



One Firm Worldwide

# **REITs, SIICs, PIFs and other Interesting Acronyms The Globalization of the REIT Industry**

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Thursday, 28th April 2005



# REITs Worldwide

## The Story So Far

- Publicly traded real estate companies can be found in about 20 countries.
- U.S. and Australia are the most significant:
  - U.S. REITs now have an aggregate investment of more than U.S. \$300 bn with the bulk of the growth occurring since 1989 (at that time aggregate market cap was less than U.S. \$25 bn).
  - In the same period REITs in Australia have increased market cap by 500%.
- REITs have outperformed traditional equities significantly in all markets where they exist.
- In the last 10 years France, Japan, Singapore, South Korea, Belgium and the Netherlands have introduced REITs.
- Consultation on REIT legislation is taking place in Germany, Italy, U.K. and others.

# Why the Move to REITs?

- Improve efficiency and liquidity of property investment markets.
- Improve access to real estate as an asset class for long term savings.
- Allow small investors to pool investments and achieve diversification.
- Reduce discount between share price and net asset value of listed companies.

# Issues in Emerging REIT Regimes

- Listed or Private
- Closed-ended or Open-ended
- Investor Base
- Internal or External Management
- Distribution Requirements
- Borrowing Levels
- Permitted Activities
- Conversion (“Exit” or “Entry” Tax)
- Holding Period

# US: Real Estate Investment Trusts (REITs)

- Since 1960; Public and Private.
- 100 shareholder minimum; closely held rules apply.
- No leverage limitations.
- 90% of REIT taxable income must be distributed.
- 75% of income must be derived from rents from real property or interest on debt secured by real property.
- Taxable REIT Subsidiaries (TRS).

# Australia: Property Trusts

- Since 1985; Public and Private Unit Trusts.
- Public Trading Trusts (more than 50 investors) are limited to passive investment activities.
- No leverage limitations.
- 100% of trust's income must be distributed.

# France: Société d'Investissement Immobiliers Cotés (SIIC)

- Approved and entered into force in 2003, amended on December 31, 2004.
- Must be a company listed on the Paris stock exchange which is otherwise subject to French corporate income tax.
- Main activity must be acquisition or erection of buildings for lease. Ancillary activities (real estate development, management, etc.) are allowed but limited.
- Leverage is not limited.
- 85% of Profits and 50% of Capital Gains must be distributed.

# Netherlands: Fiscale Beleggingsinstelling (BI)

- Since 1969.
- Pure tax regime; election made yearly; applies to NVs, BVs and mutual funds.
- Not required to be listed but closely held rules apply.
- Restricted to passive investment; excludes management and development activities.
- Leverage limited to 60% of book value.

# Japan: J-REITs

- Since 2000; 15 in existence; market value > U.S. \$11 bn.
- Modeled on U.S. REIT law.
- 75% of assets must be invested in Real Estate.
- Number of investors must exceed 1,000 to be listed.
- Company may manage assets.
- No limitation on leverage.
- 90% of distributable income must be distributed.

# UK: Property Investment Funds (PIFs) Case Study of a REIT in Development

- Treasury consultation document issued March 2004.
- Responses submitted July 2004.
- No mention in Pre-Budget report in December 2004
- Implementation at the time of passing Finance Act 2006 at the earliest.
- Very little is set in stone/all aspects of the PIF are being consulted on.
- Drawing on international experience : U.S., France, Australia, Netherlands and Japan.

# Property Investment Funds Questions for Consultation

## Should PIFs be listed?

- No such requirement in the U.S. although 100 Shareholder minimum requirement
- France: SIIC must be listed
- Australia: Not required, but typically are listed
- Netherlands: Not required, but closely held rules apply

# Property Investment Funds Questions for Consultation

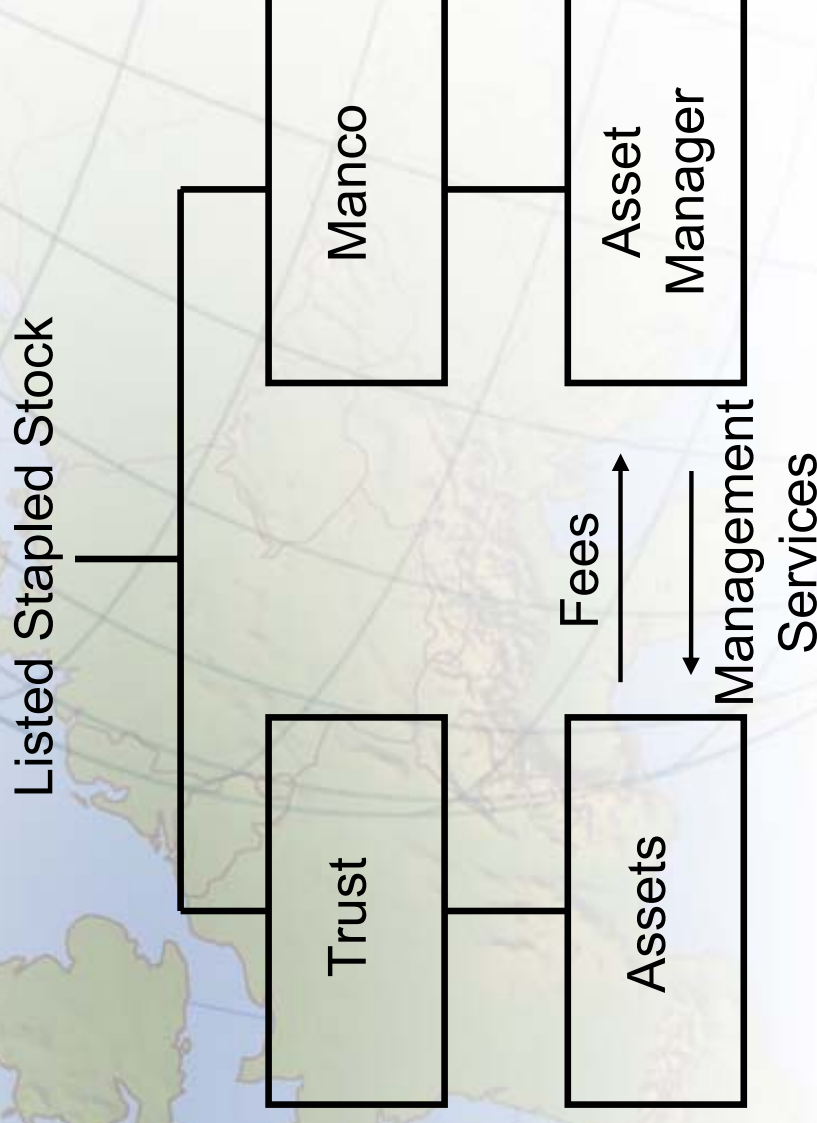
## Should there be a maximum leverage level?

- The two most significant REIT markets (U.S. and Australia) have no borrowing restrictions
- France and Japan have no restrictions
- In other markets leverage limits are conservative (e.g., Netherlands 60% of book value)
- REIT fundraising : the French and American experience
- Weighted average of REIT borrowing (38%) is in line with UK sector average borrowing (41%)

# Property Investment Funds Questions for Consultation

## Internal -v- External Management

- U.S. management is largely internal
- Stapled Structures (Australia)



# Property Investment Funds Questions for Consultation

## Distribution Requirements

- All REIT legislation requires high distribution of income consistent with the philosophy of REITs (90% in the U.S., 100% in Australia and 85% in France)
- Distribution of gains is not necessarily required
- U.S. requires full distribution of gains but property exchanges make this less relevant

# Property Investment Funds Questions for Consultation

## Property Development

- While development may be permitted it is generally penalized and restricted
- Both U.S. and France restrict development (U.S. 20% and France 20%)
- No fixed holding periods for assets
- Refurbishment/renovation -v- trading

# Property Investment Funds Questions for Consultation

## Conversion Charge

- Conversion charge is a near certainty
- The French model : reduced and deferred charge
- Adapting U.S. techniques to avoid a conversion charge
- Borrowing to pay the tax

# Property Investment Funds Questions for Consultation Avoiding Conversion Charges The U.S. UPREIT model

