citizenship of their children in certain conditions), (II) have not been convicted in Portugal for a crime punishable with deprivation of liberty exceeding 3 years, (III) show evidence of sufficient knowledge of Portuguese language (to be proven through a written test) and (IV) have a link with Portugal and with the Portuguese culture (to be ascertained by the immigration authorities on a case by case basis).

12. - CONTACTS

Prima Carta is an independent specialized Portuguese boutique house, founded to provide full support to real estate investors in Portugal.

In close cooperation with our partners of the highest level of competence, we provide a full range of services related to the acquisition, due-dilligence, financing and ownership of commercial real estate in Portugal.

Prima Carta works with private and institutional investors, who targets investments in stand-alone food retail, street retail, office building, logistics & industrial complexes, commercial real estate projects at construction stages, residential development and land plots, in Portugal

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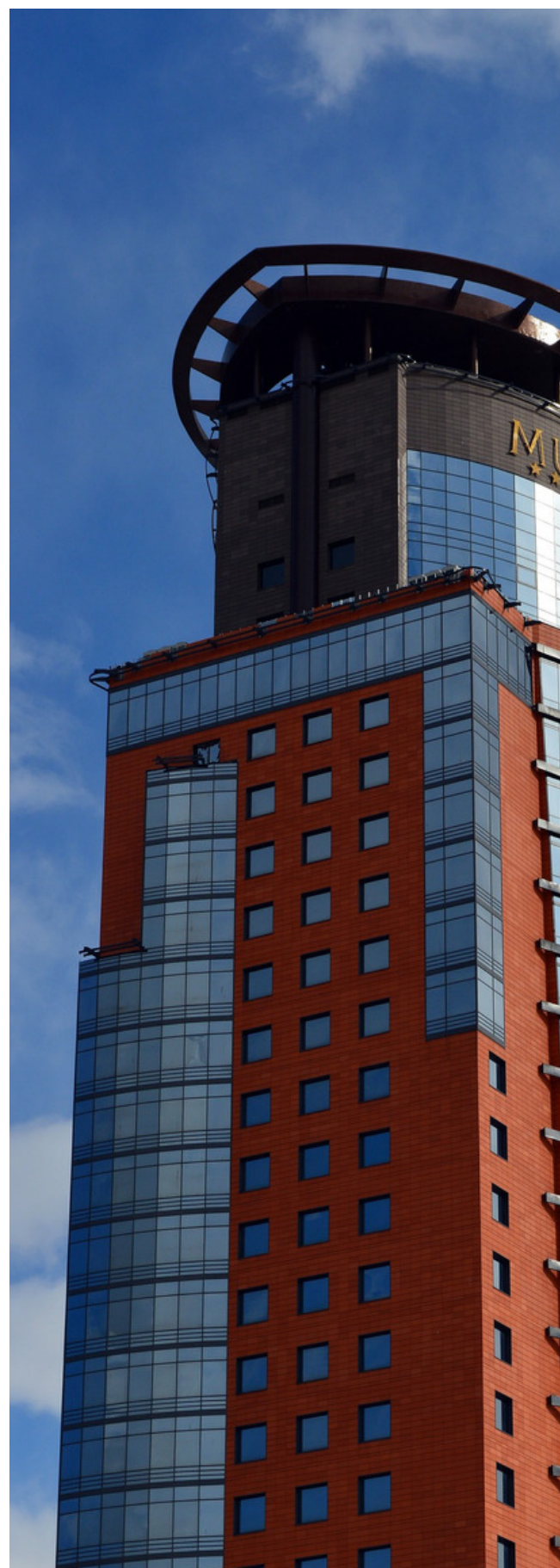
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