



MULTISTATE TAX COMMISSION

Working together since 1967 to preserve federalism and tax fairness

Resolution Adopting Model Statute for Disallowance of Deductions for Payments to Captive Real Estate Investment Trusts as Recommendation to the States

Whereas, in 2008 the Commission adopted a Model Statute for the Taxation of Captive Real Estate Investment Trusts (“REITs”) which prevents inappropriate income-shifting to captive REITs by denying a dividend paid deduction where the captive REIT is effectively subject to state taxation; and

Whereas, in 2009 the Uniformity Committee subsequently undertook a project to develop a Proposed Model Statute for the Disallowance of Deductions for Payments to Captive REITs that could be adopted in states as an alternative, or in addition, to the 2008 Model Statute as a superior method for addressing inappropriate income shifting for separate entity states and in situations where the captive REITs are not included in a combined report; and

Whereas, the Uniformity Committee on April 13, 2010 voted to recommend to the Executive Committee a proposed Model Statute for the Disallowance of Deductions for Payments to Captive REITs, and the Executive Committee on July 29, 2010 voted to conduct a public hearing on the proposed Model Statute; and

Whereas, a public hearing on the proposed Model Statute for Disallowance of Deductions for Payments to Captive REITs was held on September 14, 2010, and a hearing officer’s report was provided to the Executive Committee on November 23, 2010; and

Whereas, the Executive Committee voted to recommend the Commission approve the proposed Model Statute for the Disallowance of Deductions for Payments to Captive REITs on January 9, 2011; and

Whereas, a Bylaw 7 Survey was sent to the affected compact member States on April 14, 2011, with a majority of States indicating they would consider adoption of the proposed Model Statute for Disallowance of Deduction for Payments to Captive REITs;

Now, therefore, be it:

RESOLVED, that the compact member States adopt the attached Model Statute for the Disallowance of Deductions for Payments to Captive Real Estate Investment Trusts as a uniformity recommendation to the States.

Steve Cordi, Chair

Joe Huddleston, Executive Director
Multistate Tax Commission

Dated: July 27, 2011



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

As approved by the Multistate Tax Commission July 27, 2011

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

(1) 'Real estate investment trust' shall have the meaning ascribed to such term in Section 856 of the Internal Revenue Code, as amended.

(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) 'Association taxable as a corporation', for purposes of applying paragraph

(a)(2)(A) of this [section], shall not include:

(A) A real estate investment trust as defined in this section, other than a "captive real estate investment trust";

(B) 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';

(C) 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

(D) 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.

(4) "Related entity" means a stockholder who is an individual, or a member of the stockholder's family enumerated in Section 318 of the Internal Revenue Code of 1986, as amended, if the stockholder and the members of the stockholder's family own, directly, indirectly, beneficially, or constructively, in the aggregate, at least 50 percent of the value of the taxpayer's outstanding stock; a stockholder, or a stockholder's partnership, limited liability company, estate, trust or corporation, if the stockholder and the stockholder's partnerships, limited liability companies, estates, trusts, and corporations own directly, indirectly, beneficially, or constructively, in the aggregate, at least 50 percent of the value of the taxpayer's outstanding stock; or a corporation, or a party related to the corporation in a manner that would require an attribution of stock from the corporation to the party or from the party to the corporation under the attribution rules of section 318 of the Internal Revenue Code of 1986, as amended, if the taxpayer owns, directly, indirectly, beneficially, or constructively, at least 50 percent of the value of the corporation's outstanding stock. The attribution rules of 26 U.S.C. §318 shall apply for purposes of determining whether the ownership requirements of this subdivision have been met.

(5) "Related member" means a person that, with respect to the taxpayer during all or any portion of the taxable year, is: (A) a related entity, (B) a component member as defined in subsection (b) of section 1563 of the Internal Revenue Code as amended; (C) a

person to or from whom there is attribution of stock ownership in accordance with subsection (e) of section 1563 of the Internal Revenue Code of 1986, as amended; or (D) a person that, notwithstanding its form of organization, bears the same relationship to the taxpayer as a person described in (A) to (C), inclusive.

(b) For purposes of this 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.

(c) For purposes of this section, a real estate investment trust that is intended to be regularly traded on an established securities market shall not be deemed a captive real estate investment trust within the meaning of this section if it becomes regularly traded on an established securities market within one year of the beginning of the tax period for which its election to become a real estate investment trust becomes effective.

(d) 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 that is a related member. Such expenses and costs shall be added back in the calculation of [State] taxable net income before the income is apportioned or allocated as provided by [UDITPA].

(e) The amount of the adjustment required by subsection (d) of this 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 a proportionate amount of the expenses allowed in computing the captive real estate investment trust's federal taxable income that have not been paid, accrued or incurred by the captive real estate investment trust to persons that are related members.

(f) No adjustment shall be required under subsection (d) of this section if:

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

(2) the tax paid by the captive real estate investment trust and its shareholders on the corresponding income, when divided by the expenses and costs minus any adjustment in (e), yields an effective tax rate of not less than ___%.

(g) In claiming the reduction allowed by subsection (e) or the elimination of the add-back requirement in (f), 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.

(h) Nothing in this 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.

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

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

- (1) make adjustments under [cite to state's Section 482 authority, if any];
 - (2) use alternative apportionment rules as allowed by [cite to state codification of UDITPA Section 18 authority, if any]; or
 - (3) enter into agreements and compromises otherwise allowed by law.
- (k) The Commissioner is authorized to prescribe forms and promulgate rules and regulations deemed necessary in order to effectuate this section."