New Normal – the future of the Real Estate industry

WebCast 02. September 2020 10:00 – 11:00 a.m.

More resilience & transparency in the real estate sector

• Financing – Cash inflow to Germany
• Department stores – Potentials of different conversion alternatives
• Update ESG – News on Strategy & Legal
• Update Tax – DAC-6 affects the market!

Registration via LINK: www.pwc-events.com/Real-Estate-WebCast
Updates and Information also on https://blogs.pwc.de/real-estate/
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More resilience & transparency as the order of the day

Social change as trigger!

- **Change in social mindset** has also affected the real estate sector – more **resilience and transparency** is the order of the day in the real estate business
- **Need for adjustment** on the real estate markets – **practicable solutions** are required – **social responsibility** of the sector is high
- **Desire for lively city centers** – Conversion of existing properties as an opportunity
- **Mixed uses in city centers**: investors and the capital market take a **positive view of diversified usage risk**
- **Climate protection and well-being**: **ESG is here to stay!**
- **Tax transparency** and the **desire for minimum taxation**: DAC6 as a legal requirement
Local investment focus of European investors!

Does the trend towards onshoring in supply chains also apply to global capital flows?

Cash flows to Germany

- United States
- Switzerland
- Austria
- Singapore
- Sweden
- United Kingdom
- France
- South Korea
- Luxembourg
- Canada

Beginning of Covid-19

Q1 2018: 1,000
Q2 2018: 2,000
Q3 2018: 3,000
Q4 2018: 4,000
Q1 2019: 5,000
Q2 2019: 6,000
Q3 2019: 7,000
Q4 2019: 8,000
Q1 2020: 9,000
Q2 2020: 10,000

Q3 2018: 1,500
Q2 2019: 2,500
Q3 2019: 3,500
Q4 2019: 4,500
Q1 2020: 5,500
Q2 2020: 6,500

Beginning of Covid-19:

2020: Cash flows dramatically increased due to Covid-19.
Department stores in transition

**Department store concepts no longer up to date!**

- Many department stores have to close – reconstruction concepts with a mix of uses are most successful.
- 46% decline in sales in German department stores in recent years – from €10.4 billion in 2003 to €5.6 billion in 2018.
- 52 Department stores in Germany had to close in the last ten years (large market share).
- 80% of them were structurally modified for subsequent use.
- 56% of the pure retail uses have already had to be closed again.

**LINK:** [www.pwc.de/de/real-estate/pwcs-real-estate-institute/warenhausimmobilien-im-wandel.html](http://www.pwc.de/de/real-estate/pwcs-real-estate-institute/warenhausimmobilien-im-wandel.html)

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Mix-Used concepts as a chance for city centers!

**Key-Results**

- **Mixed-Used concepts** as reuse of former department stores are most successful.

- **Stationary retail trade** (e.g. self-service department stores, grocery stores or branch operations) as a concept for reuse is rarely successful.

- **Structural changes** (connected with not inconsiderable costs) for subsequent use **always necessary** - reason: **unsatisfactory quality** of many department stores.

- **Mixed-use inner city quarters** (retail with residential or office) is the **most sustainable concept**!

- **Great heterogeneity** of real estate - subsequent use concepts must be **adapted to the individual circumstances** of the property.
Real Estate needs a sustainable foundation!

Call for Action!

- **Scarcity of resources** and **volatility** → „Climate change is the greatest danger in the human history.“ (Ban Ki Moon)

- **Climate change** as a topic has become a major part of public discourse and is no longer a **niche topic**

- **Increased and more intensive** occurrence of consequences of climate change – **unforeseeable costs** as a result!

- Market participants position themselves in a **field of tension between regulation** and **strategic impulses**

- **Fund- and asset managers** have already started **extensive projects**!

More information about ESG in Real Estate:

https://www.pwc.de/de/nachhaltigkeit/nachhaltigkeit-in-der-immobilienbranche.html

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ESG is here to stay – Sustainability as central value contribution

Implications for the definition of the ESG strategy

• **Strategic ESG positioning** – new markets and sustainability potential for organizations

• **License to operate** – newly defined risk, transparency and business requirements

• **Stakeholder engagement** – involved customers, investors, employees & the public in ESG issues

• **Operational excellence** – sustainability offers potential for cost reduction and efficiency increase

• **ESG Regulation** – holistic and restrictive regulations and economic stimulus programs
The interlocking of ESG regulations in contracts is essential for sustainable corporate action!

All participants - including service providers, administrators, tenants, investors, financing providers and insurers must be subject to coordinated regulations.

Otherwise there is a risk of violation of contractual and/or legal regulations.

Project development / Revitalization
- Green planning and construction contracts
- Certifications for "Green Building"
- Energy law (e.g. sustainable self-sufficient energy supply, e-mobility concepts)
- Contractual implementation of Cradle to Grave and/or Cradle to Cradle concepts
- Clauses on the collection and use of ESG data
- Green energy and supply contracts
- Agreements with providers of sustainable PropTech solutions

Purchase and sale
- Legal ESG due diligence (checking compliance with ESG standards)
- Consideration of the results of ESG due diligence in property and share purchase agreements as well as in transaction documents (e.g. guarantees, warranties)
- Clauses for the exchange of ESG data

Asset Management
- Green lease/rental agreements
- Agreements on the management of environmentally friendly facilities, real estate and equipment
- Agreements with providers of sustainable PropTech solutions

Financing
- Green Funds
- Green Bonds
- Green financing agreements and securities

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Objectives in the preparation of ESG-compliant contracts

- Rules for the collection and exchange of ESG data in all property-related contracts as a central component of an ESG strategy
- Requirement: Compliance with data protection regulations and protection of business secrets

- Ensuring the adaptation of continuous obligations to changing conditions (market / regulation)
- Opening clauses for implementation and adjustments of ESG strategies

- Changed due diligence and risk management processes with regard to ESG risks (location and/or other risks)
- Tightening of minimum standards for occupational safety, environmental protection, combating corruption, etc.

- Agreement on blind sustainability criteria (including increased user comfort)
- Creation of healthier environmentally friendly living, living and/or working spaces
- Life cycle assessment

Transparency
Flexibility
Risk Management
Qualitätssteigerung
Basics of the design of ESG-compliant contracts

Exchange of ESG data

- **Central regulation** of all property-related contracts during the entire life- and investment cycle (construction and planning, auditing, certification, purchase, management, service provider and rental contracts, community regulations, etc.)

- Data form the **basis of any ESG strategy** (identification and optimization of sustainability standards) and ESG reporting

Personal data

- When exchanging personal data, the General Data Protection Regulation (GDPR) must be observed
- Prior to disclosure, a balancing of interests must be carried out, in the course of which the interests of the persons concerned must also be taken into account.

Business and trade secrets

- These are all facts, circumstances and processes relating to an enterprise which are not obvious and in whose non-disclosure the legal entity has a legitimate interest (Federal Constitutional Court, decision of 14.3.2006)
- There are legal obligations for the corporate representatives of legal entities to take precautionary measures to protect business and trade secrets (e.g. for the AG from § 91 para. 2 AktG (German Stock Corporation Act) and for the GmbH from § 43 para. 2 GmbHG (German Limited Liability Company Act)).

Practical tips

- Include as broad a definition of ESG data as possible
- If necessary, grant a power of attorney to obtain ESG data from third parties
- Exchange in "appropriate form (electronic if available)"
- Right to self-recovery with the support of the other party
- Obligation to anonymize before transfer
ESG aspects should be included in investment considerations at an early stage!

Recommendations to ensure ESG conformity:

1. **Ongoing monitoring** of regulatory developments. Regulatory requirements in the area of ESG will have a **considerable steering effect**.

2. **Review of all contracts** for compliance with ESG criteria and closing of regulatory gaps, formulation of clauses

3. **Lifecycle approach as a business case** – anticipatory inclusion of ESG aspects at every stage of the investment phase
The Directive on Administrative Cooperation does not only concern Germany!

Deep Dives on DAC6 reporting requirements

Why is it necessary to report?
• Increase transparency to uncover potentially aggressive tax structuring!

Where must be reported?
• DE, PL and FIN

Who must report?
• Intermediary and / or user

What must be reported?
• As intermediary
• As user
• Hallmarks

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# DAC 6 – Overview of the labels according to § 138e AO

## § 138e para. 1 AO (German Fiscal Code)

<table>
<thead>
<tr>
<th>A1-A3</th>
<th>B1-B3</th>
<th>C1</th>
</tr>
</thead>
<tbody>
<tr>
<td>General characteristics</td>
<td>specific characteristics</td>
<td>specific characteristics</td>
</tr>
<tr>
<td>Nr. 1 a)</td>
<td>Nr. 3 a)</td>
<td>Nr. 3 d-e)</td>
</tr>
<tr>
<td>A.1</td>
<td>Qualification confidentiality clause</td>
<td></td>
</tr>
<tr>
<td>Nr. 1 b)</td>
<td>Nr. 3 b)</td>
<td></td>
</tr>
<tr>
<td>A.2</td>
<td>Agreement of a success fee with regard to the tax advantage</td>
<td></td>
</tr>
<tr>
<td>Nr. 2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>A.3</td>
<td>Standardized documentation or structure</td>
<td></td>
</tr>
<tr>
<td>Nr. 2</td>
<td>Nr. 3 c)</td>
<td></td>
</tr>
<tr>
<td>B.1</td>
<td>Acquisition of a loss-making company with termination of activity (loss acquisition)</td>
<td></td>
</tr>
<tr>
<td>B.2</td>
<td>Conversion of income into assets, gifts or low taxed types of income</td>
<td></td>
</tr>
<tr>
<td>B.3</td>
<td>Circular transfers of assets</td>
<td></td>
</tr>
</tbody>
</table>

+ additional: MAIN BENEFIT TEST

## § 138e para. 2 AO (German Fiscal Code)

<table>
<thead>
<tr>
<th>C1-C4</th>
<th>D1-D2</th>
<th>E1-E3</th>
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<tbody>
<tr>
<td>specific characteristics</td>
<td>specific characteristics</td>
<td>Transfer pricing</td>
</tr>
<tr>
<td>Nr. 1 a)</td>
<td>Nr. 2</td>
<td>Nr. 4 a)</td>
</tr>
<tr>
<td>C.1</td>
<td>Deductible cross-border payment between affiliated companies if the recipient is not located in a tax jurisdiction or in a non-cooperative tax jurisdiction</td>
<td></td>
</tr>
<tr>
<td>D.1</td>
<td>Elimination of the notification obligation under the common reporting standard</td>
<td></td>
</tr>
<tr>
<td>E.1</td>
<td>Use of a unilateral safe-harbour arrangement</td>
<td></td>
</tr>
<tr>
<td>C.2</td>
<td>Multiple depreciation of the same asset</td>
<td></td>
</tr>
<tr>
<td>D.2</td>
<td>Interposition of legal owners or beneficial owners to conceal the beneficial owner (non-transparent chain)</td>
<td></td>
</tr>
<tr>
<td>E.2</td>
<td>Transfer of intangible assets that are difficult to value to affiliated companies or permanent establishments abroad (hard to value-intangibles)</td>
<td></td>
</tr>
<tr>
<td>C.3</td>
<td>Multiple exemption of the same assets or income from double taxation</td>
<td></td>
</tr>
<tr>
<td>D.3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>E.3</td>
<td>Intercompany cross-border relocation of functions, risks, assets or other benefits if the EBIT forecast of the transferor decreases by more than 50% over 3 years</td>
<td></td>
</tr>
</tbody>
</table>
Your questions to the PwC experts

**Financing**

**Department store study**

**Update ESG - Strategy**

**Update ESG - Legal**

**Update Tax**

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PwC information about the New Normal and its impact on the real estate industry can be found here:

Current information about real estate also in the context of New Normal
https://blogs.pwc.de/real-estate/

Central email address for questions to PwC experts on New Normal
de_covid19_pwc_real_estate@pwc.com

PwC Plus - All information about real assets with push messages function
https://pwcplus.de/

Bi-weekly expert session via WebCast on current topics always Wednesday 10:00 to 11:00
The new normal – the future of the real estate industry

Next session on 16th of September from 10:00 am

Registration via link: www.pwc-events.com/Real-Estate-WebCast