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# GUIDE TO PROPERTY INVESTMENT IN PORTUGAL

### A Message from AICEP

Portugal is an excellent place in which to live, invest and do business. Its skilled human resources, world-class infrastructure, business-friendly environment and easy access to markets are several factors which have contributed to a continuous flow of new investments into industry, tourism, commerce and services.

In due recognition of the economic importance of real estate activities and Portugal's attractiveness to inward investment in this area, AICEP is delighted to be associated with the publication of this Investment Guide. We consider it to be an important tool to support investment decisions, illustrating the potential to conduct safe business in a stable country which prides itself on the way it welcomes visitors and investors.

AICEP, as an Investment Promotion Agency is available to help all developers interested in finding out more about investment opportunities in Portugal.

#### Basílio Horta

Chairman and CEO



# INTRODUCTION

Portugal is an Iberian Peninsula country, bordered by the Atlantic to the west and south and Spain to the north and east and, in addition to its continental landmass, also comprises the archipelagos of the Azores and Madeira. It has a population of 10.6 million with a population density of 115 inhabitants per sqm.

Portuguese territory is split up into three administrative divisions. The first such division comprises 18 administrative county districts plus the autonomous regions of the Azores and Madeira which are, in turn, sub-divided into 308 municipal districts and 4,260 parishes.

Lisbon is the capital of Portugal and its largest city with around 480,000 inhabitants (2 million in Greater Lisbon). Portugal's second largest city is Porto, in the northern region with around 210,000 inhabitants (1.3 million in the Greater Porto Area).

Portugal is a democracy. Its sovereign bodies are the President of the Republic, Assembly of the Republic, Government and the Courts. The current President of the Republic, elected for a 5 year term, is Aníbal Cavaco Silva. Elections for the 230 deputies of the Assembly of the Republic are held every 4 years and are followed by the appointment of the Prime Minister (currently José Sócrates) who then forms the government.

Portugal has been a member of the European Union since 1986 and was a founding member of NATO in 1949. It has been a member of the United Nations since 1955.

### MAP OF PORTUGAL



# PROPERTY MARKET

# 1. Overview of the domestic property market

The property market in Portugal is highly developed. It has a high relative quality of supply in all sectors, on a par with the larger core European markets, dynamic demand and a considerable presence of foreign occupiers. The market is highly transparent, with various international consultants providing information on all commercial property sectors. There is also a strong international contingent of developers and investors and many of the main European investment houses have assets in the country.

The legal and fiscal framework is particularly favourable to Portuguese property investment funds (FIIs) which, since their creation at the end of the 1980s, have achieved strong growth and development. This industry is currently responsible for managing assets of more than €12 billion, split up over all sectors and geographic zones in Portugal.

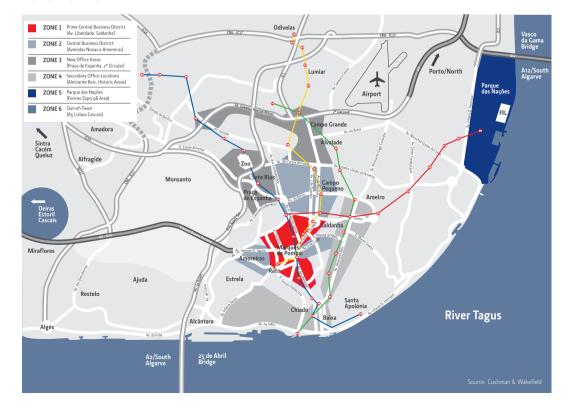


Lisbon | Source: Cushman & Wakefield

# Occupational market Office, retail and industrial space

The **office market** mainly revolves around the city of Lisbon. It has grown in importance since the 1990s and has a current supply of more than 4.4 million sqm split up into 7 zones.

### LISBON OFFICE MAP

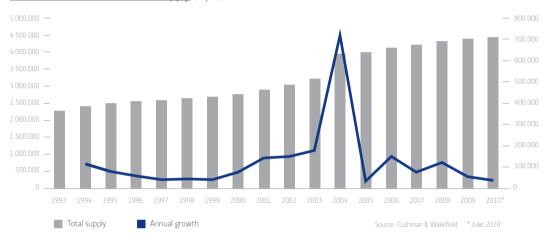


Lisbon's central business district, or CBD, is mainly housed in zones 1 and 2; followed by zones 3 and 4 which, although within the perimeter of the Lisbon municipal district, occupy a secondary position. Zone 5 (Parque das Nações) is located in Lisbon's northern zone, built on the back of the Expo 98 Lisbon World Exposition and currently the capital's office market showcase. Zone 6 is the out-of-town market, comprising the municipal districts of Oeiras, Cascais and Sintra. There are no defined geographic limits to Zone 7 which comprises a series of high quality office buildings located

outside the six market zones. Zone 7 has approximately 680,000 sqm of office space, and was added to the zonal system of Greater Lisbon's total supply in 2004.

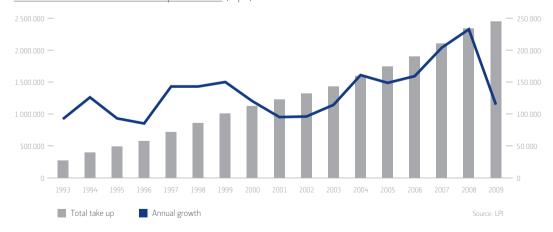
After more intensive growth in the 1990s and first few years of the twenty first century, with annual growth rates of around 3%, developers have adopted a more cautious approach over the last 5 years. This has translated into annual rates of less than 2% growth in supply.

### Greater Lisbon Offices - Total supply (sqm)



Average annual take up in Lisbon is around 120,000 sqm but has been rising steadily since the start of the current decade. Maximum demand for office space reached its peak in Greater Lisbon in 2008 however, at more than 240,000 sqm in transactions. The market was then hit by the economic crisis in 2009, returning to the level of transactions recorded in 2003.

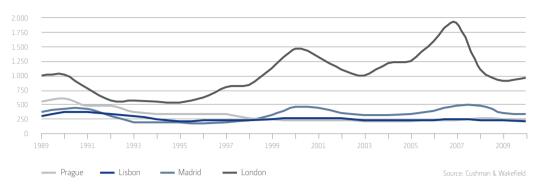
### Greater Lisbon Offices - Take up evolution (sqm)



Lisbon's prime rent, at the end of first half 2010, was €18.5 sqm. This was sharply down over 2009 and early 2010, which was a crisis stage in the main European property markets and to which Lisbon was no exception. A long term view underlines the stability of rents in the Lisbon market, over the course of more than 20 years of analysis. A comparison between prime rent changes in other European capitals indicates a degree of

stability which would bring lower levels of risk. Lisbon's rent values are on a par with Prague, which is very similar to the Portuguese capital in market terms, both in regional population size and in the quality of its stock.

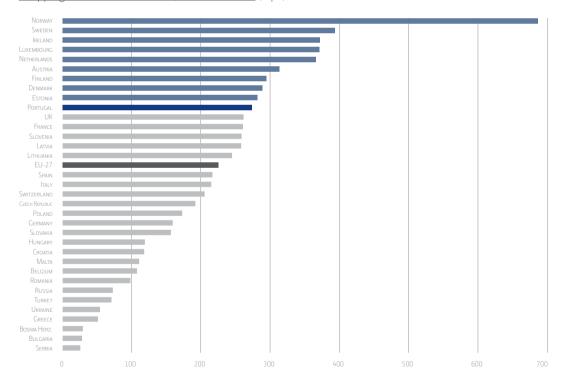
### Office rents - Lisbon vs other european cities (€/sqm/year)



The **retail sector** has, since the 1990s, been the main player in the property market in Portugal. Reactions to the first modern shopping centres in Portugal, clearly demonstrated the enormous appetite of consumers and retailers for this retail format, very much owing to the fact that high street retail activities were less well developed than in other European countries. These projects

which, since early days, have recorded excellent performance levels and sustained growth in profitability, were mainly responsible for attracting many of the foreign investors who continue, even in present times, to own property assets in Portugal.

### Shopping Centre Provision Per 1,000 Inhabitants (sqm)

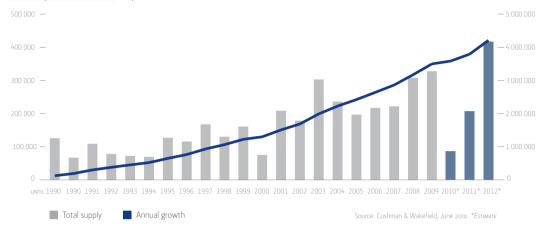


Source: Cushman & Wakefield

The increase in the supply of retail space in Portugal has kept pace with this industry's success story, having recorded high growth rates up to the last few years, when the market started to show signs of maturity with fewer new openings. Future prospects will take the form of a development market involving the exploitation of one-off opportunities or specialising in the

reconversion and modernisation of centres which have opened over past decades. Modern retail space (shopping centres, retail parks and factory outlet centres) in Portugal as at the end of the first half 2010, amounted to more than 3.5 million sqm, of which around 3 million sqm in shopping centres.

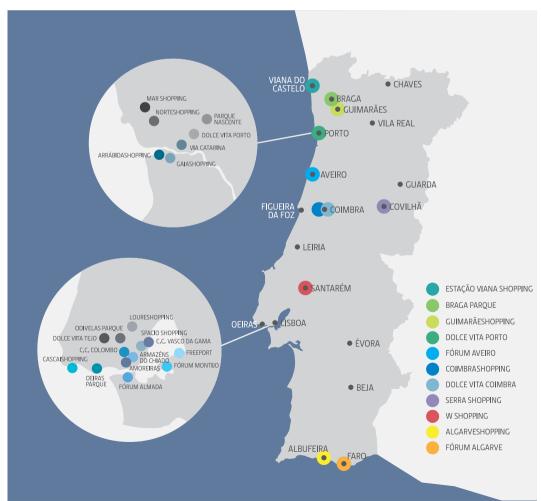
### Retail space evolution (sqm)



Retail schemes in Portugal comprise projects of internationally recognised quality which, in many cases, represent the most recent architectural trends in European retail. Portuguese shopping centres are frequently awarded prizes in recognition of their excellence from international institutions specialising

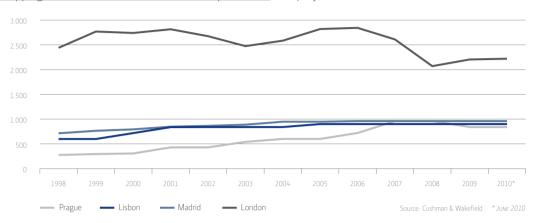
in the sector. Most of Portugal's shopping centres are located in Lisbon and Porto. The Greater Lisbon Region has around 1 million sqm and the Greater Porto Region, around 700,000 sqm.

### MAIN RETAIL SCHEMES IN PORTUGAL



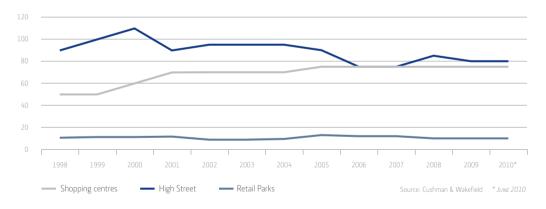
Portuguese shopping centre rents have always tended to be competitive in Portugal versus other European countries and have also proved to be more stable in many cases.

### Shopping centre rents - Lisbon vs other european cities (€/sqm/year)



Notwithstanding a certain lower level of dynamism, Lisbon's Chiado prime zone is the retail segment with the highest rents. The scarcity of high quality space and growing success of this high street retail trading zone go part way to explaining this trend. These are followed by shopping centres, whose rents are reasonably similar to shops in the Chiado and whose evolution, over the years, has also been marked by stability, particularly over the last decade.

### Prime retail rents - Portugal (€/sqm/year)



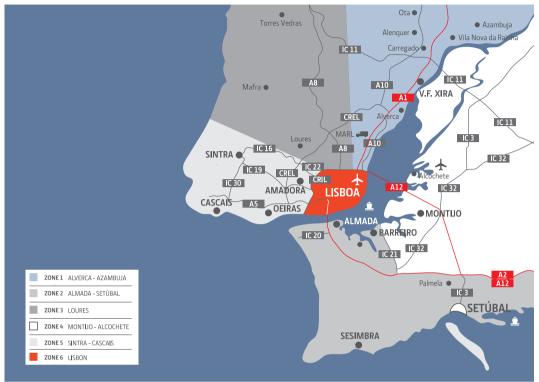
The **industrial market** in Portugal is somewhat less professional and transparent than the other sectors relative to the rest of Europe and has a smaller contingent of international operators, particularly in terms of investors and developers. The gap with the current level of development of the other property sectors in Portugal has, however, been closing over the course of the last few years. New projects in the market, or currently under construction, comprise high quality premises designed to meet the requirements of international logistics operators. Notwithstanding the fact that overall supply remains high, there has been a slight increase in demand for high quality space in prime zones. Logistics and distribution operators continue to dominate the sector, particularly in zones with high quality infrastructure and good accessibility.

The government's Portugal Logistics programme, for the creation of a nationwide network of strategic platforms located next to freight transport infrastructure such as airports, railways

and ports and the border with Spain, is also likely to make a future contribution to a higher quality of supply and greater development in this sector in Portugal.

Greater Lisbon's industrial and logistics market is split up into 6 zones, as shown in the following map - Zone 1 (Alverca-Azambuja), Zone 2 (Almada-Setúbal), Zone 3 (Loures), Zone 4 (Montijo-Alcochete), Zone 5 (Sintra-Cascais) and Zone 6 (Lisbon).

### GREATER LISBON INDUSTRIAL AND LOGISTICS MAP

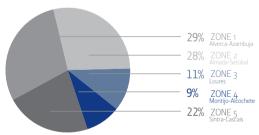


Source: Cushman & Wakefield

The Lisbon Metropolitan Area has around 12 million sqm of industrial and logistics space. The warehousing and logistics sector accounts for around 70% of this.

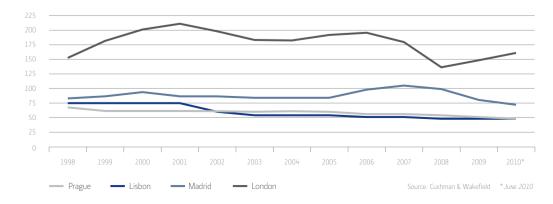
Although there has been a considerable drop in rent levels in Greater Lisbon's industrial space since the end of the 1990s, the fact that they have remained stable since 2008, is indicative of the market's greater resilience during the recent property crisis. Rent levels in Portugal are also among the lowest in Europe.

### Industrial and Logistics Market Supply Greater Lisbon



Source: Cushman & Wakefield

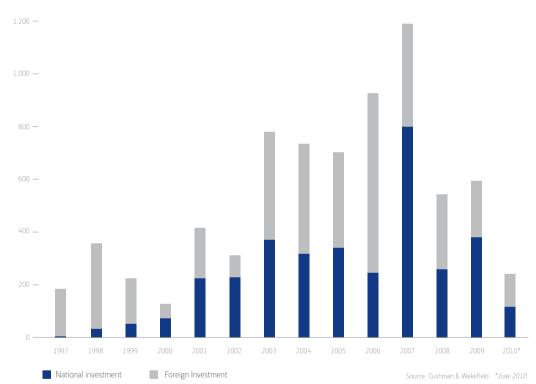
### <u>Prime industrial rents - Lisbon vs other european cities</u> (€/sqm/year)



1985 paved the way for property investment funds in Portugal. Since their launch and up until the 1990s, these funds had typically been used as SPV's rather than as an actively managed, pooled, closed-end-fund. The market in Portugal, up to 1998, was relatively small and not particularly professional, with foreign investments being few and far between. Reference should be made to business transactions involving the purchase of the Arquiparque office park in Miraflores and the sale of 50% of CascaiShopping and Colombo shopping centres, then belonging to Sonae Imobiliária

The elimination of foreign exchange risk *vis-à-vis* most other European markets, when Portugal joined the euro in 1999, placed the country on the radar of international investors. Investment, in 1998 ahead of the Euro's launch, increased from around €180 million to more than €400 million, around 90% of which was foreign. Almost all asset transactions were in the office or shopping centre sectors; with retail property accounting for more than 60% of the capital involved.

### <u>Domestic vs Foreign Investment</u> (Million €)

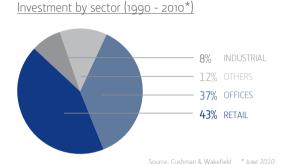


The market has continued to develop positively since then, with increasing investment volumes and growing demand for investment products from Portuguese and foreign investors. 2003 closed with growth of around 150% in the investment volume, with unprecedented levels of liquidity in the property market. The investment market continued to grow over the following years, breaking through the €1 billion barrier in asset transactions in 2007 and achieving a new investment volume record. This was an exceptional year for the market and the euphoria felt by investors, at this stage, was hardly dented by the events of the summer of 2007 in the United States, which, at a later stage, came to be seen as the harbinger of the major crisis of recent times.

The full effects of the economic crisis were felt in Portugal in 2008 and had an almost immediate impact on property investment. The misgivings of institutional investors, allied with the scarcity or virtual non-existence of funding for the property sector, had a severe effect on the market.

After two years' growth of around 30% in transactions, 2008 was down more than 60% over the preceding year, at just over €500 million. Notwithstanding slight growth in 2009, the market remained depressed, with transactions of around €590 million. The second half of the year did see the first signs of recovery in the European economy however, consequently giving property markets a lift in the first three months of 2010, with a level of guarded optimism in the market when occupational activity stirred slightly from its state of lethargy and a number of investors returned with the aim of studying the market and making the odd transaction. In the second quarter however, concerns over the sustainability of European sovereign debt as well as depressing news on the Portuguese national economy took its toll on the occupational market and on investment activity. January to June 2010 witnessed 18 transactions, totalling €240 million, at an average lot size of €13 million.

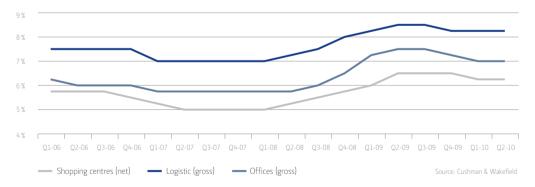
Retail and office space are still the sectors most in demand. A certain level of investment in the industrial and hotel sectors has been noted since the start of this decade, as well as several one-off deals involving hotels and educational facilities. The residential sector has always been the poor cousin in terms of investment market activity, owing to a highly unprofessional rental market and legal environment which is not in line with institutional investors' requirements. Since 2008, however, several asset management companies have formed a "Property Investment Fund for Housing Rentals" and nowadays a larger share of investment has been channelled into the residential investment market.



The retail sector's domination derives from the excellence of its performance since the 1990s. Today's more mature market and the less positive effects of the crisis in the sector, may contribute towards a change in this trend. Prime products in Portugal's retail market sector will, however, always be in the sights of major international investors, based on historical performance and resilience even in times of crisis.

The evolution of market values as shown by yields (capitalisation rates of rents in perpetuity) accurately reflects the investment market's global development. Prime yields, in the 1990s were very high on relatively low asset values in comparison to other European markets. The domestic market's evolution and greater professionalism, together with a consequent increase in asset values, explains the falls in yields in all sectors over subsequent years. The effects of the international crisis were first felt in Portugal in 2008 meanwhile, with the beginning of the upwards trajectory of market yields translating into considerable losses in value. Prime yields, from June 2008 to June 2010 increased 150 basis points to 7% for office space, 6.25% for retail operations and 8.25% for the industrial sector, as at the end of the first of quarter 2010.

### Prime yields evolution (1996-2010)



### 4. Property investment funds (FIIs)

The property investment funds industry in Portugal dates back to 1987, following the implementation of Decree Law 1/87 of 03 January 1987, regulating the activity of property investment funds in Portugal.

According to the latest data supplied by securities watchdog CMVM, the property investment funds industry currently has around €12.3 billion in assets under management. These assets are split up into more than 250 investment funds of which 94% are closed-end funds administered by 52 fund managers. Open ended funds, in spite of being fewer in number, account for 46% of the sector at around €4.86 billion.

Notwithstanding the number of active funds, there is a high degree of concentration in this industry with the top three investment funds accounting for more than 20%, in value terms,of the volume of assets under management, at around €2.5 billion. Caixa Geral de Depósitos Group fund Fundimo manages the largest domestic property fund. The fund, also known as Fundimo, has more than €1 billion in assets. The Gespatrimónio Rendimento fund, managed by Esaf (Espírito Santo Group), with around €900 million in assets under management, comes second in this ranking. Santander Asset Management (Santander-Totta Group) manages Novimovest, which is the third largest domestic property investment fund with around €560 million in assets under management.

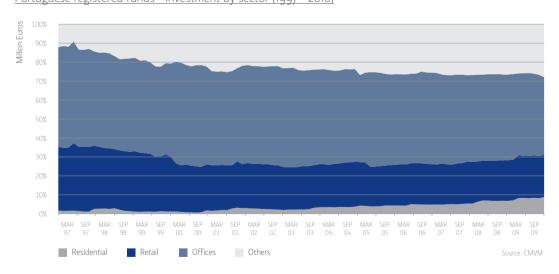
### Portuguese registered funds - Total net volume under management (1996 - 2010)



The investment vehicles' first ten years, which ended with total assets of €2,300 million in 1996, were characterised by a modest level of consolidation activity in the property market itself. It has been over the last 15 years that the industry has evolved strongly with an average annual growth rate of around 14% pa.

The 2001-2006 period was particularly active, in line with the strong evolution of the occupational market. Assets under management grew at an annual average rate of around 20% over the said five years. 2007 witnessed the beginning of a significant slowdown with virtual stagnation in the average three year asset value growth rate. This slowdown has been offset by the development of new types of property investment funds however, in the form of "Special Property Investment Funds" and "Property Management Funds".

### Portuguese registered funds - Investment by sector (1997 - 2010)



An analysis of property investment funds by type of property shows the domination of the retail sector with current totals of around €3,818 million. However, the proportion invested in this sector has been gradually diminishing since the end of 2005, essentially due to the increase in residential and other assets. There has, in particular, been a significant increase in the housing sector over the end of 2009 to an additional €800 million in assets under management in June 2010, due to the creation of **"Property Investment Funds for Housing Rentals"**. Assets related with the services sectors totalled around €2,040 million.

# 5. Foreign investment in property

The property investment market in Portugal came on to the radar of foreign investors when Portugal joined the euro in 1999. The reduction of foreign exchange risk and the positive evolution of the retail and office sectors acted as a magnet for foreign investment. Albeit classified as an emerging market at the time, asset value growth potential was high, associated with a track record of rent stability providing controlled risk for more conservative investors.

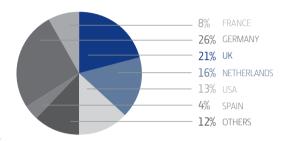
The Portuguese market has, since then, been generating interesting levels of return, particularly in the case of core products, with a certain resilience to the crisis while, at the same time, generating better performance than in some other European countries.

More than €4 billion has been invested by Germans, French, Dutch, American, British and others over the last 14 years and more than 50 international investors have invested directly or indirectly in Portugal since the country joined the Euro. This figure could have been higher as the Portuguese market was, on occasions, simply not large enough to supply sufficient products in terms of number, quality and/or scale, to fully meet the demand recorded at the time.

Most investment has been made in the retail sector and almost invariably in medium and large scale retail schemes, areas where there is less focus from local investors, owing to questions of scale and lack of specialisation. Foreign investors have also targeted the larger prime office assets, typically lot sizes over €20 million

Notwithstanding the recent, dramatic changes in the economic scenario affecting Europe, and the existence of caution in respect of any southern European country, Portugal remains ever present in the investment intentions of several of the most

### Foreign investment in Portugal (1996 - 2010\*)



Source: Cushman & Wakefield \* June 2010

important European investment houses, interested in effectively diversifying risk and achieving slightly higher income returns than those from mature markets, in a country offering security, transparency and less competition.

The future of property investment in Portugal is intrinsically associated with future economic and financial market performance. The fact that Portugal is a Eurozone country and has a good track record in terms of its capacity to rebalance its accounts has the effect of increasing many investors' comfort zone.

# 6. Property investment in the tourism sector

Tourism is, undoubtedly one of Portugal's main sectors of economic activity and is unanimously considered to be a strategic, priority area. It makes a significant contribution in securing external revenue, to cover the external trade deficit and in generating employment.

According to Turismo de Portugal's "Tourism Satellite Accounts", GVA (gross value added) generated by the sector in 2009, represented around 5% of national GVA, national tourism around 10% of GDP and with employment in the sector accounting for around 8% of total employment. According to the Bank of Portugal, revenue of €6,913 million from tourism in 2009, comprises the main current account heading at more than 42.5% of the total services revenue, i.e. 4.2% of GDP. In 2009, the tourism inflow/outflow balance was €4.2 billion, comprising a tourism cover rate of 20.1% in the current account. According to the latest figures, for the end of the first four months of 2010, the Portuguese travel and tourism account billed €839 million, recovering 30% of the net revenue "lost" over the same period 2008 - 2009.

Notwithstanding recent weaker performance, medium term prospects for domestic tourism are thought to be highly positive. A Euromonitor International study in August 2009, forecast tourist inflows by 2013 of around € 15 billion, with revenue of around €10 billion from tourism. The WTTC – World In turn, the Travel and Tourism Council, forecast 4% p.a. growth of the Tourism Economy in Portugal for the period 2010-2020.

In the case of investment in the tourism property market, many investors have firmly backed off and indefinitely postponed their investments. This is mainly due to a combination of the current highly uncertain context affecting the domestic and European economies and rapidly deteriorating budget deficit, entailing higher levels of public debt and liquidity shortages for companies, associated with greater difficulty in raising bank loans.

Many owners, on the other hand, have adopted a wait and see approach and are reluctant to sell, unless forced to do so by creditors or unless they receive higher than expected offers.

Transactions, however, require a reduction in the chronic gap between the levels offered by investors and the prices asked by owners, with the latter still not reflecting the strong reduction of hotels' operating cash flow verified over the last few months. Notwithstanding the difficult economic and financial market situation, owing to owners' and banks' reluctance to sell at a discount from peak bubble prices, the availability of products for sale has been more limited than expected and prices have remained relatively high, as there have not been many distress sales. This situation is not sustainable over the short to medium term.

In the current circumstances, with the almost non-existence of new bank loans and many financial institutions' reluctance to renegotiate debts on the maturity of current loans, the need to refinance bank loans granted to Portuguese hotels (and resorts) in the 1990s, may eventually lead to a significant increase in distress sales over the next few months. This has not, as yet, been the case in Portugal, as many domestic banks prefer to work out alternative solutions with their debtors, avoiding at all costs sales at current market levels and consequently immediately booking the loss. Although domestic banks have endeavoured to monitor default risk, the continued poor operating performance of many hotels and resorts in 2010, may spark a change of attitude. Such assets, however, are not expected to be released onto the market, en masse, as this would only put market prices under greater pressure and force the recognition of higher write-downs.

On the other hand, current historically low interest rates will need to increase at some point and their gradual increase, together with higher spreads on bank loans (owing to higher country risk and banks' own higher funding costs) will, over the short/medium term entail a significant increase in the cost of capital that many hotel operations will probably not be able to meet.

Inded, the patience of the banks' and owners' capacity to resist will continue to be put to the test in 2011, with the inevitability of a further reduction of market prices. The relative extent of the reduction will be dependant on the volume and rate at which such assets are eventually brought onto the market and investors' expectations over future performance.

There are certainly several domestic and international investors with major funds at the ready who are keeping an eye on the situation and impatiently awaiting opportunities afforded by distress sales. These are split up into two groups: one (private equity) with long term objectives and another (vulture funds) on a merely opportunistic basis. Risk aversion remains high and selectivity is accordingly much higher than in the past, predominantly focusing on trophy hotels in Lisbon's prime zones, i.e. the right product and in the right location. Several such transactions will involve the acquisition of hotel assets from administrators or the direct purchase of bank loans, always heavily discounted.

Although new project developments will be highly limited over the short term, due to the imbalance between supply and demand in many areas, difficulty in securing bank loans and low values of property assets, the Portuguese market still provides investment opportunities in specific sectors such as boutique hotels in historic quarters of main cities, low cost hotels on outskirts of the major cities and provincial city centres and serviced apart hotels-tourism apartments in major urban centres.

Chapter in Colaboration with CTP





Torres Colombo | Source: Sonae Sierra, CGD, ING, Iberdrola

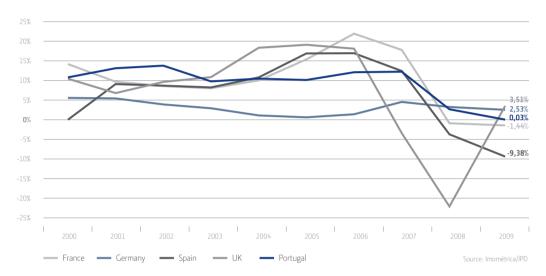
### 7. Imométrica / IPD Index

The Imométrica / IPD index monitors returns on direct property investment. The results of the index, in Portugal, were based on a sample of 810 properties with an end of 2009 value of around  $\in$  9.2 billion in which the retail sector accounts for around 51% of the sample at more than  $\in$  4.7 billion.

The latest data provided in the index indicate a continuation of the falling trend in total returns from property, visible, to a

certain extent, throughout the whole of Europe, including several of the main European markets. In general, property market returns continue to be heavily affected by higher yields, a brake on whose upwards trajectory was only recorded in 2009. The year 2008 results, in Portugal, already bear the hallmarks of the crisis, with a severe drop in total returns, from 12.2% to 2.7%. Although property, in Portugal, continued to generate losses at the end of 2009, at no more than 0.03%, they were still higher than in Spain and France.

### IPD Index - Total return



Over the longer term, the track record of the last 10 years as evidenced by this Index shows that property, in Portugal, is still a good option for investors. Annualised returns of 9.4% from property over the long term (10 years) is a highly competitive figure in comparison to the main European markets and only outperformed by the United Kingdom. These results validate the option to invest in Portugal, particularly for investors with a general interest in less volatile and consequently lower risk assets.

# TAX & LEGAL

### CHAPTER I Forms of Property Investment

### 1. ASSET DEALS

### 1.1. Ownership in Portugal

The concept of ownership, in Portugal, is in line with other continental legal systems. It is rooted in Roman law and the French Code Civil and encompasses not only "full ownership" but also other in rem rights relating to guarantees and purchases.

The "full ownership" concept is, therefore, coincident with the French concept of "propriété", the British concept of "freehold" and the German concept of "voll eigentum" and it is based on the full and exclusive right of use, fruition and disposal of the property.

Other lawfully established rights, in terms of property transactions, particularly include surface rights ("direito de superficie"). This is similar to the German "Erbaurecht" and comprises the right to build or maintain a construction on land which is part or fully owned by third parties, in perpetuity or temporarily, in which case surface ownership reverts to the owner of the land at the end of the respective period.

As opposed to other legal systems, the Portuguese system does not provide for fiduciary ownership which is only accepted in the Madeira Free Trade Zone, where the law permits the possibility of forming trusts (i.e. fiduciary management) for activities therein pursued.

Co-ownership of property is allowed under Portuguese law. Reference should also be made to the possibility of constituting a building or several buildings which are functionally interconnected under "horizontal property" regulations.

### 1.2. Formalities

The sale of (rural or urban) property in Portugal is formalised either in a deed, which is signed before a notary, or in a certified private document, signed in the presence of a lawyer, solicitor, chamber of commerce and industry, recorder or registrar. The sales contract must also comply with other formalities. The mentioned contract may only be signed after the officiator has examined and confirmed the documents required for its preparation, in accordance with the type of business to be entered into and the property to be conveyed, in addition to proof of payment of the respective fiscal obligations.

Documents required for the transfer of property ownership particularly include the need to produce a permit for the use of the property, or a building permit and proof that the property use permit application was submitted more than 50 days beforehand (unless the construction predates 7 August 1951, in which case these formalities do not apply).

### 1.3. Land registry

The purpose of the land registry is to provide information on a property's legal status, guaranteeing the lawfulness of the property transaction and confirming the presumption of the existence of a right to the property. The land registry is managed by the State. Based on these principles, the regulations currently in force in Portugal, require any facts determining the constitution, recognition, purchase or changes of *in rem* rights over property to be filed with the land registry. The absence of a record may imply a purchaser's lack of

protection vis-à-vis third parties in addition to the impossibility of transferring the property.

With the exception of special cases set out in law (e.g. provisional records of purchase which retain priority after their conversion into a definitive record of entry), pursuant to the principle of the priority of registration, the first recorded right is effective *vis-à-vis* third parties and takes precedence over the other incompatible rights of third parties even if such rights have been established prior to the date of registration.

### 1.4. Due diligence and preliminary contracts

Purchasers, either directly or using the services of consultants, are advised to check the commercial, legal, urban, environmental and fiscal status of any property they intend to acquire.

It is standard market practice, in such circumstances, for purchasers to commission a due diligence exercise on all of the mentioned areas, to confirm that the property in question is not subject to any encumbrance, costs/charges or limitations (whether or not registered with the respective Land Registry Office) or that any such impediments have been extinguished before or after the sale (e.g. preference rights or mortgages).

Prior to formalising a sale, it is also common practice for the parties to exchange contracts or similar preliminary agreements, comprising letters of intent, memorandums of understanding or heads of terms, binding to the extent required on a case by case basis.

If the parties require an immediately binding document, a promissory contract for the sale of the property in question is usually entered into, in which case the signing of the definitive sales contract is usually conditional upon the parties' compliance with several obligations (e.g. building, licensing and leasing of the property) or fulfilment of several conditions (e.g. issue of the respective property's use permit or a tenant's waiving of its lawfully established pre-emption right on the sale of the leased property). The parties may also agree to pay a part of the price on account. In such circumstances, in the event of a default by the promissory purchaser, the promissory vendor is entitled to keep any amounts already paid and in the event of a default by the promissory vendor, the promissory purchaser is entitled to receive twice the amount it has paid. The parties may also agree to subject the promissory contract to "specific performance" in the event of a default (i.e. obtaining a legal ruling in lieu of the defaulting party's negotiating statement).

To provide the promissory purchaser with the necessary legal protection, a provisional record of entry of the property purchase is usually filed at the Land Registry on the date upon which the promissory contract is signed.

### 1.5. Sales guarantees

Under the Portuguese Civil Code, a vendor is liable for any defects (flaws or lack of quality assured by the vendor or necessary for the purpose for which the property is intended) for a period of five years starting from the date of the vendor's delivery thereof.

The parties may waive this legal guarantee and specifically agree to sell the property on an "as is" basis.

The purchaser of the property is entitled to a 5-year legal guarantee covering any defects, *vis-à-vis* the property's contractor, whether or not it is a party to the construction contract. This will allow the purchaser to challenge the vendor and/or contractor directly in the event of any defect.

The property developer (unless developer and contractor are one and the same) is not liable for any property defects.

In the case of commercial transactions such as shopping centres, hotels and logistics parks, the vendor (whether or not also the property developer), usually provides the purchaser/investor with a guarantee covering defects for a specific period of time. Such guarantees usually specify different guarantee periods covering structural defects, leaks, technical equipment, façades, windows, roofs, etc. The guarantee may be subsidiary to the guarantees contractors must lawfully provide or be autonomous (the vendor being jointly liable with the contractor).

### 2. SHARE DEALS

### 2.1. Share deals

The main reasons for indirectly acquiring property through an equity stake in an investment vehicle owning such property are the fiscal implications.

The most common property investment vehicles are commercial companies (public limited companies ("sociedades anónimas") and limited liability companies by quotas ("sociedades por quotas")) and undertakings for collective investment of a contractual nature (property investment funds) or of a corporate nature (property investment companies).

### 2.2. Formalities

The acquisition of equity stakes in investment vehicles involves entering into a private sale contract in which the parties agree the price and other conditions relating to the transfer of the equity investments, usually including obligations or conditions specifically connected with the underlying property asset (e.g. the need to obtain a licence as a prerequisite for the purchase) and representations and warranties relating to the equity investments, the vehicle, the property assets underlying the vehicle, tax status, compliance with fiscal obligations, etc.

Except for limited liability companies by quotas ("sociedades por quotas"), in which the transfer of equity investments (quotas) must be set out in writing, the transfer of equity investments in public limited companies ("sociedades anónimas") or in undertakings for collective investment (shares or participation units) is not subject to any specific formal requirement. Formalities required for the effectiveness of the transfers also vary depending on the type of investment vehicle in question.

Therefore, in the case of limited liability companies by quotas ("sociedades por quotas"), transfers must be filed with the relevant commercial registry (1) and the company informed thereof, under penalty of the transfer being considered ineffective vis-à-vis the company. In the case of public limited companies ("sociedades anónimas") and undertakings for collective investment (whether or not under a corporate form), there is a difference between securities represented by certificates and by book-entries (i.e. book entry-securities) (2).

Nominative certificates are transferred by endorsement and upon request by the vendor to the company (as their corporate issuer) for the new ownership to be registered in the respective ledger. The transfer of bearer securities represented by certificates simply entails their surrender to the purchaser.

The transfer of book-entry securities is carried out through registration in the purchaser's account on the basis of a vendor's written instructions.

### 2.3. Due diligence and preliminary contracts

As stated in terms of asset deals for property purchases, in the case of share deals through the purchase of equity investments in the vehicle owning the property, a purchaser is also advised to commission a due diligence process to ascertain the commercial, financial, fiscal, corporate, legal and labour-related status (former or current employees) of the investment vehicle whose equity investments they intend to acquire and of its underlying assets (property and other).

The considerations on contracts and preliminary agreements for the sale of property assets set out in 1.4 above also apply here mutatis mutandis.

### 2.4. Sales guarantees

In the case of indirect acquisition of property ownership (share deal) a vendor usually accepts liability for a specific length of time for any infringement of its representations and warranties on the object of the sale and underlying assets. Such representations and warranties usually include special guarantees on the property, with a distinction being made between the type of defect and the relevant guarantee period. This special guarantee provided by the vendor may be autonomous or subsidiary to the general guarantees provided by the property's contractor.

<sup>(1)</sup> The objective of the Portuguese Commercial Registry is to afford legal protection to the corporate market and provide information on the legal status of companies.
(2) There may be changes in the system described if the securities have been deposited with a financial intermediary or are part of a centralised securities system.

### CHAPTER II Vehicles and Forms of Property Investment

It is common practice to set up vehicles for direct or indirect investment in property assets.

The following is an analysis of the most commonly found property investment vehicles in Portugal: (i) commercial companies, (ii) property investment funds and (iii) property investment companies.

### 3. COMMERCIAL COMPANIES

Most Portuguese commercial companies are public limited companies ("Sociedades Anónimas"-"SA") or limited liability companies by quotas ("Sociedades por Quotas" - "Lda") whose common denominator is the fact they are limited liability companies.

### 3.1. Public limited companies ("SA")

Public limited companies are the format usually adopted by larger Portuguese companies. Their equity capital is divided up into shares, with a minimum initial amount of € 50,000 and must, initially, have at least five shareholders. The possibility of forming an "SA" with a sole shareholder is permitted by law, provided that the sole shareholder is a commercial company.

As stated in 2.2 above, no particular format is required for share transfers although they may be subject to restrictions. Another peculiarity is the fact that information on the respective shareholders is not usually public thus ensuring a measure of confidentiality on the owners of the respective equity capital.

### 3.2. Limited liability companies by quotas ("Lda")

Limited liability companies by quotas are by far the type of companies mostly found in Portugal. They correspond to a standard small and medium-sized company structure owing to their lower initial capital requirements and simpler operating structure, enabling their founding partners to exercise greater control.

As described in section 2.2 above, quotas must be transferred in writing and officially registered. Equity capital is divided into quotas, with a minimum initial amount of € 5,000 and, initially, at least two quota-holders. The law allows such companies, which are subject to specific conditions set out in the law, to be formed by a sole quota-holder in which case the corporate name must bear the expression "sociedade unipessoal por quotas" ("sole quota-holder limited liability companies by



Justice Campus | Source: Norfin

quotas"). Information on the name of the respective quotaholders and the amount of their respective quotas is filed with the commercial registry. This information is publicly available.

### 4. PROPERTY INVESTMENT FUNDS

The fact that property investment funds ("FIIs") have been one of the most common property investment vehicles in the Portuguese market over the last few years is essentially due to the favourable fiscal regulations which apply to them.

FIIs are undivided aggregations of assets under the joint ownership of natural or legal persons, referred to as the "unitholders", who may not, under any circumstance, be held liable for the debts of such funds or of entities which are liable for their management.

FIIs are divided up into identical investment units (3) which may be in book-entry form or represented by certificates.

### 4.1. Types of Flls

FIIs may be open-ended, closed end (public or privately subscribed for (4)) or mixed, depending on whether the number of investment units is variable, fixed or variable and fixed, respectively. Closed end FIIs (privately subscribed for) are the most commonly used investment funds by investors to promote their property investments in Portugal.

### 4.2. Management of FIIs

FIIs are a type of undertaking for collective investment of a contractual nature (i.e. they are not corporate entities) and their management must therefore be performed by third parties. FIIs may be managed by property or securities investment fund managers with registered office and effective management in Portugal or by credit institutions (e.g. banks, leasing and investment companies).

Fund managers, in performing their duties, must act in the exclusive interest of their unit-holders and are, in general, responsible for all acts and operations considered to be necessary for the good management of the FII, in accordance with criteria relating to diligence and professional competency.

Property fund managers should, inter alia, in acting for the account of the FII, select the assets (e.g. properties) which comprise the FII's portfolio, and enter into all business arrangements, undertaking all acts required for the purchase and management of the FII's assets. Thus, it is the fund manager who carries out the FII's activity, for and on behalf of the FIL.

Reference should also be made to the fact that the formation of fund management companies is a relatively complex procedure requiring the approval of the Bank of Portugal. Fund management companies come under the supervision of both the Bank of Portugal and the Portuguese Securities Market Commission (CMVM). Their activity must comply with certain rules, in addition to shareholders' equity requirements.

Property investors, in most cases, use existing investment fund managers who specialise in setting up and managing FIIs. The relationships between investors (unit-holders) and fund managers are regulated by the **FII**'s management regulations and any other necessary contractual instruments.

### 4.3. Depositary

The securities comprising the assets of the FII should be entrusted to a single depositary, which should be a credit institution. The depositary should have its registered office in Portugal or, if based in another Member State of the European Community, should operate through a branch in Portugal. The fund management company and depositary are jointly and severally liable to unit-holders for compliance with the obligations set out in the law and in the Fil's management regulations.

### 4.4. Activity

FIIs may perform the following activities relating to property: (a) purchases of property for rental or other forms of use, for consideration; (b) purchases of property for resale; (c) purchases of other rights over properties with a view to obtaining an economic profit; and (d) performance of building projects and property refurbishments, obtaining an economic profit for consideration or through resale.

FIIs may not: (a) encumber their assets in any way, except for financing purposes, within lawfully defined limits; (b) grant loans or provide guarantees; (c) enter into promissory agreements on the sale of properties which are not owned by the FII yet, except for promissory sales agreements on property coming under the aegis of construction projects.

The assets of an FII may comprise property, liquidity and shareholdings in property companies, whose composition should comply with the rules and limits defined for each type of asset.

The FII's properties should be valued at least once every two years by a minimum of two independent property appraisers and under other lawfully defined circumstances (e.g. prior to the performance of building projects and property acquisitions and sales). There are specific rules on the valuation of FII's property assets (valuation criteria, etc.) particularly as regards development projects comprised therein.

The management regulations of closed end FIIs should define the rules for calling unit-holders' meetings and their respective modus operandi. Any omissions or insufficiencies are governed by the rules on public limited liability companies.

### 4.5. Incorporation

The incorporation of an **FII** is subject to the CMVM's consent and is contingent upon the submission of an application from the fund manager, together with the draft management regulations, contracts to be entered into with the depositary and documents certifying the acceptance of functions of all of the entities involved in the FII's activity.

<sup>[3]</sup> Investment units are securities without a nominal value which provide owners (unit-holders) with the right to an ideal share of the fund's assets.

<sup>(4)</sup> Depending on whether the distribution of investment units in a property investment fund is made by means of a public or private offering pursuant to the Portuguese Securities Code

A **FII** must, within one year, from its inception, have assets worth at least  $\le$  5 million under management, under penalty of the CMVM's entitlement to revoke its authorisation to set up the **FII**.

Management regulations, which must be produced and kept up-to-date by the fund manager, must set out the particulars on the **FII**, fund managers and depositary in addition to the rights and duties of unit-holders, fund managers and depositary, the **FII**'s investment policy and the terms governing the winding up of the **FII**.

The duration of a closed end **FII** may be specified or unspecified. Although the duration of a closed end **FII** may not exceed 10 years, it may be extended on one or more occasions if certain conditions are met.

### 4.6. Charges/Fees

Various costs/charges and expenses (in addition to those involved in the property deals in question) are payable on the incorporation and management of **FIIs**. Special reference should be made to the following: (a) charges payable to the CMVM; (b) commissions payable to the fund manager and depositary; (c) fees payable for the appraisal of property as required by law; and (d) fees payable for the audits on the **FII**'s accounts required by law.

### 5. PROPERTY INVESTMENT COMPANIES

As in most other European countries, the possibility of forming **FIIs** with a corporate form was recently enacted in Portuguese legislation by Decree Law 71/2010 of 18 June, under the name property investment companies (*"Sociedades de Investimento Imobiliário"* - "**SIIMO"**).

### 5.1. Types of SIIMOs

SIIMOs are collective investment undertakings with their own legal personality which may take the form of SICAVIs (public limited companies - SAs - with variable capital) or SICAFIs (public limited companies - SAs - with fixed capital), whose property assets they own and manage (self-management) or which are managed by a contracted third party (outside management), always acting independently, on a fiduciary basis, in the exclusive interest of shareholders.

**SICAVIs** and **SICAFIs** are subject to (i) the regulations on open-ended and closed end property investment funds, respectively and (ii) to the extent is not incompatible with the nature and object of **SIIMOs**, the regulations set out in the Portuguese Companies Code ("Código das Sociedades Comerciais") and other Portuguese corporate legislation.

A **SIIMO** must have a minimum initial share capital of € 375,000, divided into identical nominative shares with no nominal value.

A **SICAVI**'s share capital is equivalent, at any point in time, to the net global value of its assets, which constantly changes in line with the number of redemptions and subscriptions, as in the case of open-ended **FIIs**. The **SICAFI**'s share capital is equivalent to the amount defined at the time of its incorporation and varies in line with any increases in or reductions of share capital, as in the case of a closed end **FII**.



Prada Store, Av. Liberdade | Source: Cushman & Wakefield

As in the case of fund managers of **FIIs**, **SIIMOs** should ensure that the global net value of its assets does not fall below  $\in 5$  million.

### 5.2. Management of SIIMOs

Unlike **FIIs**, in which there is an inevitable separation between the fund manager and investors (unit-holders) and the fund manager manages the fund on a contractual basis (i.e. based on the **FII**'s management regulations upon which the fund manager's mandate is based), the risks split in the case of **SIIMOs** is not necessary and shareholders may jointly be investors (as shareholders) and managers of a **SIIMO**'s assets (self-management) or, alternatively, appoint a property investment fund manager to perform the said function (outside management).

The main advantage afforded by a **SIIMO** on this level consists on the possibility of self-management, allowing investors (shareholders) to be actively involved in its operation.

**SIIMO**'s activity is subject to the dual supervision of the Bank of Portugal and CMVM (already applicable to **FII**'s managers in their role as financial intermediaries).

### 5.3. Formation of SIIMOs

Reference should, lastly, be made to the fact that the rules governing the formation of **FIIs** apply, *mutatis mutandis*, to the formation of SIIMOs as well as the general rules of the Portuguese Companies Code (*"Código das Sociedades Comerciais"*) on the formalities required for the formation of commercial companies when these do not clash with the **FIIs** regulations and the nature and object of a **SIIMO**.

The date of the record of entry of the **SIIMO**'s respective deed of incorporation at the Companies Registry is considered to be its formation date.

# CHAPTER III Tax Matters

#### 6 PROPERTY PURCHASES

### 6.1. Real Estate Transfer Tax ("IMT") and Stamp Tax

Property purchases are generally subject to **IMT** at a rate of 6.5% on urban property or land for construction and 5% on rural property, levied on the respective price or tax registered value, whichever is higher. In the case of residential property, there is a reduction in the applicable rate which may vary between 0% and 6%. The applicable **IMT** rate is always 8% whenever the purchaser is resident in a country, territory or region benefiting from clearly more favourable fiscal regulations, as set out in the list approved by Ministerial Order 150/2004 of 13 February ("**Listed Tax Haven**").

Stamp Tax at 0.8% is also payable on property purchases, levied on the same amount subject to **IMT** unless exemption from the applicable VAT has been waived, in which case Stamp Tax is not due, although IMT continues to apply.

In general, both taxes must be paid by the purchaser to the tax authorities before signing the public property conveyance deed. To this end, the acquirer must file a specific form (*"Declaração Modelo 1 - IMT"*) with the tax authorities, either in a local tax office or by electronic means (the tax must be paid on the day the form is filed, or on the following business day). After payment, the IMT and Stamp Tax assessments are valid for two years.

#### 6 > VAT

In general, the transfer and lease of property are exempt from VAT.

However, as the mentioned exemption is incomplete, i.e. it does not entitle the vendor of the property to deduct the input VAT borne regarding the relevant property, the vendor may waive it. In such cases, VAT will be charged on the property transfer, at the standard rate of 21%.

Waiving the VAT exemption on property transfers may, in certain cases, be advantageous, as a vendor waiving said exemption may deduct the input VAT included in the property's price or construction cost, in addition to any other input VAT borne within its activity.

Under Decree Law 21/2007 of 29 January, the VAT exemption on property transactions may only be waived when certain conditions are met. The most relevant are listed below:

### Objective conditions:

- (a) The property should be qualified as "urban" property (or autonomous units thereof) or, in the case of transfers, as land for construction:
- (b) The contract should refer to the whole of the property or its autonomous units (and not solely to one of its parts);
- (c) The property should be used by its purchaser/tenant for the performance of activities conferring a full or partial right to deduct the input VAT borne;
- (d) In the case of leased property, the amount of the annual rent should be equal to or more than 1/25th of the property's acquisition price or construction costs.

The VAT exemption cannot be waived if the vendor/landlord or purchaser/tenant is a non-resident entity without a permanent establishment in Portugal, as such an entity has no obligation to have accounts organised in accordance with the Portuguese

accounting provisions as established by the IRS (personal income tax) Code or IRC (corporate income tax) Code. However, according to the opinion of some local tax offices, the mentioned condition is considered to be met whenever a non-resident entity decides to have accounts organised in accordance with the Portuguese accounting provisions, even if it is under no obligation to do so.

To waive the VAT exemption, a vendor/landlord should arrange for the issue of a certificate by the tax authorities, confirming that the parties involved in the transaction have expressed their intention to waive the applicable VAT exemption and declare that the necessary conditions have been fulfilled.

VAT due on the sale of property, should be self-assessed by the purchaser (self-assessment mechanism) in the tax period corresponding to the date upon which the VAT exemption waiver becomes effective (which is the date upon which the respective definitive sale contract is entered into).

In the case of leased property, landlords should assess, charge and deliver to the tax authorities the VAT due on the rents payable by tenants.

Input VAT borne by the vendor/landlord regarding the property may be deducted in the tax period in which the VAT exemption waiving is considered to be effective or in the following tax period, within 4 years from the date of the respective invoices.

VAT paid on the construction of a property by a taxpayer who performs a regular construction activity involving property sales or rentals may be deducted within a period of 8 years from the date of the respective invoices, provided that the taxpayer proves that the construction of the referred property has lasted for more than four years.

### 7. PROPERTY OWNERSHIP

### 7.1. Property Tax ("IMI")

**IMI** is an annual tax levied on a property's taxable value and is payable by property owners on 31 December of each year. **IMI** is generally paid in two instalments (April and September).

**IMI** rates currently vary between 0.2% and 0.4% for urban property and land for construction, except for property which has not been valued yet under the terms of the **IMI** Code, upon which rates of between 0.4% and 0.7% are charged. The rate on rural property is 0.8%. These rates are annually increased to twice their amount in the case of urban property which has been left vacant for more than a year and three times for buildings in a state of ruin. In addition, the **IMI** rate on property which is owned by residents in a Listed Tax Haven is 1%. This rises to 2% if such buildings have been unoccupied for longer than a year or are in a state of ruin.

### 7.2. Special Contribution

A special tax called Special Contribution ("Contribuição Especial") may apply in the event of new property developments, which purpose is to tax the increase of the value of plots of land for construction, as well as of land resulting from demolitions, arising from major infrastructure public works carried out mainly in Lisbon, Porto and their outskirts.

The applicable rate usually varies between 20% and 30%, depending on the building's exact location and is charged on the increase in value

referred to above. The Special Contribution is due by the individual or entity in whose name the respective building permit has been issued.

## 7.3. Tax on income from property obtained in Portugal by non-residents

Income from property obtained in Portugal by non-resident individuals or corporate entities is taxable at a special rate of 15% (levied on the amount of the rent collected, minus maintenance and upkeep expenses incurred on the said property, including IMI). Such income when paid by entities which must have an organised accounts system is subject to a 16.5% withholding as a payment on account of the final tax due.

Non-resident investors must file with the Portuguese tax authorities a declaration of the start of activities (prior to initiating the property rental activity), as well as their respective income tax returns. Such returns, in the case of individuals should be filed in April or May of the year following the year to which they refer, depending on whether they are filed on paper or in electronic format. In the case of corporate entities, the returns should be filed in May of the year following the one to which they refer.

### 7.4. VAT

Property rentals are exempt from VAT. The VAT exemption may, however, be waived provided that the necessary conditions are met (see section 6.2. above).

#### 8. SALE OF PROPERTY

Any capital gains obtained by non-residents on the sale of property in Portugal are, in general, subject to taxation at a rate of 25%, levied on the difference (when positive) between (i) the acquisition value of the property, adjusted by coefficients set annually by the government, plus the costs/charges incurred on property improvements over the last five years and the necessary expenses incurred on the sale of the property, and (ii) the respective transfer value, which tends to be the same as the sale price.

Non-resident individuals should declare such capital gains in the same terms and within the periods referred to for income from property. Corporate investors should, as a general rule, declare the capital gains made within 30 days from the date of transfer.

Such capital gains, may, however be excluded from taxation in Portugal in the event a double tax agreement applies.

As stated in 6.2 above, property sales are generally exempt from VAT. The applicable VAT exemption may, however, be waived if the necessary conditions are met.

### 9. INVESTMENT STRUCTURES

Investments can be made in property located in Portugal through asset deals, with the tax implications referred to in section 6.1 above, or in the form of a share deal which, depending on the specifics of the case, may be a better option from a tax point of view.

Such alternative share deal structures particularly include (i) the use of a company resident in Portugal ("SPV"), and (ii) the use of a property investment fund (which may be a company or not).

### 9.1. SPVs

Regarding the use of **SPVs**, the purchase of any property already owned by an **SPV** will not have any tax implications, provided that the SPV is a public limited liability company. If the property has to be acquired by the **SPV**, the said purchase will have the same fiscal implications as in 6.1 above.

Income from property obtained by an **SPV** is subject to IRC, at the standard rate of 25%, plus a state surcharge of 2.5% on taxable profit of more than  $\in$  2 million. A municipal surcharge of up to 1.5% may also be due. The **SPV** may generally deduct all costs paid on the property, including depreciation, IMI and any interest expenses on the financing of the respective purchase and/or construction for **IRC** purposes.

IRC is also payable on capital gains on the sale of property owned by an SPV, at the above-mentioned rates, although reinvestment regulations relating to the disposal of tangible fixed assets and investment properties may apply. The said regulations allow an SPV to deduct 50% of the positive difference between capital gains and capital losses obtained in the relevant tax year from the transfer for consideration of tangible fixed assets, bearer biological assets and investment properties held for a minimum period of one year if the proceeds from the transfer are reinvested in similar assets in the tax year before the transfer, in the tax year of the transfer, or in the following two tax years.

Dividends paid to non-resident shareholders by an **SPV** are subject to withholding tax in Portugal, at a flat rate of 21% for individuals and 20% for corporate entities (both rates may be reduced if a double tax treaty applies). If such shareholders are companies resident in other EU Member States, the said dividends are exempt from tax in Portugal, provided that the shares held represent at least 10% of the **SPV**'s share capital or have an acquisition value of at least € 20 million and are held for at least one year.

Capital gains obtained by non-residents on the disposal of shares in an **SPV** are exempt from tax in Portugal, except if at least 50% of the **SPV**'s assets are comprised of property assets. In this case, the capital gains will be taxed at 25%, unless no taxation is due in Portugal under the applicable double tax agreement.

### 9.2. FII / SIIMOs

The acquisition of property by **FIIs** is, as a general rule, subject to **IMT** and Stamp Tax, except for open-ended **FIIs**, which are exempt from **IMT**.

Open-ended FIIs are also exempt from IMI.

The main features of the special tax regime applicable to income obtained by **FIIs** are as follows:

- (a) Income from property is taxed at an autonomous rate of 20%, levied on income net of maintenance and upkeep charges/fees, as well as the payment of any **IMI** (**FIIs** may not deduct neither the depreciation of the property for tax purposes, nor the interest expenses on the financing of the purchase or construction thereof). Any tax due by an **FII** must be paid by the respective management entity by the end of April of the year after the one to which it refers; and
- (b) Capital gains on property are taxed autonomously at 25%, levied on 50% of the difference (when positive) between capital gains and losses obtained in the relevant tax year, with the management entity paying the respective tax up to the end of April of the year after the one to which it refers.

Income paid to non-resident unit holders by **FIIs** is not subject to taxation in Portugal.

The above-mentioned special rules also apply to **SIIMOs** (the **IMT** and **IMI** are exemptions that are only applicable to **SICAVIs**).

# RESIDENT COMPANY vs PROPERTY INVESTMENT FUNDS / SIIMOs

	Acquisition	Activity	Income Distribution (Non Resident Investors)	Transfer - Taxation in Portugal (Non Resident Investors)
SPV	Acquisition of property:  • IMT: 5% or 6.5% (0% to 6% for residential property)  • Stamp Tax: 0.8% (not due if the VAT exemption is waived)  • VAT: exempt (the exemption may be waived)  Acquisition of SPV (owning the properties): not subject to taxation assuming that the SPV is a public limited liability company	IRC: 25% (including capital-gains from the transfer of properties)  Derrama Estadual: 2.5% on the taxable profit exceeding € 2,000,000  Derrama Municipal: up to 1.5% on the taxable profit  IMI: • Urban: 0.2% to 0.4%  • Rustic: 0.8%	Individuals: 21%  Corporate entities: 20% (exempt if the conditions for the application of the Parent/ Subsidiary Directive are fulfilled)	Transfer of the SPV shares:  • General rule: exempt  • Exception: if at least 50% of the SPV's assets are comprised of property assets, taxation will be due at a rate of 25% (unless no taxation is due under the applicable DTA)
Closed End FII and SIIMO (SICAFI)	Acquisition of property:  • IMT: 5% or 6.5% (0% to 6% for residential property)  • Stamp Tax: 0.8% (not due if the VAT exemption is waived)  • VAT: exempt (the exemption may be waived)	• Rents (deducted of maintenance costs and IMI) - 20% • Capital-gains from the transfer or properties - 12.5%  IMI: • Urban: 0.2% a 0.4% • Rustic: 0.8%	IRC: exempt	Transfer of units in the FII / shares in the SICAFI: exempt
Open-Ended FII and SIIMO (SICAVI)	Acquisition of property:  IMT: exempt  Stamp Tax: 0.8% (not due if the VAT exemption is waived)  VAT: exempt (the exemption may be waived)	IRC:  • Rents (deducted of maintenance costs and IMI) - 20%  • Capital-gains from the transfer or properties - 12.5%  IMI: exempt	IRC: exempt	Transfer of units in the FII / shares in the SICAVI: exempt

### CHAPTER IV Property Finance

### 10. MORTGAGE-BACKED LOANS

Mortgage-backed loan contracts are one of the most commonly used means of financing property projects in Portugal.

Bank loans, i.e. contracts in which the lender is a credit institution, must always be set out in writing.

Notwithstanding the fact that the law permits total freedom of form regarding commercial loan contracts (except for the definition of interest rates, which must always be set out in writing), in practical terms they are usually set out in writing.

#### 11. MORTGAGES

A mortgage is *in rem* guarantee (unlike a personal guarantee as described below). It entitles the creditor to enforce its rights against a property with priority over other creditors of the owner of the property who do not enjoy any special privilege or priority in terms of registration. Unlike a pledge, it does not imply the dispossession of assets provided as guarantees, which must always remain in possession of their owner.

The following assets and rights may be mortgaged: (a) property ownership; (b) surface rights ("direito de superficie") and (c) a share in an item or a shared right (e.g., an undivided share of the co-ownership of assets).

Mortgages accompany the changes affecting the asset. Accordingly, and without prejudice to the rights of third parties, a mortgage will be automatically extended to all improvements and constructions realised on property provided as a guarantee.

Mortgages on immovable assets may be formalised or amended in the form of a public deed or certified private document, which should be filed with the relevant land registry and which record of entry is a condition for the guarantee's existence and effectiveness. The land registry is, therefore, an essential part of the procedure for setting up a guarantee. In addition to ensuring the effectiveness thereof, it establishes the extent to which it takes preference over other similar guarantee instruments on the same asset.

The determination of the maximum amount to be guaranteed by the mortgage (including the amount of principal, interest and costs associated with its execution and foreclosure) is mandatory, as well as filing it with the land registry. With regard to interest (both loan interest and default interest), pursuant to the Portuguese Civil Code, a mortgage may only cover up to three years of interest.

### 12. OTHER COMMON GUARANTEES

The financing of a property project always entails the borrower granting a complete "security package" comprising *in rem* and personal guarantees to ensure the repayment of the loan principal, respective interest and default interest thereon under the terms of the loan contract.

### 12.1. Pledge agreement

As in the case of a mortgage, a pledge is an *in rem* guarantee giving creditors preferred payment status over other creditors, for the value of a specific movable asset or amount of other credits or asset rights which cannot be mortgaged. Excluding exceptional cases, the creation of a pledge always implies surrendering the asset to the creditor, who then becomes the guardian and administrator of the pledged asset, as set out in law.

### 12.1.1. Pledge over shareholdings

A lender will usually require investing partners owning the full amount of the share capital of the borrowing property investor to set up a pledge over all its shareholdings.

In such contracts it is generally agreed that, if the debtor defaults on the loan contract, the creditor is immediately authorised to exercise all corporate rights on the mentioned shareholdings, including the right to receive the respective dividends and participate and make decisions at general meetings of shareholders.

To provide creditors with extra comfort, partners are usually asked to confer irrevocable powers of attorney to the said creditor, to enable it, in the event of a capital increase, to immediately pledge the new shares on its behalf and also, in the event of breach of contract, to enable the creditor to dispose of the mentioned shareholdings in an extra-judicial sale, setting the respective proceeds against the debt.

A pledge agreement on shareholdings should be in the legally required format and comply with the terms and conditions set out under Portuguese law and in the company's articles of association for the transfer thereof in an inter vivos act. In the case of a pledge over shares, although the form of the pledge agreement is usually free, the formalities prescribed for said purpose in the Portuguese Securities Code ("Código de Valores Mobiliários") should be complied with. These vary depending on whether the shares are book-entry shares or represented by certificates, in which case there are different formalities to be complied with depending on whether such shares are nominative or bearer (5).

Despite not always being legally required, a pledge agreement is usually set out in writing with a creditor requesting, as a minimum, that the signatures of the partners who are parties to the contract be certified by a notary. The fulfilment of this formality provides creditors with a higher level of protection and provides evidence to be given in court in the event of the judicial execution of this guarantee, allowing the contract to be enforced (once the other legal requirements have been met).

### 12.1.2. Pledge over credit rights

In addition to pledges over a debtor's shareholdings, creditors may also require investors to provide the same guarantee over all credit rights to which they are entitled, such as those deriving from rental use of shop contracts, bank accounts, insurance

policies, construction or property development contracts. Basically, a creditor may demand, as a guarantee, a pledge over the credit rights to which debtors are entitled and which represent the main source of income from the financed project.

### 12.1.3. Financial pledges

Pledges may be qualified as financial guarantees if certain conditions have been met (e.g. the contract must have been entered into using a media susceptible to proof in the form of a written document, between credit institutions and legal entities, involving cash or financial securities).

This type of contract has the following features (which are forbidden in the case of civil pledges): (a) the beneficiary of the guarantee may dispose of the pledged object, i.e. it may alienate or encumber the pledged assets as if it were the owner, although it must return an object equivalent to the original to the provider, when the contractual obligations have been met; and (b) if the guarantee is called in, the beneficiary thereof may execute it making the assets given in guarantee its own (provided that the parties: (i) have made suitable contractual provision for this possibility; and (ii) are in agreement over the valuation of the financial securities).

#### 12.2. Sureties

A third party is often requested to provide surety (usually the debtor's partners or, if applicable, the parent company of the group to which it belongs) on the creditor's behalf.

As it is a personal guarantee, the guarantor, whose personal assets guarantee that the creditor's credit rights are met, is liable before the creditor. Unless the parties agree otherwise, the full amount of the guarantor's assets will be held accountable for compliance with the obligations undertaken by the debtor.

The standard practice is for such contracts to be set out in writing and, as a minimum, that the guarantor's signature be certified by a notary (please see the last paragraph of 12.1.1 above).



Convento dos Inglesinhos | Source: Chamartín Imobiliária

### 12.3. Stamp Tax

It should be noted that financing and guarantees granted in Portugal or herein presented for any legal purposes are subject to Portuguese Stamp Tax  $^{(6)}$ , at the following rates levied on the amount financed or the maximum amount of each guarantee, as the case may be: (i) 0.04% for each month or part thereof for finance or guarantees with a maturity of less than one year; (ii) 0.5% for finance or guarantees with a maturity of one year or more and less than five years; (iii) 0.6% for guarantees without any time limit and for finance or guarantees for a period of five years or more; and (iv) 0.04% on the average outstanding monthly balance of finance in the form of a current account, bank overdraft or any other form whose period of use has not been specified or cannot be ascertained.

No Stamp Tax is due on a guarantee which is accessory to and granted simultaneously with a contract already subject to Stamp Tax (such as a loan contract).

(6) Under the terms of the Portuguese Stamp Tax Code not only guarantees contained in documents signed in Portugal but also guarantees granted to resident entities in Portugal are considered to have been granted in Portugal.



Forum Algarve | Source: Multi Development

# CHAPTER V Urban Planning and Urban Licensing

### 13. INTRODUCTION

Property project developments in Portugal must always abide by the rules and legal standards relating to urban planning and administrative licensing of projects.

The main source for Portuguese urban planning law is legislation enacted by the State in the form of laws and decree-laws, which are approved by the Parliament and the Government, owing to the absence of administrative regions (there are currently only two regions: the autonomous regions of Madeira and the Azores). The main statutes in which urbanisation standards are set out are, in addition to the Constitution of the Portuguese Republic ("Constituição da República Portuguesa") - which defines the principles and tasks related with urban planning and territorial development - LBPOTU (Basic Law on Territorial and Urban Planning Policies - "Lei de Bases da Política e do Ordenamento do Território e do Urbanismo"), RJIGT (Territorial Planning Instruments Regulations - "Regime Jurídico dos Instrumentos de Gestão Territorial") and RJUE (Urbanisation and Building Regulations - "Regime Jurídico da Urbanização e da Edificação").

Portuguese municipalities however, perform a fundamental role both in terms of urban planning and property project licensing.

### 14. URBAN PLANNING IN PORTUGAL

Urban planning in Portugal is regulated by several principles, in particular, the principle of urban development in accordance with the relevant plans, i.e. in accordance with objectives set out by the relevant public authorities referred to in the plans, and the principle of standardised plans. The plans set out the principles and rules governing the occupation, use and transformation of the land and therefore play a central role in terms of property projects development.

The territorial management system comprises a series of territorial management instruments ("instrumentos de gestão territorial") designed to achieve specific interests and objectives, which interact and are coordinated with each other.

**RJIGT** is the main urban planning law in Portugal. It defines the coordination system between the national, regional and municipal scopes of the territorial management system, the general regulations covering land use and the production, execution and assessment of territorial management instruments.

The territorial management instruments provided for by the **RJIGT** are classified as having a national, regional or municipal scope, depending on the interests involved. Territorial management instruments are divided as follows:

(i) strategic territorial development instruments (addressed to other public entities which have to develop the plan), such as the **PNPOT** (National Territorial Planning Policy Programme - "Programa Nacional da Política do Ordenamento do Território"), **PROT** (Regional Territorial Planning Schemes - "Planos Regionais de Ordenamento do Território") and Inter-municipal Plans ("Planos Intermunicipais");

(ii) sectorial planning instruments;

(iii) special planning instruments; and

(iv) territorial planning instruments such as **PMOTs** (Municipal Territorial Planning Schemes - "Planos Municipais de Ordenamento do Território")

**PMOTs** define the land use system via its classification (based on the distinction between rural and urban land) and qualification (regulating and defining the use thereof and, when admissible, the possibility of building thereon). These are fundamental instruments designed to implement urban planning policies at a local level. **PMOTs** are approved by municipalities and are split up into **PDMs** (Municipal Master Plans - "Planos Directores Municipais"), **PUs** (Urbanisation Plans - "Planos de Urbanização") and **PPs** (Detailed Plans - "Planos de Pormenor").

PDMs encompass the whole of the municipal district and provide a synopsis of the local planning and development strategy, defining occupation parameters and land use. PUs implement territorial and urban planning policies and may encompass any area included in an urban PDM perimeter as well as rural land complementary to an urban perimeter and areas set aside for urban use. PPs develop and implement proposals for the occupation of any area within the municipal district, with the RJIGT providing for specific modalities of (i) PPs for interventions in rural spaces, (ii) PPs for urban refurbishment and (iii) PPs for protection purposes.

It should be noted that, after certain requirements have been met, **PPs** may be filed with the land registry and comprise the basis for a land transformation (e.g. dividing the property into plots of land) without the need for the approval of any specific allotment operation ("operação urbanística de loteamento").

The development of a property project must, therefore, comply with the applicable territorial management instruments, particularly **special plans** ("Planos Especiais") and **PMOTs**. A case by case analysis of the correct application of the applicable urban regulations, taking into account the multiplicity of criteria and existing interpretations, must always be made.

### 15. LICENSING OF PROPERTY PROJECTS

The licensing (in the broader sense) of property projects is generally designed to assess whether the intentions of the interested party in terms of urban planning are in accordance with the applicable legal regulations and applicable territorial management instruments.

The municipalities are responsible for preliminary control of urban planning projects, including construction and use of buildings, and allotment of land. This does not preclude the need for the involvement of other entities whose opinion may, in many cases, be binding in terms of project licensing. Municipalities are competent to approve municipal urban planning and building regulations, in addition to regulations on the payment of taxes/charges on the performance of urban operations.

The execution of urban planning operations must generally be examined in advance and may require licensing ("licenciamento"), advance notice ("comunicação prévia") or use permits ("autorização de utilização").

The **RJUE** provide a list of urban operations which require licensing ("licenciamento") and advance notice ("comunicação prévia"), respectively. Other non-listed urban operations which are not exempt from "preliminary control" require advance notice ("comunicação prévia"), which is considered the supplementary form of "preliminary control".

The **RJUE** also lists those operations which are less relevant and have less of an impact in terms of urban planning. They are exempt from licensing or advance notice requirements.

Urban planning operations for which advance notice ("comunicação prévia") must be provided are usually either less relevant in urban planning terms than those which require licensing ("licenciamento") or are performed in areas covered by an allotment operation ("operação de loteamento") or by a PP. Advance notice procedures are simpler and faster than licensing procedures.

As regards urban planning operations subject to licensing ("licenciamento"), the RJUE list the following circumstances in which licensing applications will be rejected: (i) any infringement of **PMOTs** or **Special Plans**, preventative measures, administrative rights of way, restriction of "public interest" status ("restrição de utilidade pública") or any other applicable legal and regulatory provisions, (ii) in the event of the existence of a declaration of "public interest" for the expropriation of property for which a licensing application has been submitted, (iii) the existence of a negative opinion or rejection of an approval or authorisation by any entity consulted whose decision is binding upon municipal bodies, and (iv) depending on the request, a rejection may also be based on the fact that the urban operation may have a negative effect on archaeological, historic or natural or landscape, natural or built heritage, cause an unacceptable burden on existing infrastructures or general services, or require the municipality to build or maintain any facilities, to perform works or to provide unplanned services such as streets, water distribution, electricity or sanitation networks.

Regarding the communication relating to **urban planning operations in relation to which advance notice** ("comunicação prévia") must be provided, the advance notice is rejected when the project is shown to infringe the applicable legal and regulatory provisions set out in the **PMOT**,

any existing permit ("licença") or advance communication ("comunicação prévia") on an allotment operation ("operação de loteamento"), technical building standards in force, or the terms of any existing advance information provided ("informação prévia").

Licences ("licenças") or acceptances of advance notice ("comunicação prévia") generally expire if the acts subsequently required for the performance of the urban project have not been performed within the period established by law.

Reference should also be made to the fact that an interested party may submit a request for advance information ("pedido de informação prévia" - "PIP") on the feasibility of a specific urban project as well as to any legal or regulatory constraints. This highly relevant mechanism is widely used in the field of property transactions.

An interested party may request the municipality to provide advance information ("pedido de informação prévia") on diverse aspects of a specific urban project it is interested in performing, such as volumetry, eave height, number of apartments or an estimate of urban planning costs/charges. The municipality has a term to consider the request on the said advance information and its decision is binding on the competent entities in respect of the licensing or the advance notice decision to which it refers. The effects of such information are valid for the a period of one year.

Reference should also be made to the fact that after the building has been completed a property use permit ("autorização de utilização") for the buildings or condominium units thereof must be obtained. The purpose of this authorisation is to verify the urban project's completion and conformity with approved plans and licensing or advance notice conditions. The property use permit ("autorização de utilização") certifies the use which may be given to the building or condominium units thereof and is of the utmost importance on account of the reference made in 1.2 above.

Reference should, lastly, be made to the fact that the latest **RJUE** amendment approved by Decree Law 26/2010 of 31 March 2010, enacted exceptional regulations extending the periods for the submission of applications for the issue of urban operations and works performance permits.



Logistics Platform in Azambuja | Source: Cushman & Wakefield

### CHAPTER VI Special Licensing

### 16. COMMERCIAL LICENSING

Decree Law 21/2009 of 19 January 2009 defines the authorisation process governing the installation and modification of commercial retail establishments ("estabelecimentos comerciais") and commercial complexes ("conjuntos comerciais") in Portugal, usually referred to as "commercial licensing".

### 16.1. Scope

The following commercial retail establishments and commercial complexes are covered by commercial licensing regulations:
(a) commercial establishments, either standalone or operating in commercial complexes, with a sales area of 2,000 sqm or more;
(b) commercial establishments, either standalone or operating in commercial complexes, regardless of the sales area, belonging to a company using one or more trade names or which are part of a group with an aggregate nationwide sales area of 30,000 sqm or more; (c) commercial complexes with a GLA (gross lettable area) of 8,000 sqm or more; and (d) commercial retail establishments and commercial complexes mentioned in the preceding sub-paragraphs which have been closed for business for more than 12 months, if their authorised operators intend to resume operations.

Commercial establishments belonging to "micro-companies" or companies in which they have a majority holding are expressly excluded from the scope of the commercial licensing regulations.

Commercial licensing regulations encompass not only the installation of the above mentioned commercial retail establishments and commercial complexes but also any modifications comprising (i) changes of location (unless within a commercial complex and not involving an increase in sales areas), type, sales area and trede name of a commercial retail establishment (unless within the same group), or (ii) a change of location, type and GLA of a commercial complex.

### 16.2. Competency

The **DGAE** (Directorate General for Economic Activities - "Direcção Geral das Actividades Económicas") is responsible for coordinating the commercial licensing authorisation process.

The **ASAE** (Food and Economic Security Authority - "Autoridade da Segurança Alimentar e Económica") is responsible for ensuring compliance with the licensing provisions and developers' compliance with the terms and commitments they have undertaken.

### 16.3. Criteria

The decision to issue an authorisation is the material result of an assessment of the plans of the commercial retail establishments or commercial complexes in question whose merits are awarded points in accordance with criteria defined by law.

Where applicable, the commitments undertaken by the operators when applying for permission for the installation or modification of a commercial retail establishment or of a

commercial complex, should be quantified and submitted and may be subject to an annual inspection by the relevant body, for a period of five years, starting from the date upon which the relevant commercial retail establishment or the commercial complex comes into operation.

# 16.4. Conditions on commercial licensing proceedings

If the planned installation or modification of retail outlet or space entails an urban project requiring preliminary administrative "control", the developer must, as a pre-condition to carry out the commercial licensing process, obtain advance information ("pedido de informação prévia") on the retail project's conformity with the applicable territorial management instruments in force.

If the retail project is subject to Environmental Impact Assessment Regulations the developer should also, as a precondition for to carry out the commercial licensing process, obtain a favourable or condition a favourable decision on its Environmental Impact Assessmental.

### 17. LICENSING OF TOURIST RESORTS

The installation, exploitation and operation of tourist resorts is subject to special licensing regulations. Such regulations, were subject to a reform with relevant impact, approved by Decree Law 39/2008 of 7 March and amended by Decree Law 228/2009 of 14 September (RJET - Regulations for Tourist Resorts - "Regime Jurídico da Instalação Exploração e Funcionamento dos Empreendimentos Turísticos").

## 17.1. Types of tourist resorts / local accommodation

Tourist resorts are defined as establishments providing accommodation services for a consideration, which operation is based on an adequate collection of complementary structures, facilities and services.

The **RJET** defines eight types of tourist resorts, as follows: (i) hotels, (ii) tourist villages, (iii) tourist apartments (iv) tourist resort complexes (v) cultural residential tourist resorts (manor/country houses), (vi) rural tourist resorts, (vii) natural tourist resorts in addition to (viii) camping and caravan sites.

Each type of tourist project must comply with lawfully defined common and specific requirements on construction, infrastructures, accommodation capacity, common use and entertainment facilities.

Based on the quality of service, installations and facilities provided, tourist resorts comprising hotels, tourist villages and apartments are graded between one and five stars (7). These classifications are awarded on a points system by Turismo de Portugal, I.P. (the Portuguese tourism regulatory body) and must be reassessed every four years.

### 17.2. Licensing

The licensing of tourist resorts is closely associated with the **RJUE** which apply to the licensing of urban projects used as a basis for the development of the tourist resort in question, under the aegis of the competent municipal authorities.

Turismo de Portugal, IP is, in turn, responsible for verifying the adequacy of the planned tourist resort to the envisaged type and use, involving the analysis of the project's architectural features.

After the tourist resort has been built, a use permit for tourist purposes ("autorização de utilização para fins turísticos") should be issued pursuant to a combination of **RJUE** and **RJET** regulations.

### 17.3. Tourist resorts under plural ownership

### 17.3.1. Incorporation certificate ("título constitutivo")

Tourist resorts under plural ownership, i.e. tourist resorts comprising building plots and/or autonomous units of one or more buildings, are regulated by an incorporation certificate ("titulo constitutivo") to be produced by the holder of the license or authorisation to develop the urban project relating to the tourist resort's installation or holder of the respective use permit. This certificate must be approved in advance by Turismo de Portugal, I.P.

This incorporation certificate comprises (i) information on the entity operating the tourist resort; (ii) information on and physical description of the various autonomous units/building plots into which the tourist resort is divided; (iii) information on their respective relative value and the purpose for which they are intended; (iv) information on the tourist resort's facilities and installations; (v) identification of the common services; (vi) criteria used to calculate and update owner's periodic payments and the percentage thereof to be set aside for the payment of the resort's condominium management entity, in addition to the charges/costs covered by the said periodic payment.

The incorporation certificate for a tourist resort comprising (a) building(s) on a plot of land is the horizontal property master deed when such horizontal property has not been already established, provided that it is in compliance with the legal

requirements. It should be filed with the Land Registry before any contract (or promissory contract) for the conveyance of building plots or autonomous units is entered into.

### 17.3.2. Operation and management of tourist resorts

A tourism services contract is entered into upon the sale of each accommodation unit (autonomous unit or building plot), by which the tourist resort operator indicated by the developer (and identified as such in the tourist resort's incorporation certificate) undertakes to operate the accommodation unit in question, pursuant to certain terms and conditions.

There is currently no time limit on a purchaser's occupation of the accommodation unit (i.e. if so minded, a purchaser may surrender an accommodation unit for tourist operation, and occupy it 365 days per annum). Without prejudice to the above, the operator of the tourist resort must ensure that all of the mandatory services for the category of the tourist resort in question are available, and that all of the accommodation units are furnished and equipped, and ready to be rented for tourist accommodation purposes.

The property management (condominium) of a tourist resort under plural ownership is the responsibility of the operating entity which may be relieved of its managerial (condominium) functions under the terms of a resolution passed by the owners of the tourist resort's accommodation units.

To ensure the continuity of the provision of tourist accommodation services and protect investors who have purchased accommodation units in tourist resorts, the **RJET** provides for a collection of rights and duties on the formation and management of tourist resorts under plural ownership, to be complied with, both by the owners of the above mentioned accommodation units (building plots or autonomous units), operator and property (condominium) management of the tourist resort.



Source: Vale de Lobo, Resort Turístico de Luxo

### CHAPTER VII Leases

### 18 PROPERTY LEASES

Property leases are regulated in the Civil Code since 2006, under the **NRAU** (New Urban Lease Regulations) approved by Law 6/2006 of 27 February 2006, which must be applied to all contracts involving the temporary lease of property for a consideration.

A lease contract for more than six months, must be entered into in writing and identify the parties, the leased premises, the purpose, the rent and the property's use permit certifying its suitability for the desired purpose.

Reference should also be made to the fact that leases for a purpose other than that for which the property has been licensed (e.g. if the property has been licensed for housing and is used for commerce) are null and void.

In the event of the sale of the property by the landlord, the new owner automatically assumes the landlord's respective position, with the terms of lease in force between the tenant and the property's new owner remaining unchanged without the need to formalise an assignment of the contractual position for the said purpose.

The Portuguese applicable urban lease regulations divide leases into two types: (i) leases for commercial purposes and (ii) leases for housing purposes.

### 18.1. Leases for commercial purposes

<u>Freedom of contract:</u> the most relevant aspects of lease contracts for commercial purposes may be freely stipulated by the parties who are, accordingly, free to agree on issues related to length, termination and opposition to the renewal of lease contracts.

<u>Period:</u> the law states that lease contracts may be entered into for fixed term or be of non-specified duration. The latter option is not commonly used in the property market. If entered into on a fixed term basis, the duration may be freely agreed between the parties requiring only to comply with the legal maximum limit of 30 years.

<u>Upkeep</u>: this subject matter is freely regulated between the parties. In this particular case, if no provision is made by the parties, the landlord is responsible for the property's upkeep.

Rent and other expenses: costs and expenses related with the property (such as condominium expenses) are freely agreed between the parties, who are also free to agree the criteria for updating them.

<u>Transfer of tenant's contractual position:</u> the transfer of a tenant's contractual position requires permission from the landlord except for the following situations: (a) transfer of a commercial or industrial business ("trespasse") when including the right to lease; or (b) if the new tenant continues to perform, on the property, the same profession as the tenant assigning its contractual position or if the new tenant is a company of professionals with an equivalent object to the activity performed by the assigning tenant.

<u>Transfer of Business</u> ("trespasse"): the tenant's right to the transfer of business where the lease is included is mandatory and cannot be eliminated by the parties or be waived in advance by the tenant.

Landlord's pre-emption right in case of transfer of business by the tenant: unless otherwise agreed by the parties, the landlord is lawfully entitled to a pre-emption right in case of business transfer (including the lease right) by the tenant, or in case the business (including the lease right) is given as payment in kind by the tenant.

<u>Tenant's pre-emption right on sale of leased property:</u> if a landlord intends to sell a property which has been rented out to third parties, the tenant of the property for more than three years has the pre-emption right in respect of the said sale. This pre-emption right is mandatory and cannot be eliminated by the parties nor be waived in advance by the tenant.

<u>Termination of lease:</u> either party may cancel the lease contract on the basis of a serious default committed by the other which makes the maintenance of the rental impossible. The Portuguese applicable lease regulations provide a non-exhaustive list of cases of default justifying a landlord's decision to terminate the lease contract.

The landlord's termination must be declared judicially except when based on (i) the tenant's opposition to works ordered by public authorities or on (ii) the delay of more than three months in the payment of the rent, charges/costs or expenses. In such cases the contract is terminated by means of a written communication from the landlord to the tenant.

A landlord's contractual termination based on the above referred grounds is ineffective if, within a period of three months, the tenant remedies the delay in its payments of the amounts owed or ceases to oppose the works ordered by a public authority.

### 18.2. Transitional legal framework

The entering into force of the **NRAU** on 28 June 2006, not only established the legal framework for new lease contracts but also a transitional legal framework applicable to leases entered into prior to the said date.

The transitional legal framework, in the case of commercial leases, provide for former **limited duration** lease contracts ("arrendamentos de duração limitada") currently referred to as **fixed term leases** to be considered automatically renewed (unless terminated by either of the parties) at the end of the respective term and for a period of five years except for due provision made to another renewal period.

The mentioned transitional system provides that lease contracts formerly **without limited duration** are subject to regulations on **unspecified duration** contracts. They are subject to several special features, such as the non-application of the landlord's termination right by means of a five-year written prior notice before the intended contract termination date (i.e. the original regulations to which the said lease contracts are subject are not affected).

This "protection" afforded to the tenant ceases, however, and the landlord may terminate the lease contract in accordance with the above terms (i) in the event of a transfer of the business where the commercial lease is included; or, (ii) if the tenant is a company, in the event of any disposal of its shareholdings, resulting in a change of ownership by more than 50% in comparison to the situation existing on the date of the entry into force of the **NRAU**.

## 18.3. Contracts for use of shops in commercial complexes

Contracts for the use of shops in commercial complexes (such as shopping centres, retail parks, retail galleries or outlets) are not subject to the general lease law nor to any other regulations provided by law.

Both the majority of the Portuguese scholars and case-law (including the Supreme Court of Justice) consider that contracts entered into between owners or operators of commercial complexes and shopkeepers should be construed as atypical entered into within the scope of the freedom of contract principle provided for in the Portuguese Civil Code.

It is therefore commonplace for contracts for the occupation and use of areas in commercial complexes not to be entered into pursuant to the scope of any of the types of lease provided for under the Portuguese law on leases.

Many Supreme Court of Justice decisions have ruled in favour of of the validity and lawfulness of such contracts, which are not subject to the general Portuguese law on leases. It is understood that such contracts are not lease contracts but instead atypical contracts, governed by the general contract regulations and only subsidiarily by the relevant rules on leases.

Occupiers of spaces in commercial complexes enjoy more than the mere use of the areas contracted for. The business operated therein also benefits from all of the common amenities and services provided by the owner and/or manager of the commercial development and made available to all its customers and employees.

Although the new Portuguese urban lease regulations currently allow a large margin of freedom for the definition of the contents of commercial leases, the owners of commercial complexes in which retail establishments operate, may still benefit from the fact that the use of shop agreements are not subject to the mentioned law on leases.

The fact that this type of contract is not governed by the Portuguese urban leases law signifies the non-application of the tenant's pre-emption right on a property's sale; the non-existence of a tenant's right to the transfer of business where the lease is included, the impossibility of pledging the right of use of the property covered by the use of shop agreement (as opposed to the possibility of a pledge over the tenant's rental right, in the event of enforcement proceedings brought against the tenant by a third party); the non-application of the typical eviction procedures for terminating the contract and vacating the property (despite the fact that the owner, in this case, must still go to court to enforce the tenant's eviction).



Dolce Vita Tejo | Source: Chamartín Imobiliária



CUSHMAN & WAKEFIELD Av. da Liberdade n.º 131 - 2º 1250-140 Lisboa, Portugal Tel.: (+351) 21 322 47 57 Fax: (+351) 21 343 21 17 www.cushmanwakefield.com

Marta Leote

### Uría Menéndez Proença de Carvalho

URÍA MENÉNDEZ - PROENÇA DE CARVALHO
Rua Duque de Palmela n.º 23
1250-097 Lisboa, Portugal
Tel.: (+351) 21 030 86 00
Fax: (+351) 21 092 01 01
www.uria.com