DLA PIPER

EVERYTHING MATTERS

Structures for Brazilian Investment in U.S. Real Estate

Overview

- Non-resident/non-citizen of the U.S. ("Nonresident Alien" or "NRA") looking to expand in the U.S. through acquisitions of real estate need to consider the following:
  - Choice of Investment Entity.
  - U.S. Income Tax.
  - U.S. Withholding Tax.
  - U.S. Estate and Gift Tax.

Choice of Investment Entity

- U.S. investments in real estate may be held through:
  - Corporate structures.
  - Non-corporate structures:
    - Direct individual ownership.
    - Trust.
    - Partnership (including limited liability companies).
    - Real estate investment trust (“REIT”).

Income Tax Implications - Corporations

- U.S. corporations are subject to a 35% tax at the corporate level and an *additional* tax to the shareholder when distributed.
  - Tax to shareholder ranges from 0% to 39.6%, depending on the shareholder's status.
- Non-U.S. corporations engaged in U.S. business directly (i.e., through a "branch" in the U.S.) are subject to a 35% tax at the corporate level on their income that is "effectively connected" with the conduct of a trade or business within the U.S. ("ECI") and an *additional* "dividend equivalence tax."
  - Dividend equivalence tax is imposed at 30% when a non-U.S. corporation fails to reinvest in its U.S. business; i.e., its U.S. earnings are withdrawn from its U.S. business.

Income Tax Implications – Individual

- NRAs engaged in a U.S. business are subject to a rate up to 39.6% on ECI.
- Gain on sale of U.S. real estate is taxed at lower 20% capital gains rate if property is non-inventory.
- Gain on sale of U.S. real estate is still taxed at rate up to 39.6% if inventory property (e.g., condo units).

Income Tax Implications – Trusts

- U.S. trusts are subject to a rate up to 39.6% on worldwide income.*
- Non-U.S. trusts engaged in a U.S. business are subject to a rate up to 39.6% on ECI.
- Trusts receive a deduction for distributions of income to beneficiaries.
  - Distributions of income to beneficiaries are taxed to beneficiaries.
- Gain on sale of U.S. real estate is taxed at lower 20% capital gains rate if property is non-inventory.
- Gain on sale of U.S. real estate is still taxed at rate up to 39.6% if inventory property (e.g., condo units).

* Beginning in 2013, certain investment income earned by U.S. individuals and U.S. trusts will be subject to an additional 3.8% surtax

Income Tax Implications – Partnerships

- Partnerships are not subject to U.S. income tax.
- The partnerships items of income, gain, loss, deduction, and/or credit ("tax items") are allocated its owners and taken into account in the computation of the owners' U.S. income tax; i.e., the partnership's owners pay tax on the partnership's income.

Income Tax Implications – REITs

- Generally, a REIT will be treated as a conduit and its earnings will "pass through" and only be taxed at the shareholder level; the REIT is permitted to deduct dividends it pays when calculating its taxable income.
- REIT is required to distribute cash (or possibly issue dilutive stock) to comply with annual REIT distribution requirements.
- A REIT can designate a distribution as a "capital gain dividend", permitting preferential capital gain treatment.
- A REIT must be beneficially owned by 100 or more persons.
- The taxation of a REIT will depend upon whether the REIT is "domestically controlled."
  - A REIT is domestically controlled if, at all times during a 5 year period, less than 50% in value of the REIT's outstanding stock is held, directly or indirectly, by non-U.S. persons. A sale of stock by a non-U.S. person in a domestically controlled REIT will generally <u>not</u> be subject to U.S. tax.
  - If the REIT is not domestically controlled, it is treated in the same manner as other U.S. corporations with non-U.S. persons.

U.S. Withholding Taxes

- Non-U.S. persons (including individuals, trusts, partnerships, and corporations) are subject to a withholding tax of 30% with respect to income that is not ECI received from U.S. persons (including individuals, trusts, partnerships, and corporations).
  - This income generally includes dividends, interest, royalties, rent, and annuity payments.
- Non-U.S. owners of a U.S. partnership are subject to a withholding tax up to 39.6% with respect to their share of the partnership's business profits.
  - May be reduced to lower 20% capital gains rate for individuals and trusts.
- Non-U.S. persons selling U.S. real estate are subject to a withholding tax of 10% of the sales price.
  - This withholding may sometimes be reduced through proper IRS filings.
- U.S. withholding taxes allowed as a credit against U.S. income taxes.

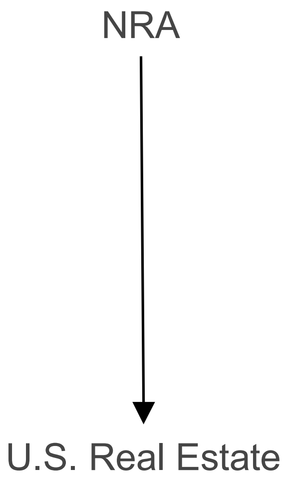
U.S. Estate and Gift Tax

- U.S. “situs” assets are subject to estate tax at rate of 40%.
  - After $60,000 estate tax exemption.
- U.S. “situs” assets include:
  - Real estate owned directly.
  - Stock in U.S. corporate issuers owned directly.
  - Debt of U.S. obligors (except “portfolio debt”).
- Non-U.S. situs assets include:
  - Non-U.S. real estate.
  - Non-U.S. corporate shares.
  - Tangible property located outside of U.S.
  - Bank deposits (including those located in the U.S.).
  - Portfolio debt instruments issued by U.S. persons.
  - Intangible personal property the written evidence of which is not treated as being the property itself, if it is not issued by or enforceable against a resident of the U.S. or a domestic corporation or governmental unit.

Investment Structures - Overview

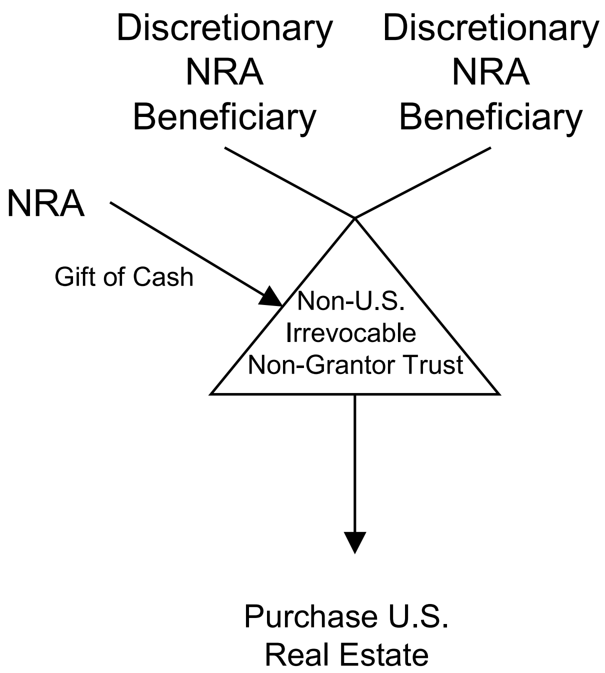
- Direct Ownership.
- Ownership Through Foreign Trust.
- Ownership Through Corporate Structure.
- Ownership Through Partnership Structure.
- Ownership Through Blended Structure.

Direct Ownership



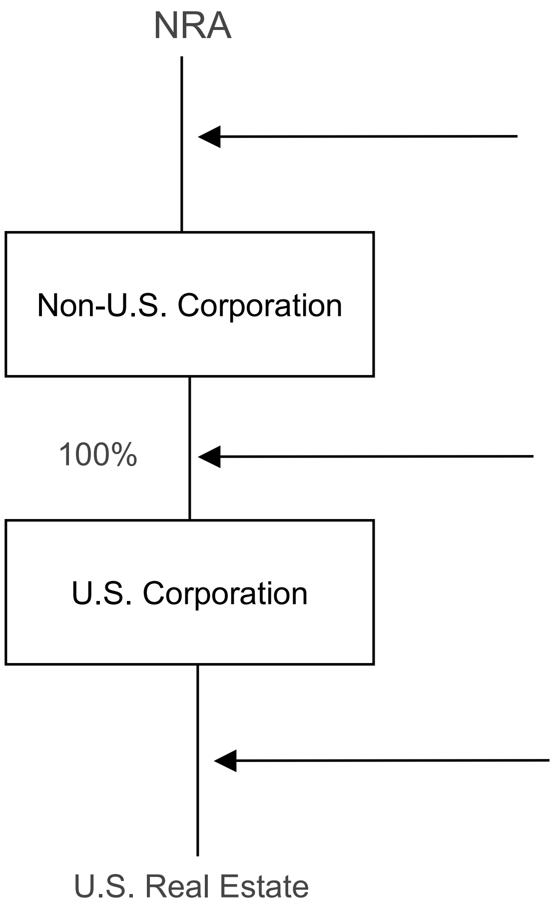
- Consequences:
  - 30% U.S. withholding tax on gross rental income from U.S. real estate.
    - May be reduced to 39.6% income tax on <u>net</u> income from U.S. real estate if proper election made.
  - 20% U.S. income tax on capital gains.
    - Tax collected through U.S. withholding tax.
  - 40% U.S. estate tax or U.S. gift tax on transfer.
  - No anonymity.
  - Must file Form 1040NR upon disposition (or earlier if used in USTB).
  - FIRPTA withholding.
  - Consider life insurance as a hedge.

Ownership Through Foreign Trust



- Consequences:
  - No U.S. gift tax on gift of cash to trust.
  - 30% U.S. withholding tax on gross rental income from U.S. real estate.
    - May be reduced to 39.6% income tax on net income from U.S. real estate if proper election made.
  - 20% U.S. income tax on capital gains.
    - Tax collected through U.S. withholding tax.
  - 0% U.S. estate tax or U.S. gift tax on death of beneficiaries.

Ownership Through Tiered Corporate Structure



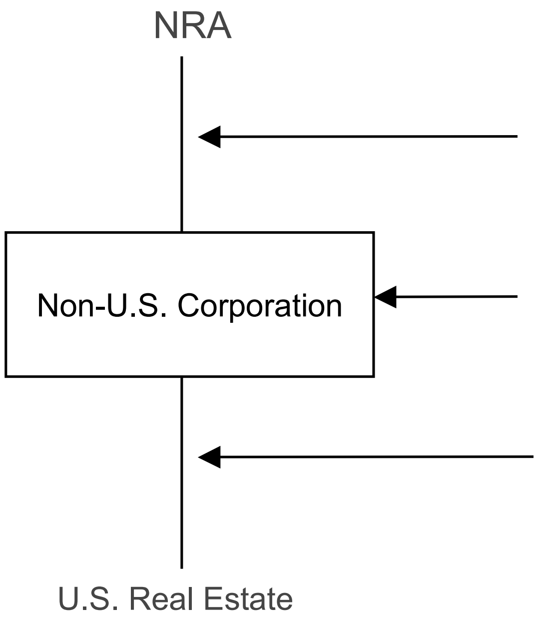
Consequences:

U.S. Estate & Gift Tax:
No estate or gift tax on transfer of Non-U.S. Corporation.
Anonymity.

U.S. Withholding Tax:
30% on dividend & interest distributions.
Sale of U.S. Corporation subject to tax if > than 50% of assets are U.S. Real Estate.

U.S. Corporate Income Tax:
35% tax on net income.
No capital gain preference.

Ownership Through Single Corporate Structure



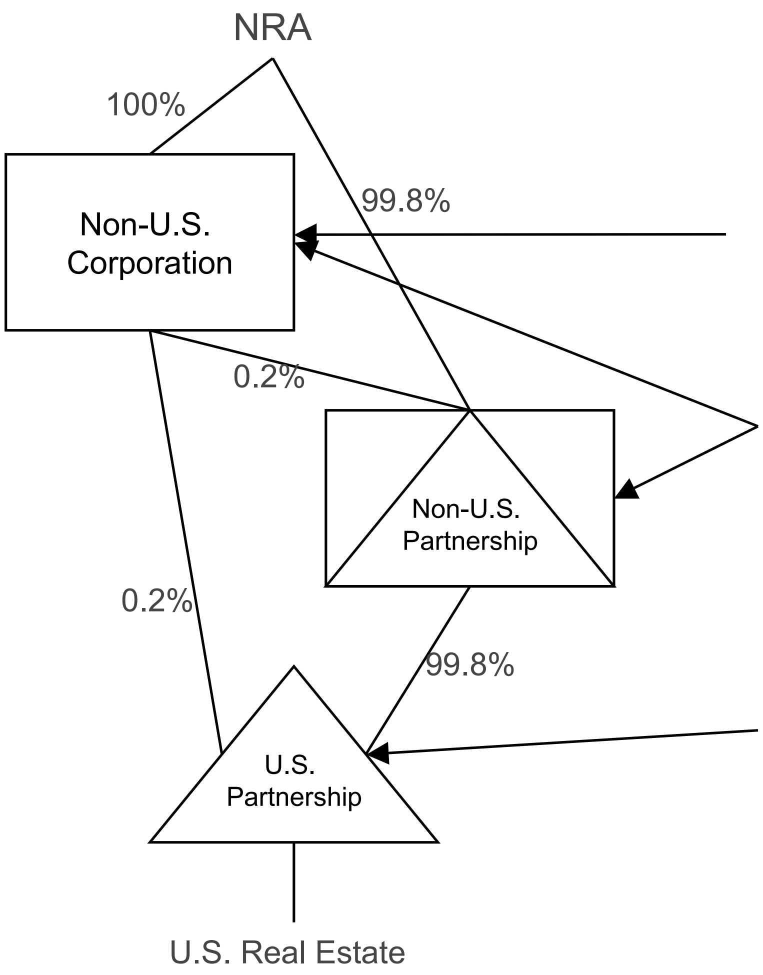
Consequences:

<u>U.S. Estate & Gift Tax</u>:
No estate or gift tax on transfer of Non-U.S. Corporation.

<u>U.S. Corporate Income Tax</u>:
35% tax on ECI.
No capital gain preference.

<u>U.S. Corporate Income Tax</u>:
30% dividend equivalence tax on withdrawn U.S. earnings.

Ownership Through Partnership Structure



Consequences:

U.S. Corporate Income Tax:
35% tax on ECI.
No capital gain preference

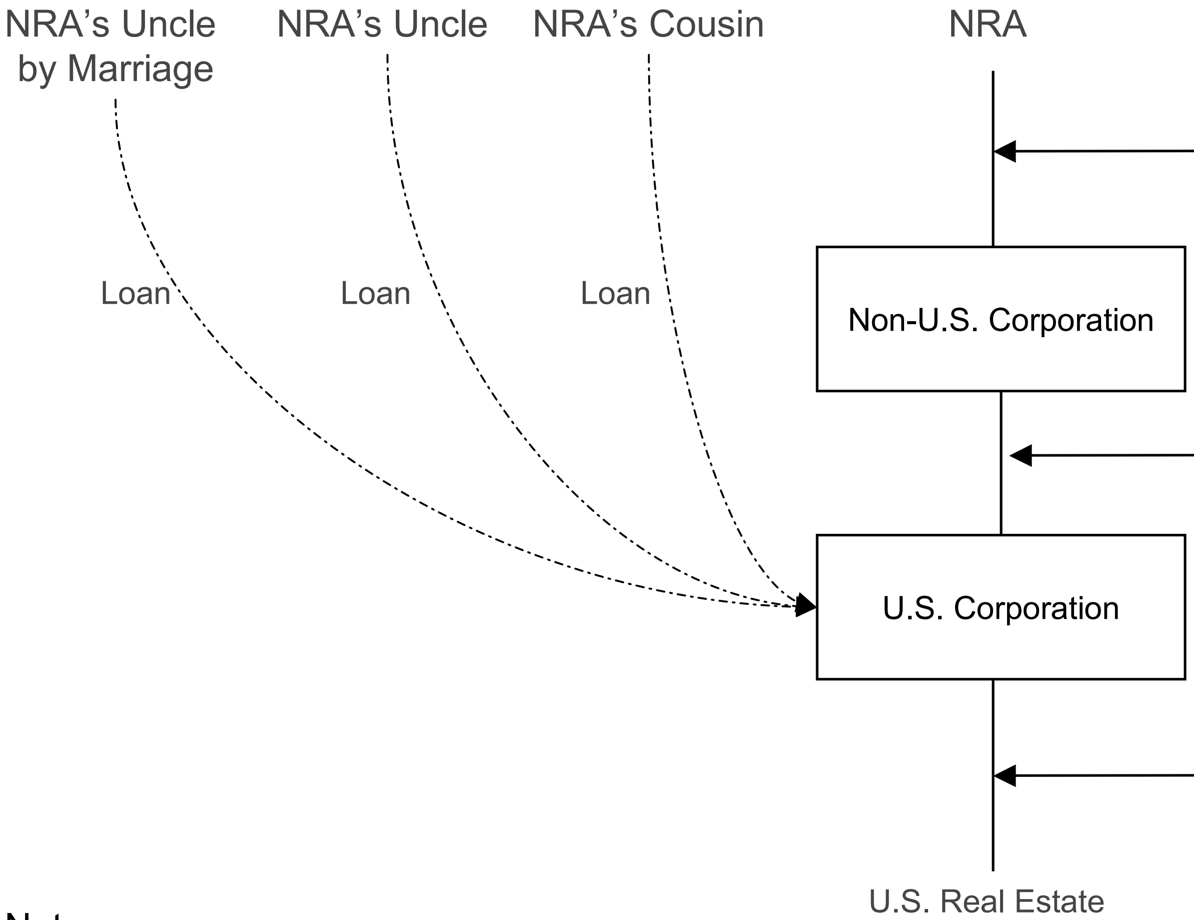
U.S. Estate & Gift Tax:
No estate or gift tax on transfer of Non-U.S. Corporation or Non-U.S. Partnership.

U.S. Partnership/NRA Income Tax:
NRA pays single level of tax on net income at 39.6%.
20% capital gain preference available.
Income tax collected through withholding.

Portfolio Interest Exemption

- There is generally a 30% withholding on payments of U.S. source interest to foreign payees.
- If the portfolio interest exemption applies, this withholding does not apply.
- Therefore, structuring a loan transaction to take advantage of this exemption can be beneficial.
- Requirements:
  - Non-U.S. lender (unrelated to U.S. borrower, not a bank, not a CFC, and is not engaged in a U.S. trade of business)
  - Lends money to a U.S. borrower pursuant to a
  - Debt instrument
  - Which pays a fixed rate of interest, and
  - Non-U.S. lender documents its non-U.S. status.

Extended Family Portfolio Loans



Consequences:

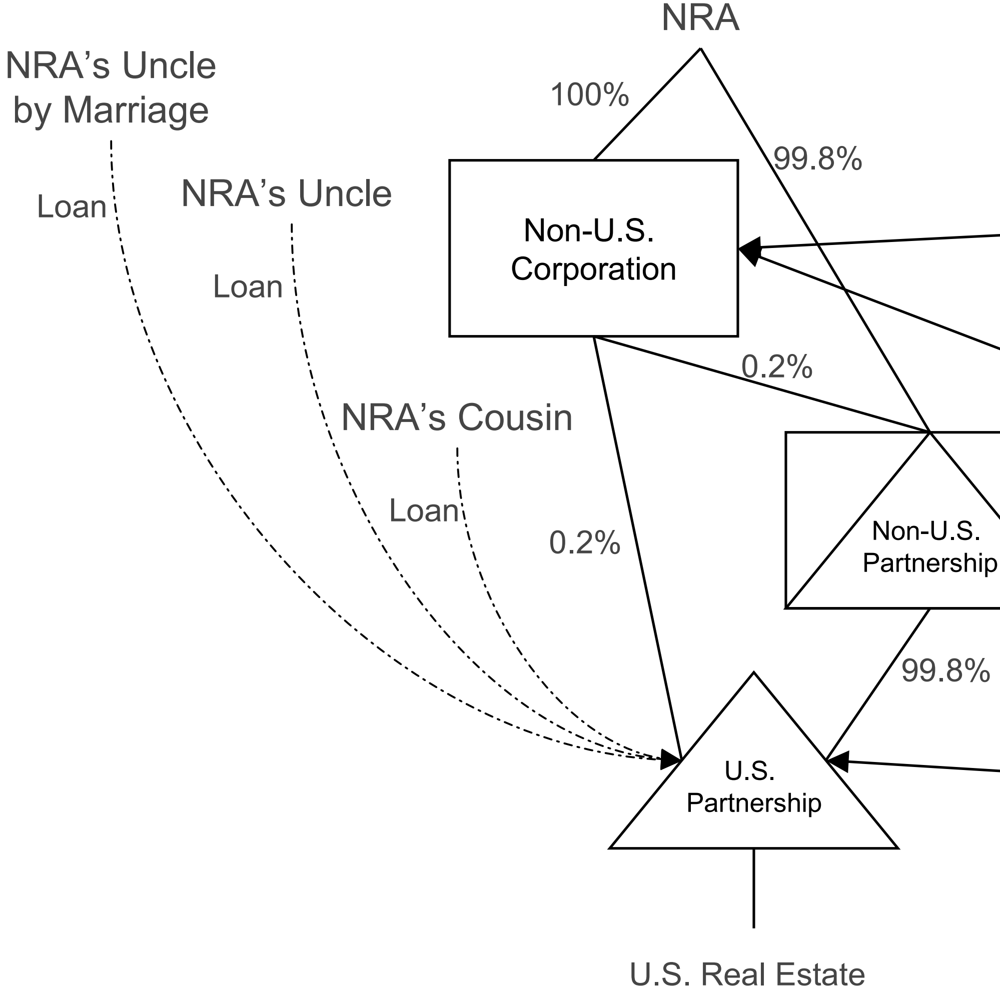
U.S. Estate & Gift Tax:
No estate or gift tax on transfer of Non-U.S. Corporation.

U.S. Withholding Tax:
30% on dividend & interest distributions.
Sale of U.S. Corporation subject to tax if > than 50% of assets are U.S. Real Estate.

U.S. Corporate Income Tax:
35% tax on net income.
No capital gain preference.
Income reduced by "portfolio loan" interest payments.

Notes:
"Portfolio loan" interest payments are not subject to U.S. withholding tax.
Loan interest rate may be up to 18%, depending on circumstances.
Unrelated entities may also qualify for "portfolio loan" U.S. withholding tax exception.

Ownership Through Partnership Structure With Portfolio Loans



Consequences:

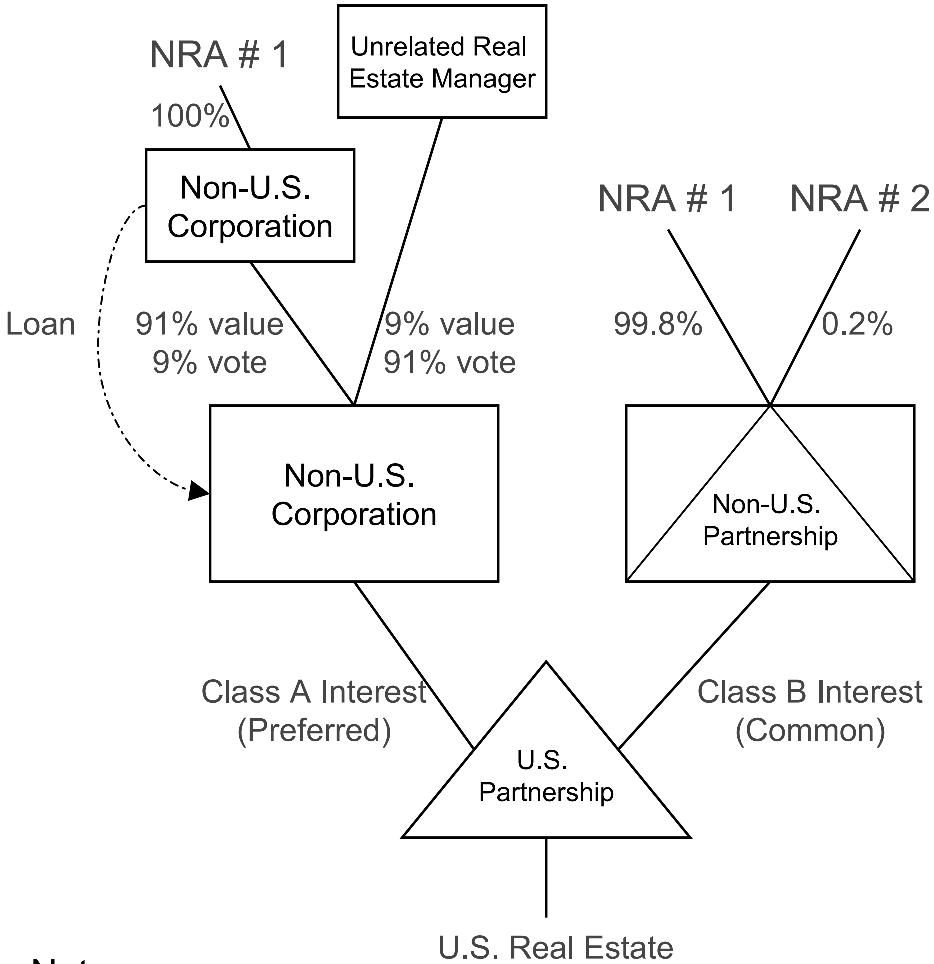
<u>U.S. Corporate Income Tax</u>:
35% tax on ECI.
No capital gain preference

<u>U.S. Estate & Gift Tax</u>:
No estate or gift tax on transfer of Non-U.S. Corporation or Non-U.S. Partnership.

<u>U.S. Partnership/NRA Income Tax</u>:
NRA pays single level of tax on net income at 39.6%.
20% capital gain preference available
Income reduced by "portfolio loan" interest payments.
Income tax on net income collected through withholding.

<u>Notes</u>:
"Portfolio loan" interest payments are not subject to U.S. withholding tax.

Ownership Through Blended Structure



Consequences:

U.S. Corporate Income Tax:
35% tax on ECI.
No capital gain preference.
Income reduced by "portfolio loan" interest payments.

U.S. Estate & Gift Tax:
No estate or gift tax on transfer of Non-U.S. Corporations or Non-U.S. Partnership.

U.S. Partnership/NRA Income Tax:
NRA pays single level of tax on net income at 39.6%.
20% capital gain preference available.
Income tax collected through withholding.

Notes:
Appreciation allocated to Class A Interest (Common).
Fixed income paid to Class B Interest (Preferred).

Overview of Structure

- Structure is flexible to accommodate U.S. greencard holder in both asset management company and investment fund.
- Structure considers U.S. partnership having minority U.S. co-investor in each project.
- Structure avoids burden of State of Florida corporate taxes.
- Structure places client in charge of accounting and tax compliance, including other financial aspects of operations.
- Structure ensures foreign individual investors can later apply to reside in U.S. with minimal pre-immigration tax planning.

Contact Information

- If you have questions regarding any aspect of this presentation, please contact one of your DLA Piper tax advisors.

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