PROPOSED MODEL STATUTE FOR DISALLOWANCE OF DEDUCTIONS FOR PAYMENTS TO CAPTIVE REAL ESTATE INVESTMENT TRUSTS

(a) As used in this [Section/Statute/Act], the term:

(1) 'Real estate investment trust' means an entity that has elected such status for federal income tax purposes and meets the requirements of Section 856 of the Internal Revenue Code of 1986, as amended, and also includes:

   (a) Any qualified real estate investment trust subsidiary under Section 856(i) of the Internal Revenue Code of 1986, as amended, other than a qualified REIT subsidiary of a 'captive real estate investment trust';

   (b) Any Listed Australian Property Trust, meaning an Australian unit trust registered as a 'Managed Investment Scheme' under the Australian Corporations Act in which the principal class of units is listed on a recognized stock exchange in Australia and is regularly traded on an established securities market, or an entity organized as a trust, provided that a Listed Australian Property Trust owns or controls, directly or indirectly, 75 percent or more of the voting power or value of the beneficial interests or shares of such trust; or

   (c) Any qualified foreign entity, meaning a corporation, trust, association or partnership organized outside the laws of the United States and which satisfies the following criteria:

      (i) At least 75 percent of the entity's total asset value at the close of its taxable year is represented by real estate assets, as defined at Section 856(c)(5)(B) of the Internal Revenue Code of 1986, as amended, thereby including shares or certificates of beneficial
interest in any real estate investment trust, cash and cash equivalents, and U.S. Government securities;

(ii) The entity is not subject to tax on amounts distributed to its beneficial owners, or is exempt from entity-level taxation;

(iii) The entity distributes at least 85 percent of its taxable income, as computed in the jurisdiction in which it is organized, to the holders of its shares or certificates of beneficial interest on an annual basis;

(iv) Not more than 10 percent of the voting power or value in such entity is held directly or indirectly or constructively by a single entity or individual, or the shares or beneficial interests of such entity are regularly traded on an established securities market; and

(v) The entity is organized in a country which has a tax treaty with the United States.

(2) 'Captive real estate investment trust' means any real estate investment trust the shares or beneficial interests of which are not regularly traded on an established securities market, and more than 50 percent of the voting power or value of the beneficial interests or shares of which are owned or controlled, directly or indirectly, or constructively, by a single entity that is:

(A) Treated as an association taxable as a corporation under the Internal Revenue Code of 1986, as amended; and

(B) Not exempt from federal income tax pursuant to the provisions of Section 501(a) of the Internal Revenue Code of 1986, as amended.
(3) Except as otherwise provided in this Code section, a real estate investment trust that is intended to be regularly traded on an established securities market, and that satisfies the requirements of Section 856(a)(5) and (6) of the Internal Revenue Code of 1986, as amended, by reason of Section 856(h)(2) of the Internal Revenue Code of 1986, as amended, shall not be deemed a captive real estate investment trust within the meaning of this Code section unless it does not become regularly traded on an established securities market within one year of the date on which it first becomes a real estate investment trust. For purposes of this subsection, a real estate investment trust becomes a real estate investment trust on the first day that it has both met the requirements of Section 856 of the Internal Revenue Code of 1986, as amended, and has elected to be treated as a real estate investment trust pursuant to Section 856(c)(1) of the Internal Revenue Code of 1986, as amended.

(4) "Related member" means a person that, with respect to the taxpayer during all or any portion of the taxable year, is: (1) a related entity, (2) a component member as defined in subsection (b) of section 1563 of the Code; (3) a person to or from whom there is attribution of stock ownership in accordance with subsection (e) of section 1563 of the Code; or (4) a person that, notwithstanding its form of organization, bears the same relationship to the taxpayer as a person described in (1) to (3), inclusive.

(b) For purposes of computing [State] taxable net income, a taxpayer shall add back all expenses and costs directly or indirectly paid, accrued, or incurred to a captive real estate investment trust. Such expenses and costs shall be added back in the calculation of [State] net income before the income is apportioned or allocated as provided by [UDITPA].
(c) The amount of the adjustment required by subsection (b) of this Code section shall be reduced, but not below zero, to the extent the corresponding expenses and costs received as income by the captive real estate investment trust are reduced by the proportionate amount of expenses that have been allowed in computing the captive real estate investment trust's federal taxable income and that have not been paid, accrued or incurred by the captive real estate investment trust to persons that are related members.

(d) The amount of the adjustment required by subsection (b) of this Code section shall be further reduced, but not below zero, to the extent the expenses and costs are:

(1) received as income in an arm's length transaction by the captive real estate investment trust; and

(2) the corresponding net income of the captive real estate investment trust or its shareholders is taxed by this State or another state at a cumulative effective tax rate of not less than _% .

(e) In claiming the reductions allowed by subsections (c) or (d), the taxpayer shall disclose on its return, with respect to the captive real estate investment trust and its shareholders, the name, the federal identification number, the name of each state, the amount of the expenses and costs allocated or apportioned to and taxed by each state, and such other information as the commissioner may prescribe. Failure to make this disclosure on the return shall preclude the taxpayer from utilizing the reductions provided in those subsections.
(f) Nothing in this Code section shall require a taxpayer to add to its [State] taxable net income more than once any amount of expenses and costs that the taxpayer pays, accrues, or incurs to a captive real estate investment trust.

(g) For purposes of this Code section, the constructive ownership rules of Section 318(a) of the Internal Revenue Code of 1986, as amended, as modified by Section 856(d)(5) of the Internal Revenue Code of 1986, as amended, shall apply in determining the ownership of stock, assets, or net profits of any person.

(h) In addition to other penalties imposed by [this title], the penalty for failure to make the adjustment required by this Code section shall be 10 percent of the additional tax that results because of this Code section. The Commissioner may waive this penalty when the Commissioner determines that the failure to make the adjustment required in subsection (b) was due to reasonable cause and not due to gross negligence or willful neglect or disregard of the law.

(i) Nothing in this Code section shall be construed to limit or negate the Commissioner's authority to:

(1) make adjustments under [Section 482 authority];

(2) use alternative apportionment rules as allowed by [UDITPA Section 18]; or

(3) enter into agreements and compromises otherwise allowed by law.

(j) The Commissioner is authorized to prescribe forms and promulgate rules and regulations deemed necessary in order to effectuate this Code section."