THE Real Estate M&A and Private Equity Review

Fourth Edition

Editors

Adam Emmerich and Robin Panovka

THE LAWREVIEWS

THE REAL ESTATE M&A AND PRIVATE EQUITY REVIEW

Fourth Edition

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PREFACE

Publicly traded real estate companies and real estate investment trusts (REITs), with help from real estate private equity, have transformed the global real estate markets over the past 25 years. Their principal innovation, and secret sauce, is 'liquid' real estate. Unlike traditional property ownership, equity in publicly traded real estate vehicles is highly liquid, and can be bought and sold in large volumes, literally in minutes, on numerous global exchanges.

Publicly traded real estate vehicles have an aggregate market capitalisation of approximately US$1.7 trillion globally, including over US$1 trillion in the United States and approximately US$200 billion in each of Europe and Asia. As public REITs and other vehicles have aggregated these properties and grown in scale and sophistication, so too have real estate-focused private equity funds, playing an important role catalysing hundreds of billions of dollars of REIT and real estate M&A transactions and IPOs.

However, despite the massive growth, the potential growth is far larger both in long-standing REIT markets and in newer REIT jurisdictions, where the trend is more nascent. With increasing development and urbanisation, the world is producing more and more institutional-grade properties, and a growing percentage of this expanding pool – an estimated US$5 trillion and counting, so far – will inevitably seek the advantages of liquidity by migrating to the publicly traded markets. The growth is expected to be both local and cross-border, with approximately 40 countries already boasting REIT regimes.

REITs and other publicly traded vehicles for liquid real estate have grown because they are often a superior vehicle for stabilised assets. Greater liquidity and transparency – and often superior governance – are attractive to investors, resulting in a lower cost of capital and superior access to vast amounts and varieties of capital in the public markets. In addition to cheaper capital, REITs and other public vehicles benefit from efficiencies of scale, sophisticated management and efficient deal structures, to name just a few advantages. With these advantages, the global march of real estate to the public markets seems unstoppable.

This publication is a multinational guide for understanding and navigating the increasingly complex and dynamic world of liquid real estate and the transactions that mostly produce it. The sea change in the markets, sometimes called the 'REIT Revolution', has meant that major real estate transactions have migrated from 'Main Street' to 'Wall Street'. They now often take the form of mergers, acquisitions, takeovers, spin-offs and other corporate transactions conducted in the public markets for both equity and debt. They have grown exponentially in complexity and sophistication, and increasingly represent cross-border multinational transactions fuelled by the now global real estate capital markets and M&A deal professionals. And they are often intermediated by international investment banks rather than local brokers, and financed with unsecured bonds or commercial mortgage-backed securities. In a fair number of cases they are catalysed by private equity firms or similar actors, sometimes building portfolios to be taken public or sold to public real estate companies, and sometimes through buyouts of public real estate companies for repositioning or sale.

To create this publication, we have invited leading practitioners from around the globe to offer practical insights into what is going on around the conference tables and in the markets in their jurisdiction, with an eye to cross-border trends and transactions. As will quickly become evident, the process of liquefying real estate and the transactions involving public real estate companies require a melding of the legal principles, deal structures, cultures and financial models of traditional real estate, public company M&A and private equity. None of this, of course, happens in a vacuum, and transactions often require expertise in tax, corporate and real estate law, not to mention securities laws and global capital markets. Each of our distinguished authors touches on these disciplines.

We hope this compilation of insight from our remarkable multinational authors produces clarity and transparency into this exciting world of 'liquid real estate' and helps to further fuel the growth of the sector.

Adam Emmerich and Robin Panovka
Wachtell, Lipton, Rosen & Katz
New York
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Chapter 16

PERU

Alfredo Chan, Alexandra Pázzara and Erick Lau[1]

I OVERVIEW OF THE MARKET

In 2018, Peru's economy rebounded to 4 per cent,[2] especially in the fourth quarter, due to an increase in public investment in October.[3] In addition, a strong recovery in the fishery sector between November and December and an improvement in performance in the mining sector led to the GDP increase.[4]

The Peruvian Ministry of Economy[5] noted that the recovery of investment and fiscal consolidation were primary drivers for the increase in GDP. Peru achieved the highest growth rates for public and private investments since 2013. This along with the reduction in fiscal deficit and an increase in the recovery of fiscal revenues since 2015 led to the strong rebound of Peru's economy in 2018.

The World Bank estimates GDP will reach 3.8 per cent[6] in 2019. According to the Peruvian Ministry of Economy,[7] continued public and private investment will continue to support GDP growth in the following years, especially in the mining sector.

Furthermore, the real estate sector has maintained its strength, in all segments, including commercial, offices and housing. Recent government measures have been implemented to provide additional support for social programmes, such as Techo Propio and Fondo MiVivienda, which promote formal (i.e., legally registered) housing by subsidising its acquisition in the lower-income socio-economic groups. Also, the government has issued regulations to allow for the formation and operation of real estate investment trusts (REITs).

1 Alfredo Chan is a partner, Alexandra Pázzara is a senior associate and Erick Lau is an associate at Payet, Rey, Cauvi, Pérez Abogados.
2 Source: The World Bank, https://openknowledge.worldbank.org/bitstream/handle/10986/31483/9781464814136.pdf?sequence=6&isAllowed=y.
3 Source: Andina, https://andina.pe/ingles/noticia-peru-bcr-maintains-gdp-growth-projection-at-4-733026.aspx.
4 Source: Andina, https://andina.pe/ingles/noticia-peru-bcr-maintains-gdp-growth-projection-at-4-733026.aspx.
5 Source: Peruvian Ministry of Economics and Finance, https://www.mef.gob.pe/contenidos/english/presentations/MEF_London_presentation.pdf.
6 Source: The World Bank, https://openknowledge.worldbank.org/bitstream/handle/10986/31483/9781464814136.pdf?sequence=6&isAllowed=y.
7 Source: Peruvian Ministry of Economics and Finance, https://www.mef.gob.pe/contenidos/english/presentations/MEF_London_presentation.pdf.

i Real estate – formal sector

Apartment sales in Lima increased in 2018, with an estimate of more than 13,000 units being sold. However, this number is still far from the levels reached in 2011 and 2012, during the years of the real estate boom.[8]

The number of apartments sold is expected to continue to increase in 2019, reaching an estimated 16,500–17,000 units.[9] This increase is driven by the population´s improved spending power, which helps families to secure mortgage loans.

With respect to the prime office market (A and A+), the number of units continued to increase in 2018. However, the vacancy rate decreased in 2018 due to increased business activity and the introduction of co-working spaces, which accounted for 20 per cent of net absorption. Although vacancy rates decreased, the market still has enough supply to continue to place downward pressure on prices.[10]

ii Real estate – informal sector

Reducing the housing gap continues to be a major challenge for the Peruvian government. The problem mainly arises from the lack of access to credit among the lower-income socio-economic groups, which is where the demand for housing is highest.

The high prevalence of self-construction has aggravated the problem. Individuals with no access to the credit system often find a solution to their housing problems through self-construction or informal housing, which in most cases does not provide access to adequate habitability conditions or public utilities such as water and drainage systems. According to recent information from the Peruvian Real Estate Developers Association, approximately 18,000 units of formal housing are being built every year, whereas the number of informal buildings is reaching 30,000 a year.[11]

Semi-formal developers increase this problem. Often companies do not provide appropriate guarantees to ensure the culmination of a real estate project, resulting in serious infringements and frauds. To mitigate this problem, the government has created a central agency to register property developers and provide accurate information to individuals about formal companies in the real estate market. However, based on public information, to date, there are approximately 8,000 informal real estate developers in our country.[12]

According to public information disclosed by the private pension fund management companies, individuals are willing to use 25 per cent of their pension funds, mainly to repay

8 Source: https://www.bbvaresearch.com/publicaciones/peru-new-home-and-prime-office-market-in-lima-metropolitana/.

9 Source: https://www.bbvaresearch.com/publicaciones/peru-new-home-and-prime-office-market-in-lima-metropolitana/.

10 Source: https://www.bbvaresearch.com/publicaciones/peru-new-home-and-prime-office-market-in-lima-metropolitana/.

11 Source: Gestión, https://gestion.pe/tu-dinero/inmobiliarias/viviendas-informales-construyen-ano-doble-formales-135748.

12 Source: CAPECO, www.capeco.org/noticias/hay-8-000-firmas-inmobiliarias-que-son-informales/.

existing mortgage debt but not to acquire new real estate property.[13] Nonetheless, according to the Peruvian Bank Association mortgage portfolio registers its highest growth rate since October 2015.[14]

To address the problematic housing issue, the government has been running two public housing support programmes aimed at securing financing from the banking system: Techo Propio provides financing to families with lower income (approximately less than US$636 per month)[15] to help them acquire, build or fix an existing home; and Fondo Mivivienda, which provides loans (between US$19,000 to US$128,000)[16] to lower-middle and middle-income families to help acquire, build or improve an existing home which can be repaid in five to 20 years. This program also offers the possibility of accessing the Good Payer Subsidy (Bono de Buen Pagador) a non-reimbursable economic aid (of a maximum of approximately US$5,470)[17] granted to persons that acquire a house through the Fondo MiVivienda which enables them to use it towards their down payment.

II RECENT MARKET ACTIVITY

i Public real estate investment fund transactions

Traditionally, the formal sector has been dominated by joint-stock corporations, however, since the mid-2000s, public and private real estate investment funds have begun their incursion into the real estate market.

Also, since 2015, new legislation on two types of public REITs, has been introduced in the market to promote real estate investments. We refer to the FIRBI (real estate investment fund) and the real estate rent securitisation trust, known as the FIBRA (Fideicomiso de Infraestructura en Bienes Raíces), both of which have been widely influenced by the Mexican FIBRA model.

Between 2016 and 2018 the first REITs (through FIRBIs) were registered before the Superintendence of the Securities Market (SMV). However, due to the gaps in the existing regulation, they did not have a major impact in the Peruvian real estate market.

However, since 2018, due to governmental promotion, alongside the modification of the REIT's regulation, the private sector has increased its interest on FIRBIs and FIBRAs and the number of FIRBIs has increased significantly. 'F Rentas Inmobiliarias – FIRBI', 'Metroport – FIRBI', 'Faro I – FIRBI', 'AC Capitales Renta – FIRBI' and 'SURA Asset Management II – FIRBI' are some of the new vehicles that have entered the market. The most recent was created with an approved capital of US$1 billion, which makes it the biggest REIT in the Peruvian market as of this date.

13 Source: Semana Económica, http://semanaeconomica.com/article/sectores-y-empresas/inmobiliario/199691-retiro-del-25-de-las-afp-no-reactivaria-el-sector-inmobiliario-en-proximos-doce-meses/.

14 Source: Gestión, https://gestion.pe/economia/mercados/asbanc-creditos-hipotecarios-registran-mayor-incremento-28-meses-227960.

15 Source: Mi Vivienda, https://www.mivivienda.com.pe/portalweb/usuario-busca-viviendas/pagina.aspx?idpage=30.

16 Source: Mi Vivienda, https://www.mivivienda.com.pe/PortalWEB/usuario-busca-viviendas/pagina.aspx?idpage=20.

17 Source: Mi Vivienda, https://www.mivivienda.com.pe/PORTALWEB/usuario-busca-viviendas/pagina.aspx?idpage=22.

Furthermore, on August 2018, the first FIBRA, 'FIBRA Prime', was registered before the SMV, with an approved capital of US$5 billion. The first IPO of such FIBRA was launched on December 2018, raising an amount of US$22.5 million. According to public information, FIBRA Prime is about to launch a second IPO during the first half of 2019, for an additional amount of US$30 million approximately.

In addition, the next release of an international FIBRA, FIBRA The Latam REIT, has been announced and is on its way to registration before the SMV. The particularity of this FIBRA is that it plans to make investments in real estate located in different Latin American countries for an amount of up to US$7.5 billion and 35.6 per cent of this amount is estimated to be invested in Peru.

ii M&A and other transactions

A successful example of an M&A transaction in the real estate and hotel sector is the acquisition in 2018 of the Atton Hotels by the international hotel chain AccorHotels and the Chilean Group, Algeciras. Through this transaction, which valued the Atton Hotels at US$365 million, AccorHotels and Algeciras will operate 11 hotels and continue with the development and construction of three new projects, located in Chile, Peru, Colombia and Florida, United States.

III REAL ESTATE COMPANIES AND FIRMS

i Traditional real estate companies

The main real estate investments and activities are developed by traditional corporations. Peru does not have specific regulation for corporations dedicated to the real estate market.

The Peruvian Corporations Law recognises three types of joint-stock corporation: a general type of joint-stock corporation (SA) and two other special types of joint-stock corporations, the SAC, which is a closed joint-stock corporation, and the SAA, which is a public joint-stock corporation.

In addition to the above-mentioned forms of joint-stock corporations, the Peruvian Corporations Law also regulates other forms of companies and partnerships, including the limited liability partnership, which is very similar to the SAC and is also often used.

All the above corporations and companies confer limited liability on their shareholders, who will only be liable up to the amount of their capital contributions. Also, all the above forms of corporations and companies receive the same tax treatment.

ii Public and private real estate investment funds

The Peruvian market has evolved in recent years because of the sustained increase in the number of public and private real estate investment funds (the Investment Funds). The Investment Funds are independent asset pools comprising of contributions made by individuals and legal entities for investments in the acquisition and development of projects that generate financial returns through the sale or rent of real estate units.

Typically, most of these investments were focused on the residential sector (housing); however, the demand for commercial premises has been growing rapidly over the past years because of the opening of shopping malls, strip malls, and office buildings, as well as the launching of industrial centres.

The Investment Funds are managed on behalf of and at the risk of the fund's members by private equity companies known as investment fund management companies, or SAFIs, whose sole purpose is to manage one or more investment funds.

In addition, the Investment Funds are monitored by an oversight committee, which oversees the SAFI's compliance with the law, membership regulations and placement terms, ensuring that the information provided to the fund's members is accurate and timely, supervising the implementation of changes required following any objections made by the external auditors, and that the general shareholders' meeting is duly held to report on the management of the fund or when necessary.

Furthermore, SAFIs are monitored by an investment committee, the main duties of which are, among other things, to follow up on the fund's assets, determining their value and the method to be used for evaluating them, and identifying and analysing different investment opportunities (taking into consideration the fund's policies and guidelines), as well as making investment decisions for the fund when required.

iii Peruvian REITs – FIBRA and FIRBI

Background

REITs are not unheard of in the Peruvian Market. They have been around since the mid-2000s, when public and private investment funds began their incursion into the real estate market through the acquisition of land and property developments. However, until 2015, the expansion of these investment ventures was very limited, mainly due to the lack of specific regulation tailored to the specific characteristics of REITs.

On 24 November 2016, the Peruvian government enacted specific legislation related to REITs for the first time. This regulation created two new types of REITs: (1) the real estate rent investment fund (FIRBI) and (2) the real estate rent securitisation trust (FIBRA). The aforementioned legislation has opened a path for REITs, accommodating these kinds of investments.

When designing the mentioned REITs, the impressive results of the Mexican FIBRA since its creation in 2011 caught the attention of the Peruvian government. In fact, it is estimated that the Mexican FIBRA has yielded a revenue of 150 per cent during periods where the performance of the Mexican stock market did not exceed 50 per cent. Moreover, since its creation the Mexican real estate market has experienced a steady increase, as well as the incorporation of a number of new REITs.

The Peruvian model: FIRBI and FIBRA

The American REIT model, together with the Mexican experience, helped design the Peruvian FIRBI and FIBRA; which is why foreign investors may find these investment vehicles very familiar. The most important characteristics shared by the FIRBI and FIBRA with the aforementioned models are the following:

a The funds raised from the investors must be allocated exclusively to the acquisition or construction of income-producing real estate (e.g., industrial buildings, commercial offices, hotels, residential developments, among other real estate assets), so that the properties owned by the trust may be allocated exclusively to the generation of income from its lease.

b The beneficiaries of these investment vehicles (in the case of FIRBI and FIBRA, the holders of the instruments are called Participation Certificates) are entitled to the revenues yielded from the fund through its two main sources: (1) the income derived from the lease of the properties, and, (2) the appreciation of said properties since its acquisition until it is sold.

c They are meant to be attractive to investors, by allowing them access to certain tax benefits through these vehicles (e.g., lower income tax rates compared to those applicable for corporate taxation). In turn, those tax benefits create efficiencies in the real estate market, since through them, almost anyone can invest in portfolios comprised of real estate assets, just as they would in other industries.

Although there are similarities with the American REITs, the Peruvian models of the FIRBI and the FIBRA have the following distinctive features:

a Unlike the American REIT, FIRBIs and FIBRAs do not have stockholders, but rather beneficiaries. They are not considered a legal entity that may be incorporated as a joint-stock corporation and, therefore, cannot make their own investment decisions. The FIRBIs and FIBRAs require another entity which makes those decisions on its behalf. In the case of FIBRAs, the entity in charge of the trust's management is a securitisation entity, while the FIRBIs are managed by a fund management entity.

b Participation in the FIRBI and FIBRA must be placed through a public primary offering with at least 10 unrelated investors, and at least 70 per cent of the funds raised by these vehicles must be used in the acquisition or construction of income-producing real estate.

c They must distribute most of their net income (i.e., at least 95 per cent of its profits according the current regulation) among their beneficiaries.

d For taxation purposes these vehicles are considered transparent, which means investors who take part in them will be taxed at an identical rate as if they were to lease their own real estate properties as individuals. This characteristic is of particular relevance when compared with the general tax rate for corporations, since the income tax rate that a corporation is taxed at for the lease of real estate is significantly higher (29.5 per cent) than that of an individual (or, in this case, a FIRBI or FIBRA); which amounts only to 5 per cent. Another example of this transparency may be found regarding the real estate transfer tax, which can be deferred to either the moment in which the income-producing real estate is transferred by the FIRBI to a third party, or, to the moment when the investor who contributed the income-producing real estate transfers any of his Participation Certificates. However, we must note that this last consideration regarding the real estate transfer tax is only applicable to FIRBIs.

It is important to highlight that, although FIBRAs and FIRBIs are quite similar in nature, there are some relevant differences between the two investment vehicles and they are subject to different regulations. FIRBIs are created under the rules of the Investment Fund Regulation, while FIBRAs are created under the Secularisation Process Regulation. This has practical consequences, in particular, in the way they are organised and how these vehicles are governed. As noted, the main difference between both vehicles is in the entity authorised to manage them; a securitisation entity in the case of FIBRAs and a fund management entity in the case of FIRBIs. In terms of operation costs, FIRBIs may be less expensive that FIBRAs, due to the participation costs of a securitisation entity.

Recent changes regarding FIBRA's regulation

Although the structures of FIBRA and FIRBI were created in 2016, they lacked comprehensive regulations regarding its organisation and governmental bodies. At the time of writing, FIRBIs still lack such regulation. However, for the case of FIBRAs this is no longer the case, since on 27 February 2019, the Peruvian Security Exchange Commission modified the regulation for asset-backed securitisation through which FIBRA and FIRBI were created to include more extensive rules regarding FIBRAs.

One of the most interesting changes introduced by this bill is the possibility for FIBRAs to make international invitations for the subscription of participation certificates, which opens the possibility for foreign investors to participate in the peruvian real estate market through FIBRAs. However, this is only possible if the placement of the participation certificates is made through a public primary offering within the Peruvian territory, and, as long the intermediary agent is supervised by a similar entity as the SMV.

Other significant changes with relevant consequences for investors are the following:

a The possibility for FIBRAs to acquire future real estate assets, such as buildings that are still under construction. The only consideration regarding the acquisition of these kind of assets, which certainly gives more flexibility to the investment decisions that can be made, is that the land where the new structure is to be built must be already registered at the time of the acquisition.

b A list of circumstances that may result in the FIBRA becoming a standard securitisation trust and, therefore, losing all tax benefits granted by the Peruvian government to FIBRAs, such as being subject to the income tax rate applicable for corporations, which as noted earlier, is significantly higher. Among those circumstances, the most relevant are the situations where the FIBRA (i) fails to allocate 70 per cent of its assets to income-producing real estate; or (ii) sells the real estate assets within the first four years since acquisition (i.e., in the case of real estate assets acquired for its construction, the term will begin when the construction is finished and it will only be possible to sell them once the construction is finished and the four year term has elapsed).

In December 2018, the first IPO for a FIBRA was launched under the name of 'FIBRA Prime'. Over US$22.5 million was raised, partially from institutional investors (30 per cent), but mainly from the general public (70 per cent). FIBRA Prime administrators expect to raise up to US$5 billion in the next three years.[18] This is certainly the first of many new investments that are expected to launch officially in 2019. Among them, probably the most important is the FIBRA called The Latam REIT, which has been officially announced and is expected to raise up to US$7.5 billion. This vehicle will include real estate properties located in Peru (35 per cent), Mexico (22 per cent), Colombia (22 per cent), and other Latin American countries.[19]

18 Diario Gestión. 'Fibra Prime hizo su primera colocación por US$ 22.5 millones': Consulted on 17 April 2019 <https://gestion.pe/economia/mercados/fibra-prime-hizo-primera-colocacion-us-22-5-millones-253447>.

19 Diario Gestión. 'Perú concentrará 35.6 per cent de las propiedades de Fibra The Latam Reit'. Consulted on 17 April 2019 <https://gestion.pe/economia/empresas/peru-concentrara-35-6-propiedades-fibra-the-latam-reit-260302>.

We see the entrance of FIBRA and FIRBIs as a great chance to take the Peruvian real estate market to the next level and forsee considerable amounts of new investment flowing towards it.

IV TRANSACTIONS

i Real estate acquisition agreements

The most common type of transaction for the acquisition of real estate properties in Peru is the asset sale and purchase contract, whether related to an existing property or a future asset.

The main reason for the buyer to proceed with the direct acquisition of a real estate property is to avoid assuming the liabilities of the existing legal entity holding the property. Prior to executing a sale and purchase contract, a complete legal and technical due diligence review of the property is highly recommended.

The legal due diligence review is focused on the property title (to confirm the areas and boundaries of the property, verify the ownership status and the existence of any mortgages, liens or encumbrances, the registration of any limitation for the sale of the property, and the registered constructions), the zoning and urban parameters, the existence of outstanding payments for property and municipal taxes, and any existing licences or permits, among other relevant matters.

On the other hand, the technical due diligence review will seek to verify the areas of the property, the structural shell and the quality of the soil, as well as the functionality of the technical installations (water supply, drainage, power and electricity systems, air conditioning, elevators, exterior lighting, heating systems and others). Also, a physical review of boundaries and environmental conditions may be useful in many cases.

It is also common to execute a future asset sale contract when the real estate property is still in the project or construction phase. These contracts are definitive agreements conditional on the effective existence of the property (usually when the property is registered as an independent unit in the real estate public register).

A share purchase agreement is less common, as it is used when the seller wishes to sell its entire real estate business, and the buyer is interested in acquiring an ongoing enterprise. One of the main reasons for the buyer to acquire the business is to receive a fixed rental income arising from contracts executed by the target company (lease contracts or any other type of onerous contract that grants use rights over the property to third parties). Spin-offs and mergers are also sometimes used to trade real estate.

In this case, the scope of the due diligence review of the target company will involve several matters focusing on identifying the liabilities arising from labour, tax, and contractual matters, as well as judicial proceedings. In addition, the buyer will need to obtain detailed information from the seller with respect to its assets, finances and business operations.

Since the information collected during the due diligence process is confidential, it is standard to execute a confidentiality or non-disclosure agreement before obtaining access to this information. It is also standard practice in this type of transaction for a letter of intent to be signed, agreeing on the main terms of the transaction and specifying that the execution of the transaction is subject to the satisfactory results of the due diligence process.

ii Financing considerations

There are no special regulatory considerations regarding the financing of real estate acquisitions in Peru. Real estate operations are typically financed from a combination of equity and debt. The most common types of structures used to secure lending obligations are mortgages, share pledges, and warranty trusts.

Under Peruvian legislation, a mortgage works as a lien over a specific real estate property. To be enforceable against third parties, it must be formalised through a public deed and must be registered in the real estate public register.

On the other hand, share pledge agreements allow companies to use their shares as collateral to avail themselves of a loan. Pursuant to Peruvian legislation, for the agreement to be effective against third parties it must be formalised through a public deed and registered in the public Moveable Property Contracts Register and in the company's share ledger.

Finally, warranty trusts have been used more frequently over the past few years as security for financings. Warranty trusts can be used in relation to either real estate property or moveable goods, and they also must be formalised through a public deed. If the trust is created using real estate property, it must be registered in the real estate public register, and in the case of moveable goods, the registration must be made with the Moveable Property Contracts Register.

With the real estate market being boosted by the entry of investment funds, it is expected that the public market will be targeted as a source of funds for the financing of real estate acquisitions or projects. However, the traditional mechanisms of financing remain those mentioned above.

iii Tax regime on real estate transactions

Buying real estate

The acquisition of real estate property is subject to a real estate transfer tax at a rate of 3 per cent of the transfer value of the property. An amount of 10 UIT (a unit of monetary measurement, updated every year by the government to handle payments to be made to the government, such as taxes and fines) may be deducted from the transfer value to determine the tax base. The UIT for 2019 is 4,200 Peruvian soles (approximately US$1,273). Note that the taxpayer of the real estate transfer tax would be exclusively the purchaser of the property.

In the case of the first sale of a new real estate property by the constructor (a real estate company), real estate transfer tax would only apply to the value of the land. In addition, the transaction will be subject to value added tax (VAT) at a rate of 18 per cent, applicable to 50 per cent of the transfer value (i.e., an effective rate of 9 per cent).

Selling real estate

In general terms, the transfer of real estate property located in Peruvian territory is subject to income tax. Income tax must be paid on capital gains derived from any transfer (e.g., sale or capital contribution in kind) of real estate property qualifying as taxable income.

The capital gains are determined as the difference between the transfer price (which must meet market value standards) and the tax base the seller has in the corresponding property. The tax rate applicable to the capital gain depends on the seller's status. Currently, the following rates may apply:

a Peruvian domiciled and non-domiciled individuals must pay 5 per cent tax on the gross income. However, non-domiciled individuals may request to be taxed only on the difference between the initial purchase price and the selling price through an administrative procedure before the tax authority, known as 'reimbursement of invested capital'.

b Peruvian domiciled entities must pay 29.5 per cent tax on their net income, and non-Peruvian entities will be subject to 30 per cent tax on the gross income. Notwithstanding, the non-Peruvian entity must also follow the 'reimbursement of invested capital' procedure before the tax authority.

For transfers of real estate property through corporate reorganisations (e.g., mergers, spin-offs, simple reorganisations), it is important to highlight that the income tax and VAT regulations establish special tax regimes, so assets can be transferred without generating tax effects. Nevertheless, the acquisition of real estate property between Peruvian entities through a corporate reorganisation would still be subject to real estate transfer tax, as previously explained.

Renting real estate

Peruvian domiciled and non-domiciled individuals who obtain an income from the lease of a real estate property must pay 5 per cent on the rental income.

Peruvian domiciled entities that lease a real estate property in Peru must pay 29.5 per cent tax on the rental income after applying the tax deductions permitted by the applicable laws, and non-Peruvian entities that lease a real estate property in Peru will be subject to 30 per cent tax on rental income.

Holding real estate

Real estate property owners are subject to property tax and to municipal taxes, the rates for which are calculated based on the value of the property and the area where the property is located.

Appendix 1

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