

## **Chapter 6 Selling Real Estate via REA**

### **6.1 Real Estate Association (REA)**

Man is a natural legal entity, and is entitled to legal activities - to buy, to sell, to sign various contracts and perform other associated acts. If one is a juvenile, these activities are performed in his name by his parents, or some other legal guardian. Artificial entities are entitled to carry out these legal activities. These artificial entities are called corporations.

Corporations are companies and partnerships generally established for the purpose of making and handling a profit. Non profit organizations are generally established for the purpose of some activity for public or social benefit, which yield no profit. Trust funds are for the purpose of some pre-planned activity, and special tasks, which serve a specific legal purpose such as administrator general.

In this chapter, I will address the subject of a company that is purchasing land or buildings. This company will be called "Real Estate Association" (hereinafter: "REA"). The REA will not sell real estate or take part in the construction of any building on the land and will not be involved in any economic activity of any kind within the realm or scope of trade.

This REA is established for the purpose of marketing real estate in an unconventional method. This marketing should be performed by means of the sale of REA's "special shares" and their allocation to different buyers, whilst the

ownership of said property remains that of the REA.

The municipal and state authorities administer the registry of ownership of property in the public property records. A notary or attorney at law transacts the trade agreement between the buyer and the seller. Commonly, at the close of the deal, the buyer is registered in the public property records.

There are three purposes and benefits in marketing real estate using the REA's unconventional method: (a) avoiding red tape and law restrictions, (b) anonymity of the real estate owner, and (c) tax shelter.

**A. Avoiding red tape and law restrictions** - The first goal of the REA is to market indirectly the equity of the property that is owned by it thereby, avoiding red tape and law restrictions -

- I No necessity of contracts for the sale of the property;
- II No need to register the buyers in the public property records; and
- III Not being subject to the laws governing purchasing and owning real estate.

The result is that in the first stage the REA purchases the ownership of the property according to property law, and is registered as the owner of the property in the public property records. The following stage is that the REA markets the equity of the property in a completely revolutionary way.

**B. Anonymity of the real estate owner** - The second goal of marketing property equity via the REA is to protect the anonymity of the buyer. When one purchases real estate and is registered as the owner, this becomes public knowledge. When one becomes the owner of shares in the REA, his name is not written in the public property records but only in the company registry. This registry is also open to public scrutiny. REA shareowners that choose to remain anonymous can accomplish this in a way that will be detailed later on in this chapter.

**C. Tax shelter** - The third goal of marketing property via the REA is the saving of tax payments. There are two principal taxes which can be saved: the purchase tax which is imposed on the buyer of property, and the capital gains tax which is imposed upon the seller of the property, taking into consideration the profit that is created by the sale of the property.

## 6.2 The Legal Structure of the Real Estate Association

A limited company has shares, and every share entitles the owner to certain rights. The rights of certain types of shares are determined by regulations that have been set down in the memorandum by the founders of the company. The shares of a limited company grant their shareholders four principal rights -

- a. The right to participate in the voting at council meetings of the company;
- b. The right to appoint the directors of the board of the company;
- c. The right to dividends earned by the company; and
- d. The right to obtain a portion of assets in the liquidation process.

When a limited company has only one type of share, it is generally termed "ordinary shares". Those shares entitle the shareholder to all available rights, including the four principal rights mentioned above. Besides the ordinary shares a limited company may issue "special shares", which represent special rights. These special shares will entitle their shareholder to those rights that are determined in the memorandum.

In the example of the REA illustrated in this chapter, it is a limited company that has two types of shares -

- a. "Ordinary shares" that entitle the shareholder to the four principal rights mentioned above;
- b. "Special shares" that entitle the shareholder to the exclusive rights in a specific asset owned by the REA. Those exclusive rights may entitle the shareholder -
  - I to occupy this asset;
  - II to lease this asset and to receive rental income;
  - III to build on the land or to enhance any construction already on it;
  - IV to obtain the assets in the liquidation process; and
  - V any other legal rights associated with this specific asset.

In this way, if an entrepreneur wishes to purchase real estate, i.e. a building that has 20 residential units and 4 stores, or land for the construction of a building such as this, he should establish an REA, which has 100 ordinary shares and 24 numbered special shares.

Each "special share" entitles its shareholder all the rights of a certain residential

unit or a certain store. These shareholders will not have the right to participate in the general assemblies of the company, appoint directors, receive dividends, or receive any assets of the company in liquidation or receivership, except with regard to said specific asset. The 100 ordinary shares are issued to the entrepreneur while the 24 special shares will be issued or sold to the customers.

### **6.3 Purchasing Real Estate by the REA**

In order to attain the three goals of the REA, the entrepreneur must establish the REA in a certain way and obtain, where necessary, permits from the Treasury of the country in which the asset lies.

In many countries there is no limit to the acquisition of property, whether the buyer is a citizen or resident of that country or a foreign citizen. Nor is there any limitation on the acquisition of property by an association whether the association is registered in that country or a foreign country.<sup>1</sup> In these cases there is no problem to purchase real estate by the REA.

There are certain countries where there are considerable limitations regarding the acquisition of land by foreign residents.<sup>2</sup> In these countries there are also limitations regarding the purchase of land by foreign companies, and upon the establishment of locally registered companies by foreign citizens or foreign corporations and associations. Within the framework of these limitations, it is possible, however, to establish a company with joint ownership between a citizen of that country and a foreign citizen; i.e. a "joint venture", and this type of company is granted a license by the Treasury.

The entrepreneur must establish an REA that has the two types of shares mentioned above. The local citizen will own the ordinary shares while the foreign citizen or corporation will own the special shares. After the license has been granted, there are usually no limitations on the transfer of the special shares to another foreign citizen or foreign corporation.

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<sup>1</sup> This list includes most of Western Europe, North America, Israel, etc.

<sup>2</sup> This list includes the countries of Eastern Europe. Recently, there have been legislative efforts made to ease these limitations, and since 1999 it is legal for foreign citizens to buy residential apartments in Poland.

There may exist legal limitations upon the transfer of shares in the REA between foreign citizens or corporations. The original model should be ratified, and the entrepreneur must establish a domestic REA and a foreign holding company that is an additional REA and owns all the shares of the domestic REA or at least the 24 special shares.

The foreign REA has 24 numbered special shares as well, (hereinafter "mirror shares") each one reflecting all the legal rights and economic equity of a specific special share in the domestic REA. The 24 mirror shares in the foreign REA will be sold to the customer. Each shareholder of a mirror share in the foreign REA has indirect ownership of a special share in the domestic REA, which entitles him an indirect ownership in a specific asset owned by the domestic REA.

For example, a Romanian domestic REA is the registered owner of 20 residential apartments and 4 stores in Oradia. Special share numbered 7 represents an apartment on the third floor of 100m<sup>2</sup> according to its regulations. A REA registered in Spain is the owner of the 24 special shares in the domestic REA including the special share numbered 7. The Spanish REA issues 24 special shares of its own. Special share numbered 7 in the Spanish REA represents according to its regulations the legal rights and the economic equity of special share numbered 7 in the domestic REA. The owner of special share numbered 7 in the Spanish REA obtains the legal rights and the economic equity of special share numbered 7 in the domestic REA, and therefore he obtains the legal rights and the economic equity of the said apartment on the third floor in Oradia.

### **6.3.1 Avoiding Red Tape and Law Restrictions**

In those countries where there is a limitation upon the purchase of land via foreign corporations, frequently a special license is granted to purchase a certain parcel of land or property by means of a foreign corporation.

After the license is granted, the REA is established, and the domestic REA is registered as the owner of the property there aren't any more restrictions in transferring the special share in the foreign REA from one shareholder to another.

### **6.3.2 Anonymity of the Real Estate Owner**

The names of the shareholders of a corporation are registered in the public records of the Corporation Registry. However, there are countries i.e. Switzerland that do not register shareholders in the public records of the Corporation Registry and the shareholder is considered the person who holds the share itself. The attorney at law who represents the shareholder, and who has registered the corporation, has his own private registry and the local laws protect access to this registry. The result is that other than the shareholders, only the local attorney at law has access to the names of the shareholders of that corporation.

The entrepreneur's choice among these alternatives is a function of the local laws where the property lies and the necessary demands of the potential purchasers of the property. The second objective of marketing property by means of the REA is to protect the anonymity of the purchaser. If the entrepreneur is convinced that the potential buyers of property will want to remain anonymous, he must choose to establish a foreign off shore corporation even if there is no limitation upon the purchase of land in a specific country by a foreign citizen or corporation.

### **6.3.3 Tax Shelters in the REA**

The third purpose of establishing an REA is to avoid paying taxes; i.e. purchase tax which is imposed upon a buyer who buys directly and capital gains taxes<sup>3</sup> which are imposed upon the seller of said property, with regard to the resulting profit of the sale.

Foreign corporations are called, "offshore company" and can be registered in countries that specialize in international tax shelters.<sup>4</sup> In these countries there is no income tax imposed upon these corporations and their foreign shareholders. These corporations and their foreign shareholders are exempt from the declaration of income and property, from the obligation to produce financial reports. They are obligated to pay only a yearly fee to the local Company Registry, as well as the retainer fees paid to the law firm who has registered them.

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<sup>3</sup> The Capital Gains Tax is also known as Land Appreciation Tax.

<sup>4</sup> Switzerland, Vaduz, The Antilles Island and many more.

When the entrepreneur purchases the land or the building via the REA, he is obligated to pay a purchase tax or a stamp tax. When the customer buys a special share or a mirror share in the REA, there is no obligation to pay purchase tax, because he did not buy real estate. At the same time, the entrepreneur who sells the special share or a mirror share has no obligation to pay capital gains tax because the REA is registered as an off shore company.

The customer who sells the special share or a mirror share has no obligation to pay capital gains tax or income tax because the REA is registered as an off shore company, nor does he have the legal obligation to declare upon this sale.

#### **6.4 Marketing Methods via the REA**

In this chapter I have presented an untraditional method of buying and selling real estate assets. Instead of performing a direct sale of real estate to the customer, the suggestion is to perform an indirect sale of real estate by performing a direct sell of shares in REA. Instead of registering the buyer in the land public records and the granting of a real estate ownership certificate, there is a confidential registration by the law firm in the off shore company. A share certificate is granted either a special share or mirror share in REA.

The REA method is effective on three levels - in countries where there are restrictions on foreign ownership of real estate, for customers who wish to remain anonymous, and anybody else wishing to enjoy the benefits of tax shelters.

Entrepreneurs who are interested in selling real estate via the REA will find a larger potential group of customers than their competitors who are not aware of these advantages. These target customers may be one of three categories -

- A. Foreign citizens who are not permitted to buy real estate in a certain country,
- B. investors who wish to remain anonymous and not reveal the fact that they own real estate or have the means to buy it, and finally
- C. anybody that does not like to share his profit with the Treasury.

An entrepreneur who is marketing real estate via the REA should approach target customers in foreign countries offering property, which is restricted by the local law to foreigners. The entrepreneur may approach target customers who probably

prefer to remain anonymous and not reveal the nature of their finances and the existence of their assets. Finally, the entrepreneur should approach the general public and offer a tax shelter in the form of real estate.

The ultimate customer is a wealthy foreigner, and he should be the main target of the marketing efforts.