

***Taking roots in
Luxembourg***
Luxembourg Real Estate
Investment Industry
Substance Survey 2010.
Second edition

*This report aims to
establish a benchmark of
the substance of entities in
Luxembourg*



Introduction

The market for real estate investment vehicles keeps improving as it provides international investors with flexible and innovative real estate investment products and structures. The three key areas of concern regarding Luxembourg holding companies should be:

- **maintaining corporate residence in Luxembourg,**
- **ensuring there is sufficient substance in Luxembourg,**
- **avoiding permanent establishments outside Luxembourg.**

About substance

Why do we care about substance?

The level of substance of a holding company is a mean to achieve tax structuring benefits. Therefore, the risk that foreign tax authorities apply local tax to the fund and/or to the Luxembourg holding company can be reduced.

The importance of substance in Luxembourg has increased as a result of the new economic environment and the recent developments on the OECD principles of transparency and exchange of information.

Recommended substance requirements

Substance is more about creating a genuine and real underlying economic activity in Luxembourg than drawing up a list of specific requirements.

However, foreign tax authorities will mainly concentrate on factors in assessing whether an economic activity is being undertaken in Luxembourg. The generally recommended substance requirements are:

- active senior decision-makers,
- employees,
- office facilities,
- documentation,
- Board of Directors and shareholders' meeting,
- profits or financing.

About local presence

As there are no hard and fast rules, each assessment will be reviewed based on the particular facts and circumstances. Each of the investment structure reviewed has taken different approaches to managing each of these issues.



About the survey

Setting up Real Estate Investment entities has heightened national interest. In this context, PwC has conducted a “local presence survey” to benchmark the Luxembourg substance of these entities.

This survey comprises of around 230 Real Estate Investment entities selected from a global list of institutions with a Luxembourg legal structure, which primarily includes large institutions. Most of the respondents have completed the survey through online forms. However, some responses were collected during structured interviews held by phone or face to face meetings. The survey respondents were kept strictly confidential.

The survey included 35 questions focused on various aspects of the Luxembourg activity and presence. This survey provides two sets of key criteria:

Key criteria 1

- a. Employees' structure
- b. Directors' involvement
- c. Documentation

Key criteria 2

- a. In-house and outsourced activities
- b. Quality of service providers

This survey comprises of around

230

Real Estate
Investment
entities



Panel description

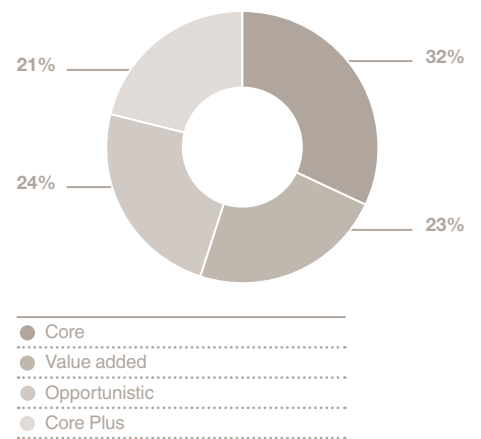
1. Activity & Roles

The overwhelming majority of the structures in the panel (90%) have their asset management located abroad as well as their fund management (60%). However, the administrative support is mostly set in Luxembourg (90%).

2. Type of funds

The vast majority (85%) of the regulated structures in the panel are direct real estate funds (the remaining 15% are funds of real estate funds). Most of these regulated structures (72%) are Specialised Investment Funds (SIF). 44% are “Fonds Commun de Placement” (FCP) and 28% are “Sociétés d’Investissement à Capital Variable” (SICAV). Umbrella structures represent 33% of the structures in the panel.

Figure 1: Most of the structures in the panel are Core and Core Plus

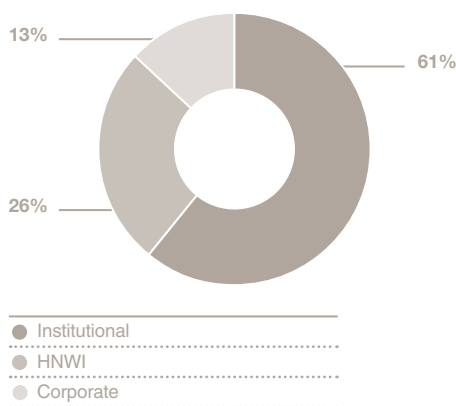


Question: What is/are the investment risk profile of your fund(s)?

3. Investors

The great majority (54%) of investors of the structures in the panel are from European countries (including 14% from Germany and 14% from the UK).

Figure 2: Institutions turn out to be the main type of investors

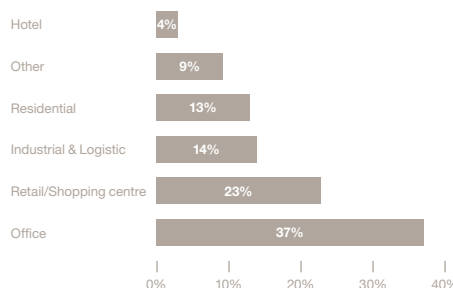


Question: What are the main type of investors of the fund?

4. Portfolio

The portfolio of the companies surveyed is made up of assets mostly (82%) located in Western Europe.

Figure 3: Office and Retail/Shopping Centre represent the main property types

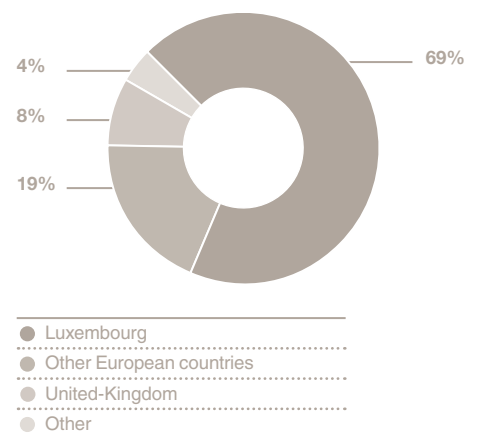


Question: What are the main property types of your assets?

5. Tax Aspects

30% of the structures in the panel have been challenged by foreign tax authorities regarding the substance set up in Luxembourg.

Figure 4: Most companies have their tax consultant in Luxembourg



Question: Where is your tax consultant located?

Key criteria 1:

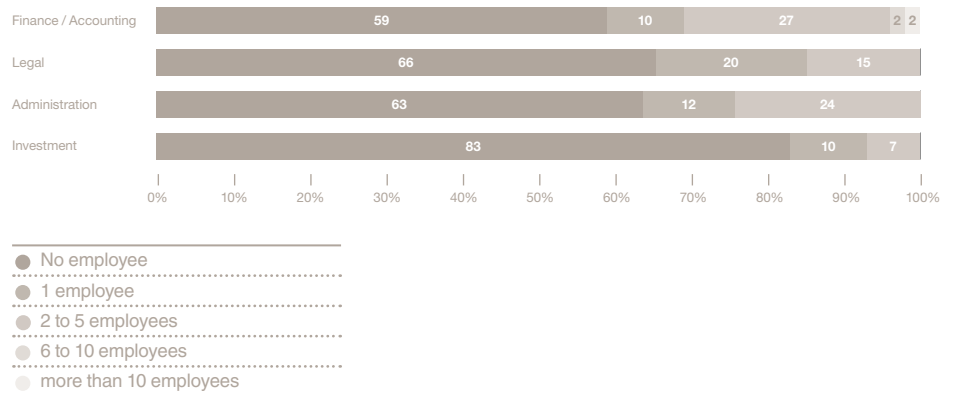
Employees' key criteria: Offices should have a proportional number of active employees in relation to the investment structure(s) to be managed.

The number and role of employees within the local organisation constitute essential elements in terms of substance. As a matter of fact, offices with a large number of active employees are generally considered to have greater substance. In other words, investment structures with a great number of employees usually started their operations with only one employee in Luxembourg and gradually employed additional staff. We found that staff was employed equally by the Luxembourg management company (28%), the Luxembourg SPV (28%) and mixed at different level (28%). Only 16% were employed at the fund level.

Recommended substance requirements

Offices should have a proportional number of active employees in relation to the investment structure to be managed. Employees must be reasonably skilled to maintain the operations of the investment structure. Sharing resources between several entities can be achieved by using dual contract structures.

Figure 5: Luxembourg staff according to role within your entity



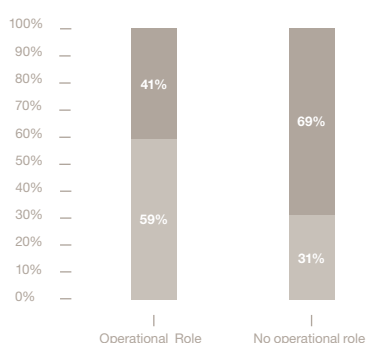
85% of the respondents have maintained or increased the number of employees over the last two years

50% of the respondents expect to increase the number of employees for the next one to three years

Directors' key criteria: The majority of Board of Directors of the investment structures should be composed of Luxembourg residents.

In most cases, Investment structures have their own premises. This trend increased in 2010.

Figure 6: Most of the Luxembourg resident directors have an operational role



- Third party Luxembourg resident Directors
- Inhouse Luxembourg resident Directors

Question: Do Luxembourg resident Directors have an active role in certain committees (investment, audit, valuation, ...)?

Only in limited cases (36%), the Directors composing the boards are Luxembourg residents.

Recommended substance requirements

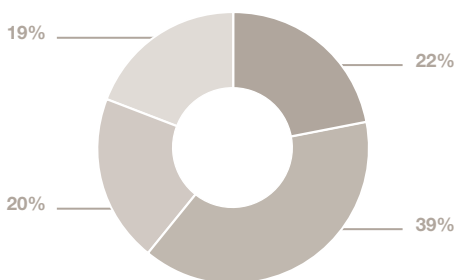
The majority of Board of Directors of the investment structures should be composed of Luxembourg residents (with the same status and rights as non-resident directors). The location of the remaining members of the board is subject to each country requirements. When a director cannot physically attend a board meeting, a legally appointed deputy should stand in. Ideally, directors should not attend meetings over the phone.

80% of interviewees consider the fiscal and regulatory environment as main drivers to help develop their operations in Luxembourg.



Documentation's key criteria: Specific documentation should be kept in the Luxembourg premises.

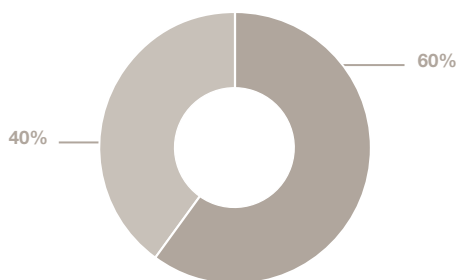
Figure 7: 39% of CEO/CFO prepare the documentation for the board



- Company secretary
- CEO/CFO
- Administration agent
- Other

Question: Who is in charge of preparing the documentation for the board and the shareholders?

Figure 8: This process mostly takes place in Luxembourg



- in Luxembourg
- abroad

Question: Where does this process take place?

Recommended substance requirements

Specific documentation should be kept in the Luxembourg premises such as a manual of procedures /operating guidelines, company books (e.g. management accounts), company files (e.g. contracts, bibles, tax returns, etc.) and archives.

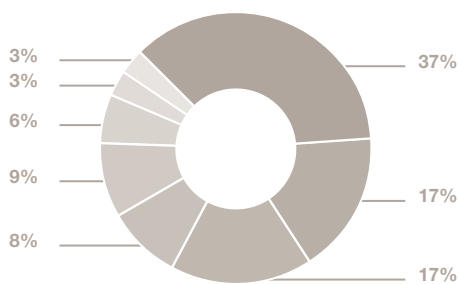


39% of CEO/CFO prepare the documentation for the board

Key criteria 2:

Outsourcing key criteria: Varying degrees of both involvement and quality of Luxembourg domiciliation agents. Some will be actively involved in senior decision-making while others will only provide administrative services.

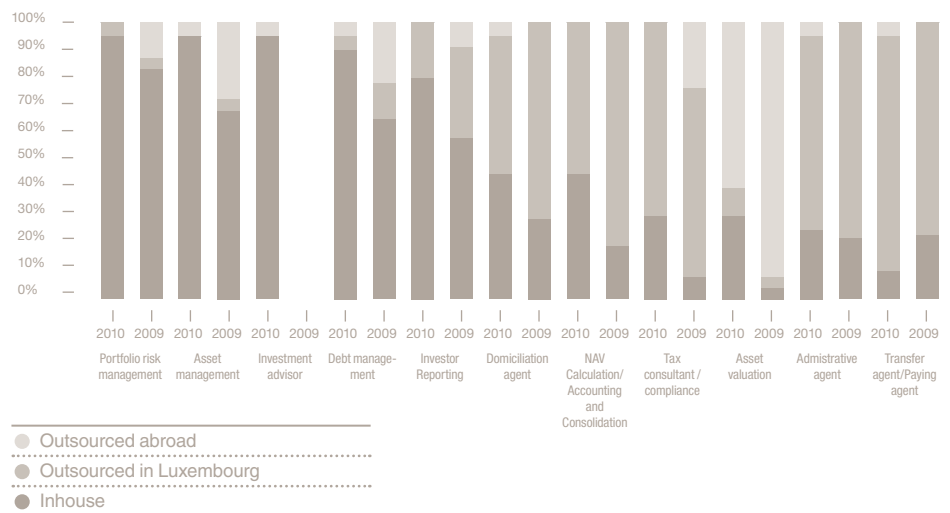
Figure 9: Finding the right staff is considered to be the biggest difficulty in developing operations in Luxembourg



- Finding the right staff
- Quality of service providers
- Flight connections
- School facilities for children expatriates
- Nothing
- Cost of living
- Absence of expatriates
- Other

Question: What do you find the biggest hurdle in developing your Luxembourg operation further?

Figure 10: There is a clear trend towards inhouse performance



Question: What are the roles and activities you have outsourced?

Conclusion

Impression of Substance

The impression of substance indicator is based on a comprehensive analysis of the respondents' answers. It gives qualitative information on the level of substance in investment structures located in Luxembourg. According to the number of respondents, the low relative substance is quite limited. However, it is surprising to note that substance indicators have decreased for some large players.

Figure 11: Impression of relative substance (% of respondents)

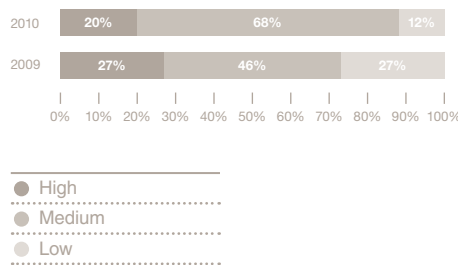
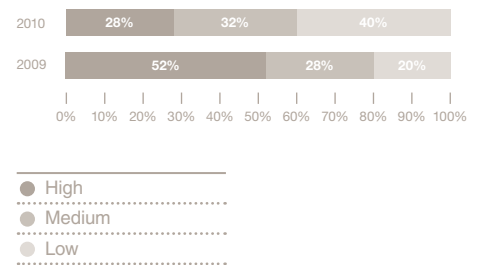


Figure 12: Impression of relative substance (% in volume)



Key points to note

1. Investment structures with a lower level of substance

are likely to represent “inadvisable practice” rather than the lower end of an acceptable level of substance.

2. Investment structures with a higher level of substance

simply have a high level of substance in comparison to the other funds, but might not benefit from additional protection from tax authorities inquiries.

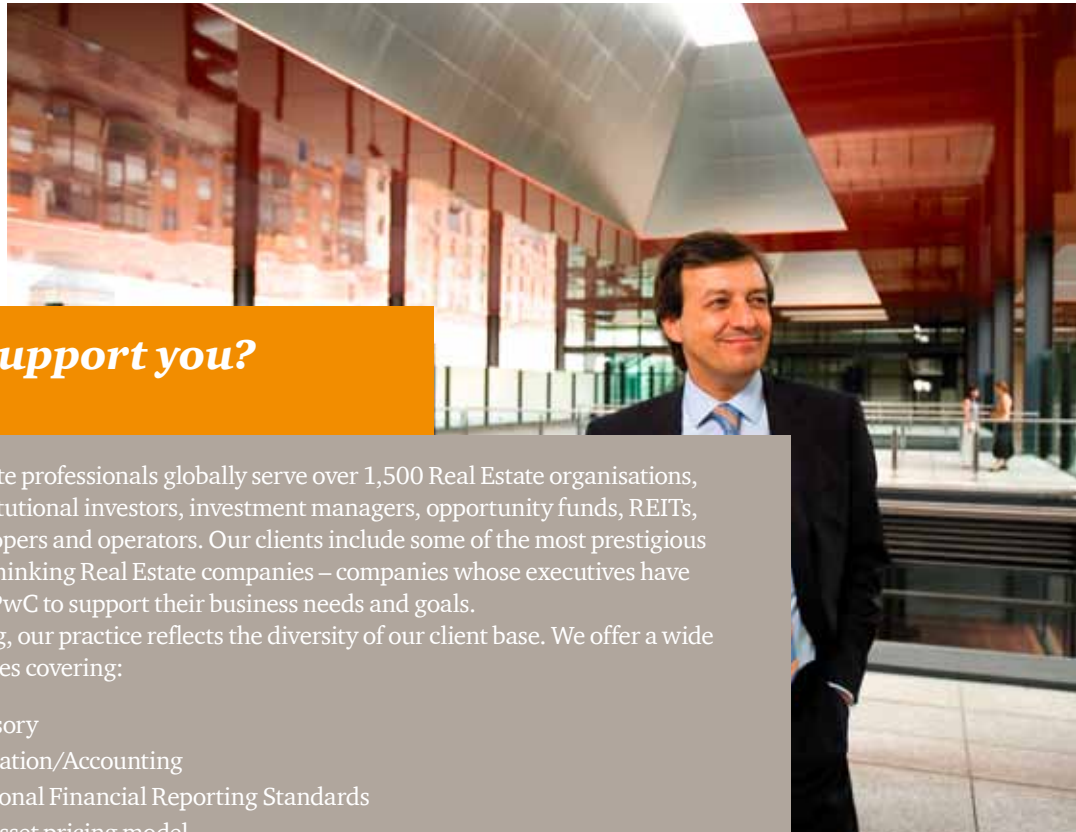
3. The introduction of new rules

in some jurisdictions, especially in Germany, France and Italy as well as the introduction of the transfer pricing circular has generated greater substance requirements.

4. The substance positions of the funds reviewed will be significantly different

in 12 months' time as our clients have required deeper analyses of the level of substance in their holding companies.

PwC Luxembourg Real Estate Group



How we can support you?

PwC Real Estate professionals globally serve over 1,500 Real Estate organisations, including institutional investors, investment managers, opportunity funds, REITs, lenders, developers and operators. Our clients include some of the most prestigious and forward-thinking Real Estate companies – companies whose executives have come to trust PwC to support their business needs and goals. In Luxembourg, our practice reflects the diversity of our client base. We offer a wide range of services covering:

- Tax advisory
- Consolidation/Accounting
- International Financial Reporting Standards
- Capital asset pricing model
- Listing and public offering
- Training courses
- ...

Our people working alongside you

Amaury Evrard , Audit Partner, Luxembourg Real Estate and Infrastructure Leader	+352 49 48 48 5751	amaury.evrard@lu.pwc.com
John Ravoisin , Audit Partner	+352 49 48 48 5717	john.ravoisin@lu.pwc.com
David Roach , Tax Partner, Central Cluster Real Estate Tax Leader	+352 49 48 48 5707	david.roach@lu.pwc.com
Alexandre Jaumotte , Tax Partner	+352 49 48 48 3330	alexandre.jaumotte@lu.pwc.com
Philip Mael , Corporate Finance Director	+352 49 48 48 2530	philip.mael@lu.pwc.com

www.pwc.lu

PwC Luxembourg (www.pwc.com/lu) has about 2000 professionals from 53 different countries. PwC firms provide industry-focused assurance, tax and advisory services to enhance value for their clients. More than 161,000 people in 154 countries in firms across the PwC network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

"PwC" is the brand under which member firms of PricewaterhouseCoopers International Limited (PwCIL) operate and provide services. Together, these firms form the PwC network. Each firm in the network is a separate legal entity and does not act as agent of PwCIL or any other member firm. PwCIL does not provide any services to clients. PwCIL is not responsible or liable for the acts or omissions of any of its member firms nor can it control the exercise of their professional judgment or bind them in any way.

© 2011 PricewaterhouseCoopers S.à.r.l.. All rights reserved. In this document, "PwC" refers to PricewaterhouseCoopers S.à.r.l. Luxembourg which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.