INTERNATIONAL ***REAL*** ESTATE
FINANCE & INVESTMENT REVIEW 2024/25

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International Real Estate Finance and Investment Review 2024/25

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Key developments in the Spanish real estate market: resilience into a new cycle

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BIO

Bernat Mullerat is a partner at the Corporate and Real Estate Practice Groups of CUATRECASAS in Barcelona, Spain.

He has advised on many real estate transactions, mainly acquisition of shopping centers, hotels and office buildings, as well as hotel and tourist resort management. He advises on regulatory and contractual matters related to tourist and timesharing transactions. He also handles national and international transactions to develop and sell renewable energy projects.

He was co-chair of the Real Estate Section of the International Bar Association (2022-2023), vice-chair of the British Chamber of Commerce in Spain (2005-2010) and senior vice-chair of the Environment, Health and Safety Law Committee of the International Bar Association (2008-2010).

He speaks regularly at national and international seminars and conferences on real estate and the environment.

He is the author of several law review articles on Spanish real estate and environmental law.

CUATRECASAS

Key developments in the Spanish real estate market: resilience into a new cycle

CUATRECASAS

The Spanish property market has long been a focal point for both domestic and international investors. Over the past few years, the market has experienced significant changes driven by economic factors, regulatory shifts, and evolving investor preferences. This article reviews the key developments and trends shaping the Spanish property market in 2024.

Economic recovery and market resilience

Spain's economy has shown remarkable resilience in recent years, bouncing back from the global financial crisis and the subsequent European debt crisis. The country's GDP growth has been steady, and unemployment rates have gradually declined. This economic stability has had a positive impact on the property market.

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Commercial real estate

In recent years commercial real estate has gone through a difficult phase due to the increase in interest rates. Investment in commercial real estate has been severely impacted by these hard financial conditions. The high interest rate environment has been here for longer than expected.

The second half of 2024 is likely to bring a decline of interest rates to stimulate economic growth. This long-awaited economic measure will improve investor sentiment across most asset classes, but not affect them equally.

Hotels and leisure are the asset class that has best resisted high interest rates. The end of restrictions to international traveling after the pandemic resulted in a record investment year in 2023. According to the European Investor Intentions Survey, Spain is positioned in 2024 as the preferred destination for investors. Geopolitical stability has also played a role in the boosting of hotel investment.

Office investment has been impacted by the debate on the future of offices, increased lease flexibility and occupier demands. These global trends, also affecting Spain, plummeted office investment in 2023 by more than 40% decrease compared to 2022.

While office investment continues to be focused primarily on Madrid and Barcelona, there is a growing need for conversion of assets to account for tenant demand of more energy efficient buildings, ESG requirements and higher quality premises for adaptable occupier needs.

The tight fundamentals for office investment are driving some investors towards changes of use of obsolete office buildings to be transformed into living and hotel use.

Investment in **retail** assets suffered a sharp decline in 2023 due to a variety of factors, including financing conditions, high inflation, moderate consumption patterns. However, the prospects for 2024 seem more positive.

The curve of e-commerce has relented since the pandemic but is still a factor influencing the lower demand for retail.

The **logistics** sector has maintained robust interest from investors while showing timid signs of slowing down. Due to the steady growth of e-commerce, investor interest in logistics is focused on value-add products where asset development or repositioning offer better return.

There is a strong competition for logistic assets with growing sale and lease back opportunities.

Housing and other living assets

Housing continues to set a pattern of continued growth. Home prices have revealed a strong resistance to price decreases.

Construction costs, regulatory requirements and slow planning and licensing processes prevent construction from tackling the growing demand of new homes. Such higher demand is driven by the employment growth, higher salaries, immigration and, in certain areas, robust demand by tourism. Demographic growth is pushing housing prices up.

Access to housing is an extremely delicate matter for Spaniards, particularly for households with lower income and acutely in certain areas. National and regional governments have adopted measures to address increasing rental prices. Tight rent controls have been imposed in 140 towns and cities in catalonia. These measures have proved so far as having little effect in the fight against rental increases.

The deficit of government sponsored affordable housing seems now systemic due to the lack of governmental investment for many decades.

The above constraints contributed to rapid development of build to rent schemes since 2021. The appearance of this asset class is caused by the strict requirements for accessing to the mortgage market for many households as well as by a change in sociocultural patterns. However, the sharp growth in build to rent is now slowed down due lower yields and regulatory changes addressed to reduce rents.

Development and investment in alternative living asset classes such as senior, purpose built student accommodation and co-living are expected to continue growing due to the robust fundamentals behind each of them.

Conclusion

The Spanish real estate market is poised for significant growth and transformation. Sustainability, flexible workspaces, e-commerce, logistics, retail transformation, and investment dynamics are key trends shaping the market.

Stakeholders who stay ahead of these trends and adapt to changing market conditions will be well-positioned to capitalise on the opportunities that lie ahead. As always, careful planning, strategic investments, and a keen understanding of market dynamics will be essential for success in this evolving landscape.

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BIO

Yolande C. Julien was called to the Bar of England and Wales in 2003. After gaining valuable experience at two local law firms in The Bahamas, she joined Glinton Sweeting O'Brien ("GSO") as an associate in 2007.

Yolande's practice is wide ranging as she is versed in all aspects of residential and commercial property sales and financing transactions; immigration matters, specifically short/long term work permit applications and permanent/annual residency applications; estate planning and probate law, administering both international and local estates and resealing estates.

She also advises clients on foreign direct investment projects and represents international companies in their bid to operate local business operations/branches in The Bahamas.

Yolande is a member of the Honorable Society of Lincoln's Inn. She holds an LLB from Queen Mary, University of London, and completed the bar vocational course at BPP Law School in London, England. She was called to the Bahamas Bar in 2016.

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BIO

Johanna J. Mayson obtained a Bachelor of Arts diploma (Magna Cum Laude) in Florida, USA and later completed the Bar Vocational Course in London, England. In 2010, she was called to the Bar of England and Wales and in the same year, she was also called to The Bahamas Bar.

Johanna joined Glinton Sweeting O'Brien ("GSO") in 2011 as a pupil and is currently a partner in the firm's Real Estate, Resort Development, and Immigration Practice Groups. Johanna specialises in real estate transactions, conveyancing, financing, resort and hotel development, government licencing, title insurance, subdivision planning and approval, local taxes, foreign direct investment, condominium and marina developments, as well as immigration and residency matters with a focus on economic permanent residency and work permits for foreign nationals.

Johanna has advised on a variety of title matters including the $1.75 billion refinancing of a mega resort on Paradise Island, and the $2.5 billion secured financing of another luxury resort in Cable Beach, New Providence. She has also acted for vendors and purchasers of private islands/cays in The Bahamas.

Johanna's clientele include high net worth commercial, corporate, and private clients participating in the sale, acquisition, financing, and development of real estate in the Bahamian ultra luxury resort and residential markets, including communities such as Albany, Lyford Cay, Old Fort Bay, Paradise Island, Ocean Club, Baker's Bay, and more.

GSO Glinton Sweeting O'Brien
Counsel & Attorneys-at-Law

Buying and Living in Paradise
An overview of property acquisition and residency in The Bahamas

Glinton Sweeting O'Brien
Counsel & Attorneys-at-Law

In its quest to become a leading tourism destination, The Bahamas welcomed approximately 9,654,838 visitors in 2023. This is a worthy milestone, and the Government of The Bahamas continues to take active steps to attract visitors to its shores. The target for 2024 is 12 million visitors and as of August 2024 approximately 6.8 million tourists have visited The Bahamas, with approximately 1.16 million arriving via air. This push by the Government is deliberate, because amongst many benefits, visitors to The Bahamas potentially turn into property owners and residents. In this vein, the Government is committed to making the process of owning property and becoming a resident as seamless and streamlined as possible.

Overview of Property Acquisition in The Bahamas

Land Reform is coming

Most recently, the Land Reform Committee recommended a transition from our current deed registration system to a title registration, a step which will revolutionise the way real estate transactions are done in The Bahamas. This modernisation of the current registration system is still in the initial stages and will be rolled out in phases, commencing as early as the first quarter of 2025. These land reforms promise to offer, amongst other advantages, clear and marketable title in a shorter timeframe, access to credit, reduction in land disputes, and enhanced land transfer taxes.

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Once an offer to purchase property is accepted, the first step is the preparation of an Agreement for Sale outlining the terms and conditions of the transaction.

Working with your Real Estate Agent and Attorney

As it stands, the process to acquire property in The Bahamas initially involves working with a realtor to identify a property. Once identified, an attorney registered to practice law in The Bahamas should be contacted to spearhead the transaction. Our Legal Profession Act provides that only a qualified attorney from the jurisdiction may prepare documents relating to real estate transactions. Accordingly, it is prudent that checks are made to ensure the selected attorney is qualified to practice in The Bahamas. The Bahamas Bar Association maintains an up-to-date website containing a listing of attorneys in good standing.

Agreement for Sale

Once an offer to purchase property is accepted, the first step is the preparation of an Agreement for Sale outlining the terms and conditions of the transaction. It provides for (not an exhaustive list):

- The payment of a deposit upon execution of the Agreement for Sale.
- The escrow/stakeholder conditions related to the deposit.
- The circumstances whereby the deposit is to be returned to the purchaser or forfeited to the vendor.
- Timeframes for deducing title. In accordance with our Conveyancing and Law of Property Act, title may be deduced (i) going back thirty years; or (ii) up to a Grant or lease by the Crown; or (iii) back to a Certificate of Title granted by the court in accordance with the provisions of the Quieting Titles Act.
- Timeframes for liaising with the vendor’s attorney for answers to any requisitions on title.
- Inspection clause (if needed).
- Financing clause (if needed).
- Time frame for completion of the transaction.
- Special conditions specific to the transaction (where applicable).
- Drafting the conveyance (transfer deed) and closing documents.

Bahamas Investment Authority

Pursuant to the International Persons Landholding Act, a foreign national acquiring property in The Bahamas is required to apply for and obtain either a Permit or a Certificate of Registration, which applications are vetted by the Bahamas Investment Authority ("**BIA**"). The Permit application is a pre-closing requirement, so it is important to reference the same in the Agreement for Sale. If the Permit is not approved for any reason, the deposit is typically returned to the Purchaser. In contrast, the Certificate of Registration application is a post-closing requirement. The BIA's main aims are to vet investors to confirm they are not nefarious characters, verify their sources of funds, and monitor their acquisition of property/ies to ensure they are not acquiring for speculative or land banking purposes. Having tirelessly worked to be removed from the European Union's blacklist earlier this year, the BIA plays a crucial role in ensuring The Bahamas is maintaining high international standards to restrict money laundering and terrorism financing. Supporting documents required from an applicant include a police reference from their country of residence, financial reference from a reputable banking institution and a character reference.

Once the Agreement for Sale is agreed by both parties, it is executed, and the deposit is paid in escrow to the vendor's attorney. A purchaser's attorney is responsible for reviewing and approving title within the parameters outlined in the Conveyancing and Law of Property Act.

Ultimately upon completion of the transaction, Value Added Tax ("VAT") of Ten percent (10%) of the purchase price is payable to the Department of Inland Revenue. As a note, our Value Added Tax Act provides the following definition:

"foreign person" means –

(a) an individual who is not –
 (i) a citizen of The Bahamas; or
 (ii) a permanent resident with a right to work in The Bahamas;

(b) a company incorporated in The Bahamas where any of its shares or other capital is legally or beneficially owned by a person who is not a Bahamian or where it is in any manner, whether directly or indirectly, controlled by a person who is not a Bahamian;

(c) a company incorporated at any place outside of The Bahamas;

(d) an unincorporated association or body firm in which any of the partners or members is not a Bahamian or where it is in any manner, whether directly or indirectly, controlled by any person who is not a Bahamian; or

(e) a trust in which any of the trustees or any person having a beneficial interest in the trust is not a Bahamian

Accordingly, any purchaser described in (a) (b) (c) (d) or (e) above must pay VAT of Ten percent (10%) on the acquisition of property in The Bahamas.

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> Once the Agreement for Sale is agreed by both parties, it is executed, and the deposit is paid in escrow to the vendor's attorney.

As it relates to (c) above, a company incorporated outside of The Bahamas must first be registered under the Companies Act, as only Bahamian registered entities may acquire real estate in The Bahamas. There is also the option to incorporate a new Bahamian International Business Company ("**IBC**") to take title. The incorporation of an IBC is more straight forward as opposed to the registration of a foreign company in The Bahamas, which is a document intensive process.

Financing

More and more local commercial banks are lending to foreign nationals for the financing and acquisition of property in The Bahamas. In the instance where a temporary resident (long term work permit holder) is acquiring an owner-occupied property, they may borrow up to B$1,000,000 to finance the transaction. Approval is however required from the Central Bank of The Bahamas for a USD mortgage loan to acquire property.

Conveyance and closing title deeds and documents

The Vendor and Purchaser attorneys shall draft, review, and agree the final form of the conveyance (transfer deed), as well as draft and finalise any other closing deeds or documents, such as mortgages and affidavits.

Post-closing steps

Once a real estate transaction is completed, the post-closing steps include the following:

- Payment of Value Added Tax ("VAT") on the title deeds (conveyance, mortgage, etc.).
- Recording the title deeds at the Registrar General's Department. This step puts the public on notice of the owner of the property and creates priority over subsequently filed deeds.
- Declaration of property with the Real Property Tax Department. Below is a breakdown of applicable taxes based on the type of property:

Real Property and Condo-Hotel Taxes

1. Owner-Occupied – Real Property Tax

FIRST	$300,000	NO TAX
NEXT	$300,000 – $500,000	Taxed at 0.625% (5/8ths)
ABOVE	$500,000	Taxed at 1.0% up to max of $150,000

2. Vacant Land – Real Property Tax

FIRST	$7,000	Taxed of $100
ABOVE	$7,000	Taxed at 2.0%

3. Commercial – Real Property Tax (rentals/property used for business operations)

FIRST	$500,000	Taxed at 0.75%
NEXT	$500,000 to $2,000,000	Taxed at 1%
ABOVE	$2,000,000	Taxed at 1.5%

4. Condo-Hotel Tax

A property owner may place his or her residence in a condo-hotel rental pool/program and receive some tax benefits.

Below is a breakdown of how the condo-hotel tax is calculated using an example value of $1,000,000.00:

- $1,000,000.00 x 0.625% (residential rate as defined under the Real Property Tax Act) = $6,250.00 Condo-Hotel Tax Rate is 75% of the residential rate = $4,687.50
- If the net VAT attributable to the rental of the property is over $4,687.50, condo-hotel taxes will not accrue.
- If the net VAT attributable to the rental of the property is less than $4,687.50, the difference must be paid.
- If the property is not rented at all, the full $4,687.50 is paid.

Central Bank Approvals

The Central Bank has recently relaxed many of the previously required steps a foreign national was required to take on completion of a transaction. Additionally, they have delegated authority to local commercial banks so that foreign nationals can transact business as it relates to their property and generally. Some examples are:

- Approval is no longer required for the repatriation of funds on the sale of non-residential/mixed use property transactions from or to non-residents.
- Maintenance of a current account with a balance up to US$100,000.00.
- Maintenance of a current account to facilitate rental payments up to the amount on the lease.
- Temporary residents may borrow up to a maximum of B$50,000.00 for consumer related purposes and may also obtain a B$ credit card if they qualify for one.

One major incentive of acquiring property in The Bahamas is the opportunity to apply for residency. Why visit when you can live in paradise.

Overview of Residency Options in The Bahamas

Foreign nationals who have purchased or leased property in The Bahamas may apply for residency status to live, or work on an annual or permanent basis. The Bahamas offers multiple options to reside in paradise, including applications for an Economic Permanent Residence, Homeowners Resident Card, Annual Resident Permit, Work Permit, or BH-1B Visa. A brief overview of each residency option is discussed below.

Economic Certificate of Permanent Residency (with or without the right to work)

Currently foreign nationals may qualify for an Economic Certificate of Permanent Residence by making a minimum investment of $750,000 in real estate in The Bahamas. For an additional fee, applicants are also able to apply for a right to work in their own business. An Economic Permanent Resident is able to live in The Bahamas permanently and enjoys most benefits of a Bahamian citizen; however, they will not be able to vote or participate in certain concessions only available to Bahamians. In most instances, a spouse and minor dependents (up to age 18 years old) may also be endorsed on a primary applicant's Certificate of Permanent Residence.

Economic Permanent Residency changes are coming

The Government of The Bahamas recently enacted legislation which will increase the minimum economic investment threshold to qualify for Economic Permanent Residence from $750,000 to $1,000,000 for a minimum period of 10 years. Additionally, investments will be diversified to not only include real estate acquisitions but also purchases of Zero Coupon Bonds from the Central Bank of The Bahamas. The proceeds of these Zero Coupon Bonds shall be used to develop education, health, family island infrastructure or youth and sports in The Bahamas. These new changes will commence on 1st January 2025.

Homeowners Resident Card

The International Persons Landholding Act provides an opportunity for foreign nationals who have purchased a residence in The Bahamas to apply for a Homeowners Resident Card, which is granted for a one-year period and can be renewed annually.

Annual Resident Permit

Foreign nationals who have not purchased a home in The Bahamas may still obtain immigration status in The Bahamas by way of an Annual Resident Permit (also called a "Permit to Reside"). This option grants the applicant residency in The Bahamas for one year and can be renewed on an annual basis. The spouse and dependents of a citizen, economic permanent resident, or work permit holder may also apply for an Annual Resident Permit.

Work Permit (short and long term)

While the Government endeavours to ensure that Bahamians are given priority in relation to employment options in The Bahamas, they do consider and approve work permits for foreign nationals offering specialty skills. Before the Dept. of Immigration considers a work permit application for a foreign national, the prospective employer will need to provide evidence that the job was advertised in the local market with no suitable candidates available. Additionally, a Certificate from the Labour Board will need to be procured indicating there are no Bahamians registered for the position. Short term work permits can be issued for 1 to 90 days. Long Term Work Permits can be issued for 1 to 3 years and can be renewed in most cases.

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> The International Persons Landholding Act provides an opportunity for foreign nationals who have purchased a residence in The Bahamas to apply for a Homeowners Resident Card.

BH-1B Work Visa

The Bahamas has established a programme to encourage foreign business owners in certain industries to move their international operations to The Bahamas. The Commercial Enterprises Act grants work permits to companies investing $250,000 or more in The Bahamas and requiring BH-1B work visas for their management and key personnel. The BH-1B visas are only available in the following industries:

Captive Insurance, Reinsurance, Mutual Fund Administration, Arbitration, Wealth Management, International Trade, International Arbitrage, Computer Programming, Software Design & Writing, Bioinformatics & Analytics, Maritime Trade, Nano Technology, Biomedical Industries, Boutique Health Facilities, Data Storage or Warehousing, Aviation Approved Maintenance Operations, Aviation Registration, Call Centres, Manufacturing or Assembly of Manufactures.

Application Processing Time

The standard processing period for most residency applications is approximately 3 months, however, the Government of The Bahamas recently introduced an expedited service which, for an additional fee, allows most residency applications to be processed within 2 to 3 weeks from the date the application is submitted. **Work Permit** applications require a pre-approval certificate from the Labour Board which may take an additional 3 to 4 weeks processing time. **Economic Permanent Residence** applications, however, take a longer time and average 5 to 8 months processing time. The expedited service is not available for Economic Permanent Residence applications.

Application Fees

All immigration applications must be accompanied by a $200 fee per application (subject to change by the Dept. of Immigration). As an illustration, an application fee for a husband, wife and their child will be a total of $600 ($200 x 3 persons). An expedited application for the same family will be an additional $1,200 ($400 x 3 persons).
The application and expedited fees for the family would total $1,800.00.

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> With its powdery beaches, crystal clear azure waters, golden sunsets, easy travel access, stable government and economy, The Bahamas offers an endless array of investment and residence opportunities.

Supporting documents required for residency applications

Supporting documents vary, however generally residency applications will need to be supported by the following documents:

- Application Form with Bahamian $10.00 stamp for primary applicant and each dependent
- Valid passport for primary applicant and each dependent
- Police certificate for primary applicant and each dependent 16 years of age and over
- Two (2) current passport size photographs for primary applicant and each dependent
- Marriage Certificate (if applicable)
- Birth Certificate for primary applicant and each dependent (if applicable)
- Financial references (for primary applicant and spouse, if applicable)
- Character references (for primary applicant and spouse, if applicable)
- Prior work references (if applicable)
- Education/course certificates in relation to work permit applications
- Registered deed of conveyance (if applicable)
- One year lease/rental agreement (if applicable)
- Evidence of ownership of a primary residence in another jurisdiction (Homeowners card)
- Proof of payment of current Real Property Tax (if applicable)
- International Landholding Certificate or Permit (if applicable)
- Medical certificate for primary applicant and each dependent
- Letter from child's school as evidence of enrollment (if applicable)
- Letter of request addressed to the Director of Immigration
- Certified translations in English with a Bahamian $10.00 stamp
- Apostille or legalisation may be required in some instances
- Other documents (death certificates, divorce decrees, adoption certificates, deed polls, etc.) may be required in certain situations

Conclusion

With its powdery beaches, crystal clear azure waters, golden sunsets, easy travel access, stable government and economy, The Bahamas offers an endless array of investment and residence opportunities for everyone, including the professional bankers, the beach combers, the island bungalow dwellers and the ultra-luxury resort jetsetters. Buying and living in The Bahamas is an incredible opportunity to experience a new culture and lifestyle. Given the increased visitors to The Bahamas and the dynamic foreign direct investment over the past year, we expect to see more and more development in the Bahamian real estate and residency space in the future.

JAPAN

Key developments & the latest trends in Japan – from a legal perspective

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BIO

Fuyuki Uchitsu is a partner who practises in the real estate, construction, structured finance and banking. He handles a wide range of real estate projects, including acquisitions, developments, large-scale redevelopments, management and sale of office buildings, residentials, hotels, retail facilities, and logistics facilities. He also has extensive experience and considerable expertise handling cross-border projects, including US real estate investment and financing as well as inbound investment by foreign investors.

Mori Hamada & Matsumoto has a real estate practice that extends from traditional acquisition and leasing transactions to complex fund structures involving a special purpose vehicle or a trust, or even investment structures for overseas properties. The team's work in this practice primarily involves private fund formation for domestic and overseas properties, J-REITs, real estate acquisition, development and disposition, and real estate financing.

MORI HAMADA & MATSUMOTO

Key developments & the latest trends in Japan – from a legal perspective

Mori Hamada & Matsumoto

1. Current Trends in Real Property Investment into Japan

The Japanese commercial real property market has been active of late, especially attracting attention from overseas investors due to low interest rates and the depreciation of the yen. In the last few years, there have been several large-scale transactions where hotel assets were sold to foreign real estate funds, indicating the strong appetite of foreign funds for Japanese hotels and the recent trend of traditional Japanese companies turning to asset-light strategies. Another trend is rising inflation stimulating investments in inflation-resistant real estate, such as residential, hotel, and retail properties. In contrast, new large-scare development projects have somewhat stalled due to the rising cost of materials and labour.

2. Basic Scheme to Invest in Japanese Real Property from Overseas

Although it is legally possible for a foreign entity to directly or indirectly own real property in Japan, not many overseas investors choose to purchase for reasons of tax efficiency. To achieve this, the following arrangements are often used.

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> In Japan, commercial real property is often traded in the form of a trust beneficial interest (“TBI”).

2.1 Use of Property Trust

In Japan, commercial real property is often traded in the form of a trust beneficial interest (“TBI”) rather than an outright sale and purchase of the real property, to reduce taxes on the real property transfer. In general, when a person acquires outright ownership of real estate, (a) a registration license tax (for the registration of the ownership transfer) and (b) a real estate acquisition tax are imposed, based on the assessed value of the property listed in the fixed property tax register book. In the case of a sale and purchase of a TBI, these tax rates are significantly lower, as shown in the table below (as of September 2024):

	Land		Building	
	Real Property	TBI	Real Property	TBI
Registration License Tax	1.5%	0.3%	2.0%	0.4%
		JPY1,000 for each TBI transfer		JPY1,000 for each TBI transfer
Real Property Acquisition Tax	1.5-3.0%	–	3.0-4.0%	–

When a property trust is used, the ownership of the real property is entrusted to a trustee, which holds the legal ownership of the real property for the benefit of the trust beneficiary (i.e., the TBI holder). The trustee manages the real property in accordance with the terms of the trust agreement and the instructions of the trust beneficiary.

When using a property trust, it should be noted that, in general, the trustee must be a licensed trust bank or trust company, so trust fees and other expenses will be incurred – hence, a property trust is usually used when the investment is above a certain size.

For tax consideration, the property trust usually falls under the category of “beneficiary taxable trust”, in which the beneficiary of the trust is deemed to have assets and liabilities attributable to the trust property, and the income and expenses attributable to the trust property are deemed to be the beneficiary’s income and expenses for corporate and income tax purposes (pass-through taxation).

2.2 Use of Unique Tax Oriented Investment Structure

In order to enhance the tax efficiency in respect of profits generated from a real property or TBI, tax-oriented investment schemes unique to Japan are often employed for real property investments.

There are two commonly used types of investment structures in Japan: (a) the TMK structure and (b) the GK-TK structure. By using TMK or GK-TK structure, double taxation at the level of an asset holding entity (TMK or GK) and its investor (a shareholder in the case of a TMK or a TK investor in the case of a GK-TK structure) can be avoided.

(a) TMK Structure

Overview of TMK

A TMK structure involves a specified purpose company known as *tokutei mokuteki kaisha* (TMK), which is a corporate entity specifically designed to acquire a specific asset (such as real estate assets) by issuing asset-backed securities under the Asset Liquidation Law.

A TMK may acquire real properties either in the form of actual real property or a TBI. Although a TMK can acquire an unlimited number of TBIs, it cannot acquire additional actual real property unless it is closely related to the actual real property already owned by the TMK. The business and operations of a TMK must be conducted in accordance with the asset liquidation plan ("ALP"), one of the constitutional documents of TMK, and a TMK is not permitted to engage in the operational business (e.g., hotel management business).

The TMK's equity consists of "specified shares" and "preferred shares", with no minimum capital requirement. Specified shares are similar to ordinary voting shares of a *kabushiki kaisha*, or a ordinary Japanese stock company. Investments in specified shares is typically nominal (such as JPY100,000) and are not supposed to be used for the acquisition of real properties. Preferred shares comprise most of the TMK's equity.

In general, (i) a TMK finances the acquisition of real properties (in either form) by issuing preferred shares and obtaining third-party debt in the form of "specified bonds" and "specified loans"; (b) a TMK must always have at least one director and one statutory auditor, and should appoint one accounting auditor, who must be either a certified public accountant or an auditing firm; and (c) certain fundamental matters with respect to a TMK require the approval of its shareholders (generally, only specified shareholders have voting rights at shareholders' meetings).

Tax Consideration

The best feature of a TMK is that, by fulfilling certain requirements, it is eligible to deduct profit distributions to its preferred shareholders from its taxable income (pay-through treatment). In practice, the key requirements for a TMK to achieve pay-through treatment are, among other things, the following

(i) The TMK must issue specified bonds to a tax qualified institutional investor ("Tax QII"), as defined in the Act on Special Measures Concerning Taxation;

(ii) If the TMK takes out a specified loan, the lender should be a Tax QII;

(iii) More than 50% of the preferred shares must be offered in Japan;

(iv) More than 50% of the specified shares must be offered in Japan, unless it is stated in the ALP that the specified shareholders have waived their rights to profit distributions and distributions of residual assets; and

(v) The TMK distributes dividends in an amount exceeding 90% of its distributable profit per fiscal year, as calculated under the tax code.

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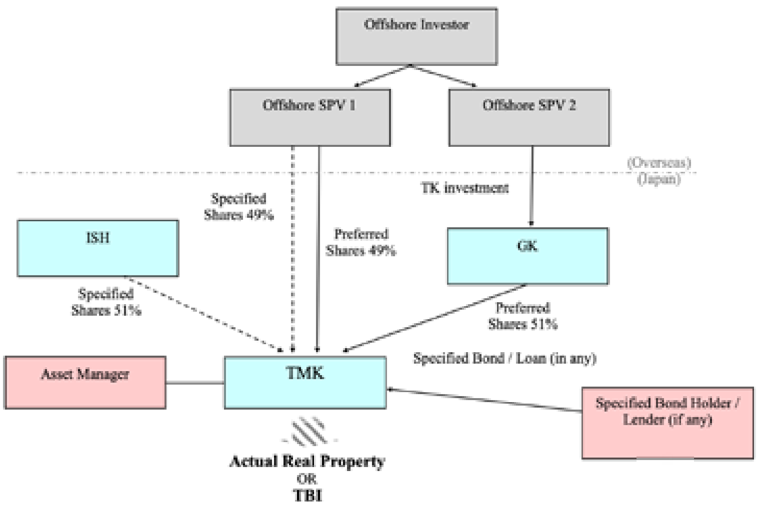
There are two commonly used types of investment structures in Japan: (a) the TMK structure and (b) the GK-TK structure.

Sample TMK structure



(b) GK-TK Structure

Overview of GK-TK

The GK-TK structure is an investment scheme established by a *godo kaisha* (GK), which is a type of Japanese limited liability company, entering into a certain type of partnership agreement, known as *tokumei kumiai* (TK) agreement, with an investor. A TK is just a contractual arrangement formed under a TK agreement between the GK as operator and the TK investor, as a way of creating equity-like investments. If there are several TK investors, each TK investor enters into its own TK agreement with the GK (TK operator), but usually the terms of the TK agreements are the same except for the investment amount.

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> By using TMK or GK-TK structure, double taxation at the level of an asset holding entity can be avoided.

In accordance with the TK agreement, a TK investor contributes funds to the GK (TK operator) and the GK (TK operator) conducts the TK business, which is defined in the TK agreement, using the funds so contributed. Thereafter, the GK (TK operator) distributes profits from the TK business to the TK investor.

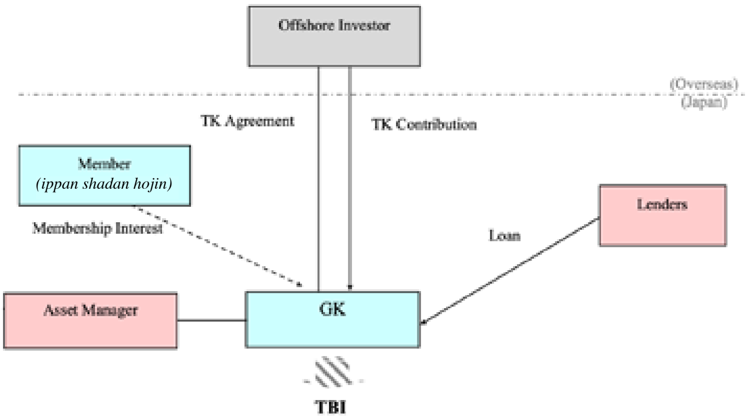
In the GK-TK structure, a GK is incorporated as a special purpose vehicle without human resources, with one corporate entity being the sole managing member representing the GK, and such managing member appoints an individual (operating officer) to act as its representative and perform the duties of a managing member. As there is no specific minimum capital requirement, the paid-in capital of a GK is usually nominal (such as JPY100,000). Due to regulatory and tax reasons, the real property to be acquired under a GK-TK structure is usually in a form of TBI as opposed to actual real property, but a GK-TK can acquire multiple TBIs (including additional acquisitions).

Tax Considerations

In principle, the profits and losses related to the TK business belong to the GK, and corporate tax will be imposed on GK. However, if the TK agreement is legally valid and recognised as a TK for tax purposes, the amount of profit to be distributed to the TK investor or the amount of loss to be borne by the TK investor under the TK agreement may be included in the amount of loss or profit in the calculation of the taxable income of GK for the relevant fiscal year. Therefore, the GK-TK structure enables to avoid the double taxation.

One of the most important points to note is that, because the TK is not a joint venture in a sense that TK operator manages the TK business but the TK investor does not, any form of participation by the TK investor in the TK business (e.g., by way of a right to approve or disapprove material decisions regarding the TK business or otherwise) would invite a risk that jeopardises the characterisation of the nature of the TK from a tax perspective. If the TK agreement involves an non-Japanese TK investor, the tax re-characterisation risk would have a significant implication because the GK (TK operator) would be recognised as a permanent establishment of the TK investor and therefore the profit at the GK level would be subject to regular Japanese income tax. Because of this tax sensitivity, overseas investors tend to avoid the GK-TK structure.

Sample GK-TK structure



3. Asset Manager

As a special purpose vehicle, a TMK or GK must retain an external advisor to ensure the proper management of its business, including the exercise of its rights (e.g., giving instructions to the trustee under the trust agreement for matters relating to the management of the real property) and performance of its obligations under the transaction documents (e.g., preparing and dispatching necessary notices or reports to the lenders under the finance documents) to which it is a party.

The asset manager of a TMK or GK must obtain a certain license, depending on the structure and underlying asset.

Asset Manager for a TMK structure

The type of license required to be obtained by the asset manager of the TMK depends on whether the TMK will acquire actual real property or a TBI.

- If the TMK will acquire actual real property, the TMK needs to sub-contract the management and disposal of the real properties to an asset manager who is licensed to engage in a real estate transaction business (*takuchi tatemono torihiki gyo*) under the Real Estate Transaction Business Law; and
- If the TMK will acquire a TBI, the TMK needs to sub-contract its day-to-day operations, including issuing instructions to the trustee, to an asset manager who is registered to engage in the investment advisory business (toshi jogen gyomu, "**Investment Advisory Business**") or investment management business (toshi un'yo gyo, "**Investment Management Business**") under the Financial Instruments and Exchange Law (the "**FIEL**"), since TBIs fall under the category of securities under the FIEL.

Asset Manager for GK-TK structure

> As a special purpose vehicle, a TMK or GK must retain an external advisor to ensure the proper management of its business.

As mentioned, due to regulatory and tax reasons, the real property acquired under a GK-TK structure is usually in the form of a TBI as opposed to actual real property.

The type of license to be obtained by the asset manager to a GK that will acquire a TBI primarily depends on whether or not there is at least one "qualified institutional investor", as defined in the FIEL (the "**QII**").

- If there is at least one QII, the GK may rely on the QII-targeted Fund Business exemption, which is meant to reduce the regulatory burden normally imposed by the FIEL. In this case, the asset manager must be registered to engage in an Investment Advisory Business or an Investment Management Business; and
- If there is no QII, the GK needs to delegate its entire investment management authority for the benefit of the TK investors to an asset manager who is registered to engage in an Investment Management Business.

4. Requirement of Bankruptcy Remoteness by Lenders

When debt financing is provided to a special purpose vehicle (TMK or GK) purely based on the credibility of the underlying asset, without recourse to the other parties involved in the investment structure (e.g., by way of parent guarantee or otherwise), financiers typically require certain measures so as to minimise the insolvency risk of the special purpose vehicle or to achieve what is often referred to as "bankruptcy remoteness" in Japan. Such measures usually include using an *ippan shadan houjin* (ISH), whose directors are independent from the sponsors (in many cases, two accountants dispatched from a tax accounting firm), as the parent company of the special purpose vehicle. The purpose of having an ISH is to use it as an independent entity holding equity interests in a TMK or GK to achieve bankruptcy remoteness; therefore, the ISH is not expected to have any significant participation in the distribution of profits from the TMK or GK.

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> Structuring an investment in Japanese real property can be complex, bespoke, and require careful consideration from both a legal and tax perspective.

In practice, for the purpose of acquiring working capital for the ISH, the asset manager, investor or other party with an interest in the transaction would contribute capital to the ISH in the form of an endowment (*kikin*), but the contributor has no voting rights or any other right to control the ISH.

5. Conclusion

Structuring an investment in Japanese real property can be complex, bespoke, and require careful consideration from both a legal and tax perspective. It is important for all parties involved to understand what is fundamental to Japanese practice and what is specific to the present case. From this perspective, the roles of the local legal advisor providing structuring advice from a regulatory perspective and the international tax advisor providing tax advice, including tax treaty analysis, are critical. Ultimately, successful structuring can help mitigate financial losses and increase the effectiveness of the investment.

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Veronica is active in the Association of the Luxembourg Fund Industry (ALFI) and the Luxembourg Private Equity & Venture Capital Association (LPEA), participating in working groups and presenting at conferences.

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Ana regularly offers specialist corporate advice to a number of fund and fund manager clients, working regularly side-by-side with our investment management team to provide a full-fledged cross-departmental service to private equity clients.

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Introduction

Looking to raise capital in Europe and around the world and invest in real estate? Choose a Luxembourg investment fund.

Luxembourg's adaptable legal and tax environment has positioned it as a European hub for diverse investment vehicles, particularly real estate funds, catering to global investors' needs. Its robust security interest system bolsters creditor protection, establishing it as a secure global financing domicile. Asset management through pooled funds often involves special purpose vehicles for ringfencing and tax efficiency. With 80+ double tax treaties and evolving corporate laws, Luxembourg provides streamlined options for acquisitions, joint ventures, and employee participation schemes.

Structuring of Luxembourg REIFs

Within a sophisticated Luxembourg toolbox, the choice of the real estate investment fund (**REIF**) vehicle typically depends on the target market in terms of capital raising and investment opportunities. Luxembourg REIFs can take the form of regulated entities, under direct supervision by the CSSF (Luxembourg's regulator), or unregulated entities and can either be managed by a European manager, authorised to market the fund through the European passport regime, or by a registered or non-European manager utilising national private placement regimes to raise funds.

> "Luxembourg's adaptable legal and tax environment has positioned it as a European hub for diverse investment vehicles.

These REIF products can be categorised into two groups: (i) retail REIFs with strict investment limitations and (ii) REIFs tailored for professional and high-net-worth investors offering varying degrees of investment flexibility. For managers pursuing diverse investment strategies, such as targeting specific sectors or regions, Luxembourg REIFs often facilitate the structuring of multi-compartment (or umbrella) vehicles. In an umbrella, each compartment is associated with a distinct investment portfolio segregated from other compartments' portfolios via legal ring-fencing. This ensures that the assets of each compartment solely serve the rights of investors and creditors related to that specific compartment.

Managers aiming at retail investors must structure their Luxembourg REIF as an Undertaking for Collective Investments, governed by Part II of the Law of 17 December 2010 (**Part II UCI**). Part II UCI requires prior approval and ongoing oversight by the CSSF, and the appointment of an alternative investment fund manager (**AIFM**) authorised under the Directive 2011/61/EU on Alternative Investment Fund Managers (**AIFMD**). It stands as Luxembourg's sole alternative investment fund accessible to retail investors. However, the distribution of Part II UCIs to retail investors within the European Economic Area (**EEA**) is contingent upon local regulations in each respective jurisdiction, as there is no European retail passport under the AIFMD.

Part II UCI may invest in diverse real estate assets and strategies, as long as it doesn't allocate over 20% of net assets to a single property (this limit becomes effective upon property acquisition, and after a maximum four-year ramp-up period). Additionally, the aggregate borrowing of Part II UCI cannot exceed an average of 50% of the valuation of its properties.

To facilitate distribution to retail investors in the EEA, managers can incorporate a European Long Term Investment Fund (**ELTIF**) 'wrapper' into their Part II UCI. A Part II UCI, or a compartment thereof, could benefit of the ELTIF label and distribution passport available under the amended Regulation 2015/760, provided the AIFM is EU-authorsied, and over 55% of capital is invested in eligible real assets. ELTIFs can only be set up as master-feeder structures, provided both the feeder and the master are ELTIFs, and fund-of-fund ELTIFs can only target European AIFs. ELTIFs also entail stricter governance rules than Part II UCIs without ELTIF wrapper, in particular in respect of duration and redemption mechanisms.

ELTIF lures retail investors in EEA with distribution passport whereas Part II UCI offers structuring flexibilities. There is growing interest in hybrid models with ELTIF compartments under umbrella Part II UCIs.

Managers targeting professional and semi-professional investors can opt for various Luxembourg REIF regimes:
(i) Specialised Investment Fund (**SIF**) under the Law of 13 February 2007
(ii) Investment Company in Risk Capital (**SICAR**) under the Law of 15 June 2004
(iii) Reserved Alternative Investment Fund (**RAIF**) under the Law of 23 July 2016

These REIFs are reserved to 'well-informed investors', i.e., institutional investors, professional investors and investors who have confirmed in writing that they adhere to the well-informed investor status, and who either invest a minimum of EUR 100,000 or have been assessed by an eligible financial institution.

SIFs and SIF-like RAIFs can invest in various real estate assets and pursue any real estate strategy, subject to a 30% concentration rule. SICARs and SICAR-like RAIFs are not subject to diversification requirements but may only invest indirectly via entities in 'risk capital' qualifying assets with an intention to develop a project (no core/core plus strategies).

SIFs and SICARs require prior CSSF approval, while RAIFs are formed and operate without CSSF's involvement. However, whereas SIFs and SICARs may be managed by registered or non-European AIFMs, a RAIF must appoint an EU-authorised AIFM.

It is also possible to structure a Luxembourg REIF outside the ambit of product laws, taking on any Luxembourg corporate form, contingent on AIFMD compliance. The most favoured entity is the Luxembourg special limited partnership, functioning as an alternative investment fund, managed by an EU-authorised AIFM, registered European AIFM, or non-European AIFM, depending on assets under management, and the requirement for a European marketing passport to raise capital. Such REIFs are exempt from CSSF supervision and investment constraints.

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> ELTIF lures retail investors in EEA with distribution passport whereas Part II UCI offers structuring flexibilities.

Except SICARs,
Luxembourg REIFs can be SICAVs (variable capital investment companies) or FCPs (co-ownership managed by Luxembourg management company). A SICAV is a Luxembourg company (of any type) whose capital constantly fluctuates, without any further formalities, with changes in subscriptions, redemptions and valuation of assets, so that it is at all times equal to the net asset value of the company (i.e., the value of its assets minus liabilities). An FCP is not a legal entity. Investors subscribe for units in the FCP which represent a portion of the net assets, and they are only liable up to the amount they have contributed. Voting rights are typically absent for FCP investors, and decisions regarding investments and operations rest with the management company, unless otherwise specified in fund documentation.

The administration of a Luxembourg REIF requires the appointment of a Luxembourg depositary, responsible for verifying asset ownership. Eligible depositaries encompass Luxembourg credit institutions and professional depositaries for assets other than financial instruments.

The annual report of a Luxembourg REIF must be audited by a Luxembourg authorised independent auditor (*réviseur d'entreprises agréé*). Luxembourg GAAP and IFRS are the applicable accounting standards, except for unregulated alternative investment funds in the form of special limited partnerships.

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> Luxembourg's adaptable legal and tax environment has positioned it as a European hub for diverse investment vehicles.

The registered office and central administration of a Luxembourg REIF must reside in Luxembourg. Hence, in instances where adequate internal resources are lacking, the appointment of a domiciliary and fund administrator, overseen by the CSSF, is necessary for the administration of a Luxembourg REIF.

External financing solutions for Luxembourg REIFs

External financing solutions are available to managers of Luxembourg REIFs at all levels of the capital structure.

The subscription line financing is a useful liquidity tool, frequently used by REIF managers. Also called, capital call facility, this financing is provided by lenders directly to the fund, where the recourse of the lenders is to the uncalled investor commitments of the fund. These arrangements are usually short-term facilities used to bridge the capital contributions of the investors and are subject to a borrowing base, determined by the value of the investors' available commitments satisfying certain eligibility criteria. Typically, the security package is comprised of a pledge by the fund of its rights under the uncalled investors' commitments, and the claims against the investors in relation thereto, as well as of a pledge over the bank account dedicated to investors' contributions.

Luxembourg REIFs' managers may also have access to net asset value (NAV) or asset-backed financing arrangements. These borrowing arrangements are facilities made available to the fund (or an SPV held by the fund) with recourse to the fund's portfolio of assets. Given that the borrowing base is calculated on the net asset value of the assets of the fund (being the primary source of repayment), this financing product is usually made available at an advanced stage of the investment period, once the REIF has acquired sufficient investments. Lenders will analyse the underlying investments, as well as cash flows and other distributions that the REIF will receive from those investments. The security package may be composed of pledge over shares, receivables, loans and/or bank accounts into which investments proceeds are to be paid with the aim to allow the lender to control the underlying assets or distributions paid on such assets. NAV facilities may be used for working capital, follow-on investments, distributions or provide liquidity to distressed portfolio companies.

Hybrid products combining subscription financing and NAV financing features may also be used by Luxembourg REIFs.

At asset level, a secured loan made by third party lenders remains the key financing tool for managers of REIFs, with two main types of product: the investment loan (financing of an existing property let to existing tenants) and the development loan (financing of a purchase and development of a property). The borrowing entity is usually the company holding the real estate asset and the typical security package for these financings are a mortgage over the financed property, as well as security interests over any other of the borrower's assets, such as bank accounts into which any accounts or proceeds are paid. It is also common for the shareholder of the borrower to pledge all its interests (shares and claims) in the borrower. In addition, in a development loan, lenders will also seek to take security over the rights of the developer in respect of any development documents during the construction phase. Lenders may also require that the REIF provides credit support for the obligations of the borrowing entities (notably equity commitment letters or guarantees).

Where the amount of the loan to be advanced (combined with the REIF's equity contribution) is not sufficient to finance the project, mezzanine financing solutions, which will be structurally or contractually subordinated to the senior lenders' debt, can be implemented to bridge the gap.

A view from underneath the REIF – SPVs, co-investments, and joint ventures

In addition to being the jurisdiction of choice for the establishment of the fund, Luxembourg is also a suitable destination for the asset acquisition structure of the REIF due to its flexible but predictable tax, legal, regulatory and general commercial environment. In addition, Luxembourg collateral law offers a unique blend of flexibility and certainty for the creation, perfection and enforcement of security interests (in particular over the shares of a Luxembourg company), making Luxembourg a jurisdiction of choice for structuring leveraged finance transactions in particular.

An important point of attention from a Luxembourg law perspective is the fact that Luxembourg follows the "real seat" theory, which means that - unlike other jurisdictions such as the Netherlands, Ireland and the United Kingdom, which follow the "incorporation" theory - a Luxembourg entity is considered to be a Luxembourg entity and subject to Luxembourg law only, to the extent that it has its "real seat" in Luxembourg. Many different terms are used in connection with this concept - 'central administration', 'principal place of business', 'effective management', 'domicile' - with Luxembourg company law referring to both 'central administration' and 'domicile'. Under Luxembourg company law, there is a rebuttable presumption as a matter of law that the central administration of a company is located at the address of its registered office.

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Luxembourg is also a suitable destination for the asset acquisition structure of the REIF due to its flexible but predictable tax, legal, regulatory and general commercial environment.

The presence or substance of the company in Luxembourg may also be a condition for access to tax benefits (in particular under tax treaties). In the case of a tax transparent fund, such access to tax treaty benefits may be particularly important for the Luxembourg company (typically a SARL and often referred to as a Master HoldCo) that sits immediately below the REIF, and is used by the REIF as an investment platform.

A chain of Luxembourg companies is often involved in the acquisition structure set up below the Master HoldCo in order to meet the various liability shield, tax or financing structuring requirements. For investments of a REIF, the Luxembourg *société à responsabilité limitée* (SARL) remains the most popular choice for financing entities and acquisition vehicles further down the chain.

A leveraged acquisition structure will typically include at least one other mid-tier holding SARL above the SPV used to invest in the property, with additional holding SARLs potentially added to the chain to facilitate co-investments or joint ventures.

While typical joint ventures between the REIF (via a chain of subsidiaries) and the asset manager are designed to marry the interests of the capital provider with the expertise and asset servicing knowledge of the asset manager, while ensuring that the manager has sufficient "skin in the game", co-investments are becoming increasingly popular with investors seeking to gain more direct exposure to interesting and attractive assets, while benefiting from a better deal on fees, or a better grip on governance and exit strategy.

A wide range of financing structures are available under Luxembourg law. Typically, transactions are funded by investors through a variety of different financing instruments, split between equity (ordinary shares, preference shares, warrants) and debt (loans, bonds, preference shares), with most transactions involving a combination of two or more such instruments. Bank financing is typically secured by pledge agreements (most commonly share pledges, receivables pledges and account pledges).

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> On the investment side, the first half of the year has remained challenging despite observers expecting recovery in 2024.

In terms of exit, the most common full exit mechanism is the sale of the SPV holding the assets, followed by the liquidation of the holding stack. In a partial exit scenario, cash is returned to the REIF through share redemptions, dividend distributions or debt repayments, or a combination of these.

Luxembourg Real Estate Market Overview

On the investment side, the first half of the year has remained challenging despite observers expecting recovery in 2024. The economic situation is solid in Luxembourg, notably due to low unemployment. A recovery of the investment market is expected in the second half of 2024, driven by an increase in rents (notably for offices) and confidence that expected and proposed yields will rebalance. The Luxembourg market remains attractive, especially in the office market, which remains stronger than in other EU countries due to Luxembourg having one of the lowest office vacancy rates in the region.

Insofar as residential real estate is concerned, Luxembourg's real estate market is characterised by high demand, limited supply, and soaring property prices, making affordability a significant challenge for many residents. In order to support the construction sector and respond to the housing crisis that Luxembourg is going through, the Luxembourg government coalition has made the housing crisis one of its priorities. Measures have been announced to boost housing construction and reduce costs, focusing on affordability and social cohesion. Key initiatives include increased tax credits and subsidies, higher thresholds for tax-exempt property transactions, and a temporary reduction in taxes on added property value. The government will also acquire 800 homes for affordable rent and invest nearly €1 billion in public housing projects over the next two years. A national housing conference is planned to address long-term strategies, and structural reforms will increase tax deductions for homeowners and provide significant tax exemptions for properties under social rental management.

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Alan graduated with an LLB (Hons) from the University of London in 2012 and obtained his Certificate in Legal Practice before being admitted to the Malaysian Bar. His practice areas include real estate, corporate, and commercial law. Alan has extensive experience in handling real estate transactions, including commercial projects, property sales, purchases, leases, and tenancies. In the corporate and commercial field, Alan has advised on corporate acquisitions, restructuring, joint ventures, share sales, and employee share option schemes. He has also assisted Malaysian start-ups, consulting firms, and technology companies. Notable transactions include advising on RM30 million corporate banking facilities for a leading shipping company, collaborating with fintech companies across 10 countries, and assisting a property developer in securing regulatory approvals for foreign currency borrowing. Alan's expertise spans both local and international transactions, making him a trusted advisor in his field.

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Akiel is currently a legal intern at Amanda Pang & Yee and a third-year law student at Multimedia University, distinguished by earning the Dean's List Award for four consecutive semesters. Fluent in Bahasa Melayu, English, Mandarin, and with basic proficiency in Thai and French, he has accumulated significant experience through internships at leading law firms, including Shook Lin & Bok, Zul Rafique & Partners, RDS Partnership and Amanda Pang & Yee. His expertise covers Litigation, Intellectual Property, Corporate and Commercial. Akiel also serves as President of the Asian Law Students' Association International Board, following his tenure as President of the Malaysian Chapter, showcasing his strong leadership abilities. His previous roles with the Malaysian Law Student Network and the Multimedia University Law Society, combined with his volunteer work as a Student Coordinator during the 2023 Malaysian State Election and as a peer tutor in his faculty, highlight his well-rounded qualifications for a successful legal career.

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1. Introduction

1.1 Overview of Malaysia's Real Estate Market

Historical Development: Malaysia's real estate market has evolved significantly over the decades. From its early development phases in the post-independence era, the market has transitioned from primarily residential projects to a diverse array of high-end commercial properties, integrated townships, and mega real estate developments. Key phases include the rapid urbanization in the 1980s, the boom in high-rise residential and commercial properties in the 1990s, and the focus on sustainable and smart city developments in recent years.

International Interest: Malaysia's real estate sector has increasingly attracted international investors due to its strategic location, favourable climate, and growing economy. Key investor groups include entities from China, Singapore, and Japan, drawn by Malaysia's stable economic environment, relatively affordable property prices, and robust infrastructure development.

1.2 Purpose and Significance of the Study

Understanding Foreign Investment Trends: Analysing foreign investment patterns helps in understanding their impact on the local market, including shifts in property demand, price adjustments, and the broader economic effects. It also aids in forecasting future investment trends and identifying key areas of growth.

> "Recent data indicates a steady increase in foreign investment in Malaysia's real estate sector.

Impact of Policy Changes: Recent regulatory changes, including updates to the Malaysia My Second Home (MM2H) programme and the introduction of Special Economic Zones (SEZs), have significant implications. These policies affect foreign investor access and property market dynamics, influencing both investment decisions and market conditions.

2. Foreign Investment in Malaysian Real Estate

2.1 Trends in Foreign Investment

Analysis of Recent Foreign Investment Trends: Recent data indicates a steady increase in foreign investment in Malaysia's real estate sector. Notable investments include high-profile projects such as the development of Forest City, which underscores Malaysia's attractiveness as a prime investment destination. Foreign investment volumes have been bolstered by Malaysia's strategic location and its status as a business hub in Southeast Asia.

Popular Regions and Property Types: Foreign investors are particularly interested in Kuala Lumpur, Johor Bahru, and Penang. These regions offer a combination of strategic advantages, including strong infrastructure, vibrant economic activities, and appealing lifestyle options. Investment preferences range from high-end residential properties to commercial real estate and integrated townships.

2.2 Key Factors Attracting Foreign Investors

Affordable Property Prices: Compared to neighbouring countries like Singapore and Hong Kong, Malaysia's property prices are relatively competitive. This affordability, combined with the potential for capital appreciation, makes Malaysia an attractive investment destination.

Strategic Location and Infrastructure Development: Malaysia's geographic location as a gateway between Asia and the rest of the world, coupled with its ongoing infrastructure projects, such as the Kuala Lumpur-Singapore High-Speed Rail, enhances its appeal. These developments improve connectivity and accessibility, further attracting foreign investors.

Investment Returns and Capital Appreciation Potential: Areas such as Kuala Lumpur's city centre and Johor Bahru's waterfront developments show high potential for value appreciation and rental yields. Investors are drawn to these regions due to their potential for significant returns on investment.

3. Legal and Regulatory Framework

3.1 Restrictions on Foreign Ownership

Minimum Property Price Thresholds: Foreign ownership of residential properties in Malaysia is subject to minimum price thresholds, which vary by state. For example, in Kuala Lumpur and Johor, the threshold is typically set at RM1 million, while other states may have different requirements. These thresholds aim to regulate foreign investment and ensure that it aligns with local market conditions.

Regulations and Conditions for Foreign Ownership: Foreign buyers must adhere to specific regulations, including obtaining approval from the Foreign Investment Committee (FIC) for certain transactions. Legal constraints also include restrictions on the types of properties that can be purchased, typically focusing on high-end residential and commercial properties.

Differences in Regulations Across States: There are variations in regulations between states, impacting foreign investment. For example, Kuala Lumpur and Johor Bahru have higher price thresholds and more stringent approval processes compared to other regions. These differences can influence investor decisions and market dynamics.

3.2 Taxation Policies

Real Property Gains Tax (RPGT): RPGT applies to gains from the sale of real property, with rates varying based on the holding period. For properties held for less than five years, the RPGT rate is 30%, while it reduces progressively for longer holding periods. Recent exemptions and reliefs have been introduced to support market stability.

Stamp Duties and Other Related Taxes: Foreign buyers are subject to stamp duties on property purchases. The rates are generally consistent across Malaysia, with the duty ranging from 1% to 4% based on the property value. Other taxes include legal fees and property management charges, which are relevant for investors to consider.

3.3 Regulatory Changes and Their Impacts

Recent Regulatory Amendments: Recent changes, such as the revision of RPGT rates and adjustments in foreign ownership regulations, impact foreign investment. These amendments aim to balance the interests of local and foreign investors and ensure a sustainable property market.

Government Policies to Curb Speculative Buying: Measures to prevent speculative buying include increased transparency in property transactions and stricter enforcement of minimum price thresholds. These policies aim to stabilize the market and prevent potential bubbles.

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> Areas such as Kuala Lumpur's city centre and Johor Bahru's waterfront developments show high potential for value appreciation and rental yields.

4. Financing Options for Foreign Investors

4.1 Access to Local Financing

Availability of Home Loans and Mortgages: Foreign investors can access home loans from Malaysian banks, including Public Bank and AmBank. These institutions offer tailored financing solutions for property purchases. Public Bank provides competitive interest rates and flexible loan terms, while AmBank offers a range of mortgage products with attractive features for foreign buyers.

Loan-to-Value (LTV) Ratio and Interest Rates: LTV ratios for foreign buyers typically range from 70% to 80%, depending on the financial institution and the investor's profile. Interest rates are competitive but may be slightly higher for foreign buyers compared to local rates. It's advisable for investors to compare offers from different banks to secure the best terms.

4.2 Alternative Financing Options

Private Financing and International Banks: Beyond local banks, foreign investors can explore private financing options and loans from international banks. These alternatives can provide additional flexibility and customized solutions for high-value investments.

Joint Ventures and Partnerships: Joint ventures with local entities offer another financing route. Partnering with Malaysian developers or investors can provide access to local expertise, market knowledge, and additional funding sources.

> "Beyond local banks, foreign investors can explore private financing options and loans from international banks.

4.3 Currency Risks and Mitigation Strategies

Impact of Currency Fluctuations: Currency fluctuations can impact the cost of investments and returns. Investors should monitor exchange rates and consider the potential effects of currency volatility on their investments.

Hedging and Financial Strategies: Hedging strategies, such as forward contracts and currency swaps, can mitigate currency risks. Investors should consult with financial advisors to implement effective risk management strategies and protect their investments from adverse currency movements.

5. Malaysia My Second Home (MM2H) Programme

5.1 Overview of the MM2H Programme

Introduction and Objectives: The MM2H programme offers long-term residency options to foreigners, aiming to attract retirees and high-net-worth individuals. Benefits include multi-year visas and property ownership privileges, designed to enhance Malaysia's appeal as a destination for long-term living and investment.

Key Benefits: Participants in the MM2H programme enjoy benefits such as the ability to purchase residential properties with fewer restrictions, access to Malaysia's healthcare system, and the opportunity to live in a country with a high quality of life.

5.2 Evolution of the MM2H Programme

History and Changes: The MM2H programme has evolved since its inception in 2002, with various changes to eligibility criteria and benefits. Recent updates reflect a focus on attracting higher-value investors and digital nomads, aligning the programme with current market trends.

Comparison of Old and New Versions: The latest version of MM2H includes stricter financial requirements and a focus on high-net-worth individuals, compared to previous iterations. Changes aim to enhance the programme's effectiveness in attracting long-term, financially stable residents.

5.3 Introduction of MM2H 3.0

Three-Tier System Overview: The MM2H 3.0 introduces a three-tier system, offering different levels of benefits based on the applicant's financial status and investment contributions. This system aims to streamline the application process and provide tailored benefits.

Removal of Offshore Income Requirement: The removal of the offshore income requirement under MM2H 3.0 simplifies the application process, making it more accessible for potential residents with diverse income sources.

Focus on High-Net-Worth Individuals and Digital Nomads: MM2H 3.0 targets high-net-worth individuals and digital nomads, reflecting a shift towards attracting investors and professionals who contribute significantly to the local economy.

Restrictions to West Malaysia: MM2H 3.0 applies exclusively to West Malaysia, excluding Sabah and Sarawak. This focus on West Malaysia aligns with development priorities and infrastructure readiness in the region.

6. Malaysia My Second Home (MM2H) Special Economic Zones Programme

6.1 Overview of the MM2H SEZ Programme

Explanation of the MM2H SEZ Initiative: The MM2H SEZ programme establishes special zones within Malaysia to attract high-value investments and enhance economic growth. These zones offer favourable conditions for foreign investors and aim to boost local development.

Objectives and Targeted Outcomes: The SEZ programme's objectives include stimulating investment in targeted areas, fostering economic development, and creating job opportunities. The programme aims to leverage foreign investment to drive local economic growth.

6.2 Key Features of the MM2H SEZ Programme

Eligibility Criteria: To qualify for the SEZ programme, investors must meet specific financial and investment criteria, including minimum investment thresholds and economic contributions. These criteria are designed to ensure that participants contribute meaningfully to the local economy.

Incentives Offered: The SEZ programme provides various incentives, such as tax exemptions and relaxed property ownership rules. These incentives are intended to attract high-value investments and facilitate business operations within the zones.

Designated SEZ Locations: Specific regions designated as SEZs include key economic hubs with strong infrastructure and development potential. These locations are chosen for their strategic significance and growth prospects.

6.3 Economic and Real Estate Impact

Impact on Local Real Estate: The SEZ programme influences local property markets by increasing demand for real estate in designated zones. This increased demand can lead to higher property values and more dynamic market conditions.

Contribution to Economic Growth: The SEZ programme is expected to contribute to economic growth by attracting foreign investment, creating job opportunities, and stimulating local businesses. Its impact extends beyond real estate, benefiting various sectors of the economy.

6.4 Challenges and Considerations

Potential Risks: Risks associated with the SEZ programme include market saturation and uneven development. Investors and policymakers must address these challenges to ensure sustainable growth and balanced development.

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> The SEZ programme provides various incentives, such as tax exemptions and relaxed property ownership rules.

Regulatory and Legal Concerns: The SEZ programme may face regulatory and legal challenges, including compliance with local laws and international standards. Effective governance and oversight are crucial to managing these concerns and ensuring the programme's success.

7. Impact of the MM2H Programmes on the Local Market

7.1 Effects on Property Demand

Influence of the MM2H Programmes on Property Demand: The MM2H programmes have significantly influenced property demand in various regions. Areas with higher concentrations of MM2H participants experience increased demand for residential properties, particularly in states like Kuala Lumpur and Johor.

Shifts in Buyer Demographics and Preferences: There have been noticeable shifts in buyer demographics, with retirees and digital nomads becoming prominent participants in the MM2H programmes. These changes affect market trends and property preferences, leading to increased demand for lifestyle-oriented properties.

7.2 Market Segmentation

Impact on Luxury, Mid-Range, and Affordable Property Segments: The MM2H programmes have varying impacts on different property segments. Luxury properties see heightened demand from high-net-worth individuals, while mid-range and affordable segments experience shifts due to changes in buyer preferences and economic conditions.

Potential Oversupply or Undersupply in Specific Sectors: The influx of foreign investment and MM2H participants can lead to potential oversupply or undersupply in certain property sectors. Market analysis and forecasting are essential to address these imbalances and ensure sustainable development.

7.3 Broader Economic Implications

Contribution to Local Economies and Property Development: The MM2H programmes contribute to local economies by generating income, creating jobs, and stimulating property development. These benefits extend to various sectors, enhancing the overall economic landscape.

> "Malaysia's political environment can present risks, including policy changes and political instability.

Long-Term Effects on Malaysia's Global Real Estate Reputation: The success of the MM2H programmes strengthens Malaysia's reputation as a global real estate investment destination. Positive outcomes enhance Malaysia's appeal to international investors and contribute to its standing in the global market.

8. Challenges and Risks for Foreign Investors

8.1 Political and Economic Stability

Risks Associated with Malaysia's Political Environment: Malaysia's political environment can present risks, including policy changes and political instability. Investors should stay informed about political developments and their potential impact on real estate investments.

Economic Factors Influencing Real Estate Investment: Macroeconomic factors such as inflation, economic growth, and interest rates influence real estate investments. Monitoring these factors helps investors make informed decisions and manage potential risks.

8.2 Market Volatility

Real Estate Market Cycles and Potential Investment Risks: Real estate market cycles can affect investment outcomes. Investors should be aware of market trends and cycles to mitigate risks associated with market fluctuations.

Impact of Global Economic Conditions on Malaysia: Global economic conditions, such as economic downturns and geopolitical shifts, can impact Malaysia's real estate market. Investors should consider these external factors when planning their investments.

8.3 Legal Disputes and Property Rights

Common Legal Issues Faced by Foreign Investors: Foreign investors may encounter legal issues such as disputes over property titles or land use. Understanding the legal framework and seeking legal advice can help address these challenges.

Dispute Resolution Mechanisms and Investor Protection: Malaysia offers various dispute resolution mechanisms, including arbitration and legal recourse through local courts. These frameworks are designed to protect foreign investors and ensure fair resolution of disputes.

9. Outlook of the Malaysian Real Estate Market

9.1 Current Market Conditions

Overview of the Current State of the Malaysian Real Estate Market: The Malaysian real estate market is currently experiencing a period of adjustment, with stable property prices and a balanced supply-demand dynamic. Recent trends indicate a gradual recovery and potential for growth in specific sectors.

Trends in Property Prices, Supply, and Demand: Property prices have shown stability with moderate fluctuations. Supply and demand trends reflect ongoing developments and shifts in buyer preferences, influencing market conditions.

9.2 Predicted Trends and Opportunities

Future Trends in Foreign Investment and Emerging Hotspots: Future trends suggest continued interest from foreign investors, with emerging hotspots including Kuala Lumpur's central business district and Johor Bahru's waterfront areas. These locations are expected to attract significant investment due to their strategic advantages.

Potential Growth Sectors and Investment Opportunities: High-growth sectors such as eco-friendly developments and commercial real estate offer promising investment opportunities. Investors should explore these areas for potential returns and growth.

9.3 Impact of Global Events

Influence of International Events: Global events, including pandemics and geopolitical shifts, impact Malaysia's real estate market. These events can affect investor sentiment and market dynamics, necessitating adaptability and strategic planning.

9.4 Policy Recommendations

Suggestions for Improving the Regulatory Environment: Recommendations include streamlining approval processes, enhancing transparency, and providing incentives for high-value investments. These measures aim to improve Malaysia's attractiveness as an investment destination.

Strategies for Making Malaysia More Attractive to Foreign Investors: Strategies include marketing initiatives, infrastructure improvements, and targeted incentives. Implementing these strategies can enhance Malaysia's appeal and competitiveness in the global real estate market.

10. Conclusion

10.1 Summary of Key Findings

Recap of Main Points: The article highlights key trends in foreign investment, the impact of MM2H programmes, and the challenges faced by investors. It provides a comprehensive overview of the Malaysian real estate market and the regulatory framework affecting foreign investments.

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> The Malaysian real estate market is currently experiencing a period of adjustment, with stable property prices and a balanced s upply-demand dynamic.

10.2 Final Thoughts on Foreign Investment in Malaysian Real Estate

Overall Assessment: Malaysia remains a compelling destination for real estate investment, with a stable market, strategic location, and favourable policies. The MM2H programmes and SEZ initiatives further enhance its appeal to foreign investors.

10.3 Recommendations for Investors

Practical Advice: Foreign investors should focus on emerging hotspots, stay informed about regulatory changes, and consider local financing options from institutions like Public Bank and AmBank. Engaging with local experts and conducting thorough market research will support informed investment decisions.

AMANDA PANG & YEE
ADVOCATES & SOLICITORS

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