

CONSULTATION PAPER

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# Review of the Regulatory Regime Governing REITs

MAS

Monetary Authority of Singapore

## PREFACE

A real estate investment trust (“REIT”) established as a unit trust is regulated as a collective investment scheme (“CIS”) under the Securities and Futures Act (“SFA”). As with unit trusts investing in equity or debt securities, REITs structured as unit trusts are subject to parameters on permissible investments, borrowing limits and annual reporting requirements. The relevant rules are set out in the Property Fund Guidelines (“Fund Guidelines”) under the Code on Collective Investment Schemes (“Code”). The Fund Guidelines, introduced in May 1999, represented the culmination of extensive efforts of researching international best practices and consulting the industry to support the introduction of REITs<sup>1</sup> in Singapore.

2 Today, there are five REITs listed on the Singapore Exchange - all of which are structured as unit trusts. In the current low interest rate environment, investors have rapidly embraced this new asset class due to their relatively higher yields. Fuelled by the positive market sentiment towards existing REITs and tax incentives available, many entities have openly expressed interest in transferring their properties into REITs.

3 Although REITs structured as unit trusts need to comply with rules on permissible investments, borrowing limits and annual reporting requirements, they are regulated with a relatively light touch when compared with unit trusts investing in securities or other financial instruments regulated under the CIS regime (collectively known as “securities CIS”), or REITs in other jurisdictions.

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<sup>1</sup> In July 1998, MAS accepted the recommendation of the then Stock Exchange of Singapore Review Committee to support the introduction of REITs in Singapore.

## Differences between REITs and Securities CIS

4 Despite being regulated under the same CIS regime, there are several inherent differences between REITs and securities CIS. The risks arising from the differences are set out below:

- (a) **Structural differences:** Securities CIS are open-ended investment vehicles; the manager is required to stand ready to sell or redeem units of the CIS at net asset value (“NAV”). On the other hand, REITs are close-ended investment vehicles and investors have to exit their investments on the exchange. Market sentiment and confidence will play a part in determining the price at which investors can acquire or exit their investments, which may result in REITs not trading near their NAV.
- (b) **Liquidity of underlying assets:** The timeframe needed to dispose of real estate is much longer and the actual sale price could be much lower than the book value and/or valuation of the properties in the event of liquidation. Unlike securities CIS, REITs may not be able to liquidate their holdings readily at NAV or values close to NAV.
- (c) **Valuation of underlying assets:** Unlike securities CIS where market quotations of the underlying financial instruments are readily available, the valuation of real estate held by REITs is more subjective in nature.
- (d) **Related party transactions:** REITs are usually sponsored by property holding/development companies, i.e. they are formed with properties acquired from these related parties. After their formation and listing, most REITs continue to transact with related parties.

5 With experience gained from administering the Fund Guidelines, MAS is of the view that the existing regulatory framework can be enhanced to help maintain investors’ confidence and to achieve long-term sustainable growth in the nascent but fast growing REIT industry.

6 Taking into account market developments as well as regulatory developments in other jurisdictions, MAS has undertaken a review of the REIT regulatory framework and had preliminary discussions with REIT managers, REIT trustees and institutional investors. The proposals to enhance the current Fund Guidelines will:

- (a) strengthen oversight of REIT managers;
- (b) improve corporate governance practices; and
- (c) better align the interests of REIT managers and unitholders.

7 MAS will continue to monitor international developments and best practices to enhance the regime for the REITs industry in order to promote and sustain its growth.

#### **Request for Comments**

8 MAS invites interested parties to give their views and comments on the proposals set out in this consultation paper. Comments may be submitted to:

Corporate Finance Division  
Securities and Futures Supervision Department  
Monetary Authority of Singapore  
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MAS Building  
Singapore 079117

Email: [reits@mas.gov.sg](mailto:reits@mas.gov.sg)

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MAS would request that all comments and feedback be submitted by 11 July 2005.

9 Please note that all submissions received may be made public unless confidentiality is specifically requested for whole or part of the submission.

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## **SECTION 1: INTRODUCING A REGULATORY FRAMEWORK FOR REIT MANAGERS**

### **A Introduction**

1.1 Like managers of securities CIS, REIT managers engage in active discretionary management of monies sourced from the retail public. Hence, a parallel can be drawn between the management of a REIT and the conduct of fund management. However, unlike managers of securities CIS, REIT managers are not licensed or regulated under the SFA. This practice differs from that in other countries.

### **B SFA Licensing Regime**

1.2 The licensing regime under the SFA imposes several key requirements on the admission and conduct of licence holders and that of individuals who are employed by or act for the company to carry out the regulated activity. This includes requiring the licence holder to adhere to requirements on maintenance of records, safeguarding of customer assets and audit certification under Part V of the SFA, and business conduct requirements under Part VI of the SFA.

1.3 MAS is of the view that a REIT manager should be expected to meet and maintain high standards of business conduct, professionalism and competence. MAS proposes to include the management of a portfolio of real estate properties as a regulated activity under the SFA. Our intention is to exercise greater regulatory oversight over managers of Singapore constituted REITs that are offered to retail investors.

1.4 The proposed supervisory framework for REIT managers comprise the following:

- (a) licensing of the corporate principal and its representatives;
- (b) approval of persons to be appointed as a chief executive officer or director;
- (c) requirements on financial resources, adjusted net capital and lodgement of documents under the Securities and Futures

- (Financial and Margin Requirements for Holders of Capital Markets Services Licences) Regulations; and
- (d) requirements under the Securities and Futures (Licensing and Conduct of Business) Regulations including requirements on conduct of business and safeguarding of customer's moneys and assets.

### **C Admission criteria for REIT managers and their representatives**

1.5 MAS proposes to subject REIT managers to an admission criteria similar to that for securities CIS managers:

- (a) be a corporation that has a physical office in Singapore;
- (b) have a chief executive officer and directors who meet MAS' fit and proper criteria, and are based in Singapore;
- (c) employ at least two full time representatives;
- (d) satisfy the base capital requirement of S\$1 million;
- (e) possess the relevant competence and expertise to carry out the activity of managing a portfolio of real estate properties and securities;
- (f) take up adequate professional indemnity insurance; and
- (g) put in place key internal control procedures to satisfy MAS that the REIT manager will be able to comply on an on-going basis with the requirements of the SFA, and has the adequate means of supervising its employees and representatives.

1.6 The minimum entry requirements for individuals applying for a representative's licence to act on behalf of a REIT manager will be similar to the requirements for representatives who conduct other types of regulated activities under the SFA. Representatives should satisfy the following conditions:

- (a) be at least 21 years old;
- (b) meet the fit and proper criterion, including possessing the relevant experience in managing a portfolio of properties;
- (c) have minimum academic qualifications of 4 'O' Levels; and
- (d) comply with relevant examination requirements to be determined by MAS.

1.7 To ensure that licence holders adhere to the requirements under the framework, MAS will also be provided with powers to inspect and mete out disciplinary action to errant REIT managers.

1.8 In order to institute the proposal to license REIT managers, MAS expects to amend the Second Schedule of the SFA to include the management of a portfolio of real estate properties as a regulated activity. MAS will also make the necessary amendments to the subsidiary legislation under the SFA to set out the appropriate business conduct requirements for REIT managers.

Q1: MAS seeks your views on the proposal to require REIT managers and representatives to be licensed and regulated under the SFA licensing regime and require compliance with the key criteria set out in paragraphs 1.4 – 1.6. If you do not agree with any of the criteria, please suggest alternatives.

In addition, MAS seeks your views on whether there are any other criteria not listed in paragraphs 1.4 - 1.6 that a MAS licensed REIT manager or representative should satisfy.

## D REITs holding Foreign Properties

1.9 The set-up of a typical REIT manager is presented in Figure 1.

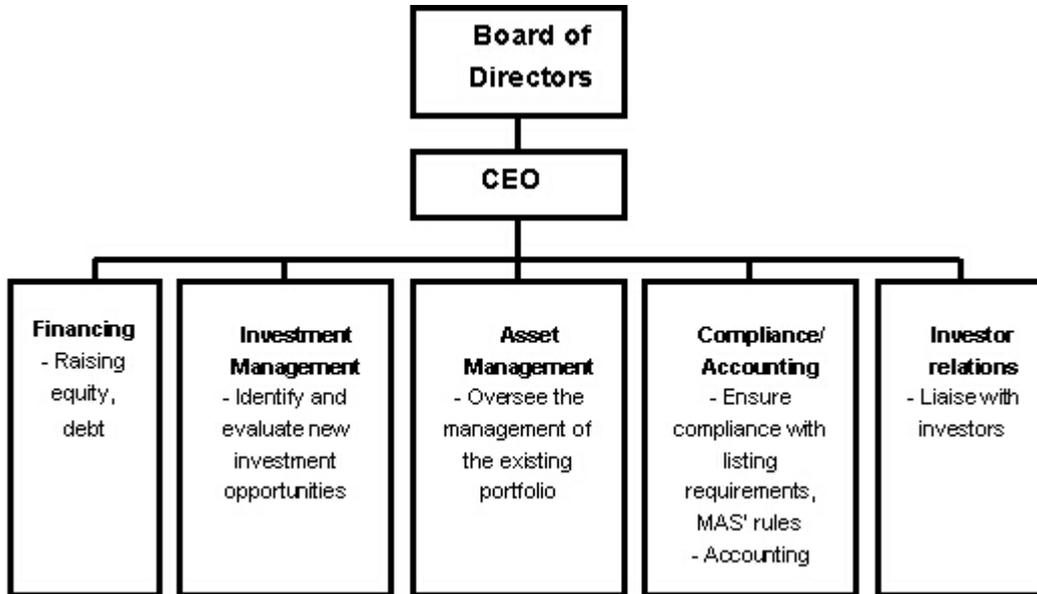


Figure 1: Set-up of typical REIT manager

1.10 For REITs holding a portfolio of entirely local properties, the entire operations of the REIT manager is performed in Singapore. There may be practical difficulties for a REIT manager of foreign properties to do the same. This is because for proximity reasons, the investment and asset management functions may be best undertaken where the properties are located.

1.11 In order for MAS to exercise effective oversight of the activities of REIT managers licensed by MAS, such managers, would be required to, at least perform the following activities in Singapore:

- (a) investment strategy formulation;
- (b) investor relations including procedures to handle queries and complaints;
- (c) compliance/accounting; and
- (d) financing (raising of debt and equity).

Q2: MAS seeks your views on whether a REIT manager licensed by MAS should be required to perform any other specific activities in Singapore not listed in paragraph 1.11.

MAS also seeks your views on whether the requirement to have the activities stated in paragraph 1.11 performed in Singapore would cause any operational difficulties for a REIT manager licensed by MAS and how this could be addressed.

1.12 As for managers of foreign domiciled REITs that wish to offer the REIT through a listing on the Singapore Exchange, MAS would assess whether the foreign manager is licensed and regulated in its home jurisdiction such that it provides investors comparable protection to that afforded if the REIT were to be offered by a Singapore-licensed manager.

## **SECTION 2: IMPROVING CORPORATE GOVERNANCE PRACTICES**

### **A Introduction**

2.1 For good corporate governance, there should be incentives for the board and management to pursue objectives that are in the interests of the REIT and unitholders. There should also be channels where management and stakeholders can communicate readily and effectively. In this regard, MAS has explored various avenues to improve the corporate governance practices of REITs. Specifically, MAS has considered whether to:

- (a) require REITs to hold annual general meetings (“AGMs”); and
- (b) set rules on the removal of REITs manager.

### **B Unitholders’ meetings**

2.2 Like securities CIS, REITs are not required to hold AGMs. AGMs can serve to enhance the accountability of managers by providing a platform for investors to query the manager’s decisions. However, MAS is mindful that requiring REITs to hold AGMs would impose additional costs that may not serve their intended purpose especially if the AGMs are poorly attended. It is noted that the existing REITs have provided in their trust deeds that a meeting may be convened at the request of least 50 unitholders or unitholders representing 10% of units (whichever is lesser). This is a good practice as the provision provides an avenue for unitholders to call for an AGM as and when necessary, when there is sufficient interest to do so. As it is uncertain if the resulting benefits arising from investor empowerment through the holding of AGMs outweigh the costs, we do not propose requiring REITs to hold AGMs. However, we propose to formalise in the Fund Guidelines the current market practice that a meeting may be convened at the request of at least 50 unitholders or unitholders representing 10% of units (whichever is lesser).

Q3: MAS seeks your views on the proposal to formalise in the Fund Guidelines that a meeting may be convened at the request of at least 50 unitholders or unitholders representing 10% of units (whichever is lesser).

MAS also seeks your views on whether REITs should be required to hold AGMs.

## **C Removal of REIT manager**

2.3 The rules on removal of REIT managers in foreign jurisdictions differ. In Hong Kong, the removal of the REIT manager requires a consensus representing 75% of the REIT's units. The votes of the manager, its related parties and any unitholder who may have an interest in retaining the manager are disenfranchised for this purpose. In Australia, a consensus from more than 50% of those present and voting is needed to remove a manager/trustee while the manager and its related parties who hold units may vote.

2.4 This aspect of corporate governance has not been prescribed in the Fund Guidelines. As a result, some of our existing REITs have provided in their trust deeds that the manager may only be removed if a resolution is passed by unitholders holding 75% or more of the units in the REIT. Since units held by the manager and/or its related parties are not disenfranchised, the manager and related parties need to hold only more than 25% of the REIT's units for the manager to be entrenched even if all the other unitholders are dissatisfied with the manager's performance.

2.5 In view of the above, MAS proposes to prescribe either one of the following:

- (a) The REIT manager may be removed by 50% of unitholders who are present and voting with no unitholder being disenfranchised; or
- (b) The REIT manager may be removed by a consensus representing 75% of the outstanding REIT's units, with units held by the manager and related parties being disenfranchised.

Q4: MAS seeks your views on the option to prescribe with respect to the removal of REIT managers:

- (a) 50% of unitholders who are present and voting with no unitholder being disenfranchised; or
- (b) a consensus representing 75% of the outstanding REIT's units, with units held by the manager and related parties being disenfranchised.

## **SECTION 3: ALIGNING INTERESTS OF REIT MANAGERS AND UNITHOLDERS AND ENHANCING THE ROLE OF TRUSTEES**

### **A Introduction**

3.1 The following market practices have been observed:

- (a) payment of acquisition and disposal fees to REIT managers for the purchase and sale of properties;
- (b) transactions by REITs with related parties of their managers; and
- (c) transaction by a REIT with a related party of the trustee.

Against this backdrop, MAS proposes specific enhancements to improve the alignment of interests of stakeholders of a REIT. We also propose to bolster the current rules on the duties and obligations of a REIT trustee.

### **B Payment of property acquisition/disposal fees to REIT manager**

3.2 In the offering documents and trust deeds of existing REITs, there is a provision that managers would receive a percentage-based fee upon the REIT's acquisition or disposal of properties ("Transaction Fee").

3.3 Like managers of securities CIS, REIT managers earn a recurring base management fee based on the value of the scheme's property. Since REITs also levy a performance fee<sup>2</sup>, Transaction Fees represent a third source of fee income for REIT managers.

3.4 As the presence of such Transaction Fees could provide an incentive for managers to embark on the buying or selling of properties that may not be in the best interests of unitholders, it may not be wholly consistent with the fiduciary obligations of the REIT manager.

3.5 On the other hand, MAS acknowledges that placing a curb on the Transaction Fee may lead to REIT managers losing the incentive to actively

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<sup>2</sup> The performance fee payable to the REIT manager is typically set as a percentage of the REIT's income.

source for yield accretive properties or dispose of properties that are a drag on the REIT's yield. Another possible outcome of a curb is that the REIT manager may instead engage a third party broker to perform a similar function and pay him a similar fee.

3.6 On balance, MAS considers that clear and prominent disclosure of such Transaction Fees would enable investors to make an informed investment decision whenever a property is acquired or disposed of. In this connection, MAS proposes that the REIT manager discloses, in dollar quantum, the following during an acquisition:

- (a) acquisition fee payable to the REIT manager; and
- (b) if a profit forecast is made,
  - (i) the expected incremental income to the REIT; and
  - (ii) the expected incremental base and performance fee payable to the REIT manager.

The above fees, together with all other requisite fee disclosures, are to be disclosed prominently in tabular form in the offering document or circular.

3.7 As for disposal of properties, the REIT manager should disclose the percentage-based disposal fee, in actual dollar quantum, payable to the REIT manager and substantiate why the disposal would be in the interests of unitholders.

3.8 In addition, to better align the interests of REIT managers with unitholders, MAS is considering whether to require the payment of the percentage-based acquisition and disposal fee to the REIT manager to be made in the form of units in the REIT instead of cash. This is to ensure that the manager has a continued interest in the performance of the REIT after the transaction has taken place. The units will be priced at the date of the transaction (at higher of market price or NAV per unit) and subject to a one-year moratorium on sale from the date of the transaction to prevent the manager from disposing of the units in the market immediately.

Q5: MAS seeks your views on the proposal to require the REIT manager to disclose, in dollar quantum, the following during an acquisition:

- (a) acquisition fee payable to the REIT manager; and
- (b) if a profit forecast is made,

- (i) the expected incremental income to the REIT; and
- (ii) the expected incremental base and performance fee payable to the REIT manager.

It is proposed that these fees be disclosed prominently in tabular form in the offering document or circular.

MAS seeks your views on whether other matters should be disclosed and what would be the most effective form for this disclosure.

As for disposals of properties, MAS seeks your views on whether the REIT manager should disclose the disposal fee, in actual dollar quantum, payable to the REIT manager and substantiate why the disposal would be in the interests of unitholders.

In addition, MAS seeks your views on whether the payment of the acquisition and disposal fee to the REIT manager should be made in the form of units priced at the date of the transaction (at higher of market price or NAV per unit) and if you agree that a moratorium period of one year should be imposed on such units. If you do not agree, please suggest what other measures may be introduced to ensure that the interests of the manager and unitholders are properly aligned when percentage-based Transaction Fees are paid.

## **C Augmenting guidelines on interested party transactions**

3.9 The Fund Guidelines prescribed rules with respect to the acquisition and sale of properties from/to interested parties. The current rules broadly cover the following aspects:

- (a) requiring independent valuations;
- (b) setting a cap and a floor on the price for the purchase and disposal of properties to “interested parties”; and
- (c) stipulating thresholds that trigger the requirement to announce transactions or obtain unitholders’ approval<sup>3</sup>.

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<sup>3</sup> A REIT that acquires assets from or sells assets to interested parties is required to:  
(a) where the transaction is equal to or greater than 3% of NAV, announce the transaction immediately; or  
(b) where the transaction is equal to or greater than 5% of NAV, obtain a majority vote at a unitholder’s meeting and announce the transaction immediately.

3.10 All the existing REITs are sponsored by property development/holding companies. Since listing, most REITs have acquired additional properties from their sponsors in interested party transactions. The trend of REITs acquiring properties from interested parties is expected to continue. Whilst a REIT manager is required to conduct related party transactions at arm's length, conflicts of interests are inherent in such transactions. These conflict of interest concerns are compounded by the fact that the valuation of properties, unlike securities, is more subjective in nature.

3.11 In this regard, MAS proposes to augment the Fund Guidelines by requiring:

- (a) the REIT to obtain two independent valuations of the properties for related party transactions, with one of the valuers commissioned independently by the trustee;
- (b) in the case of an acquisition, the transaction price should not be above the higher of the two independent valuations;
- (c) in the case of a disposal, the transaction price should not be below the lower of the two independent valuations; and
- (d) the trustee to provide written confirmation that it is of the view that the transaction is at arm's length and the terms are in the interests of unitholders where:
  - (i) unitholders' approval for the transaction is not required;
  - (ii) in the case of an acquisition, the final transaction price is not at the lower of the two valuations; or
  - (iii) in the case of a disposal, the final transaction price is not at the higher of the two valuations.

Q6: MAS seeks your views on the proposal to augment the Fund Guidelines on interested party transactions by requiring the following:

- (a) the REIT to obtain two independent valuations of the properties, with one of the valuers commissioned independently by the trustee;
- (b) in the case of an acquisition, the transaction price cannot be above the higher of the two independent valuations;
- (c) in the case of a disposal, the transaction price cannot be below the lower of the two independent valuations; and
- (d) the trustee to provide written confirmation that it is of the view that

the transaction is at arm's length and the terms are in the interests of unitholders where:

- (i) unitholders' approval for the transaction is not required;
- (ii) in the case of an acquisition, the final transaction price is not at the lower of the two valuations; or
- (iii) in the case of a disposal, the final transaction price is not at the higher of the two valuations.

If you do not agree to the above proposals, please suggest other measures that may be introduced to protect the interests of unitholders in interested party transactions.

#### **D Extending ambit of interested party to trustees of REITs**

3.12 The Fund Guidelines consider interested parties of the REIT to include its sponsor, manager, adviser and their non-independent directors as well as any controlling (15% or more) unitholder. The holding company, subsidiaries and associated companies of the sponsor, manager or adviser are also deemed to be interested parties.

3.13 Although the trustee of the REIT will typically not be involved in property transactions, a REIT was observed to have acquired a building from the holding company of the REIT's trustee. MAS has concerns that the trustee would not be able to act independently if it was called upon to rule on any issue in such instances. Hence, MAS proposes to extend our ambit of interested parties to include the trustee of REITs.

Q7: MAS seeks your views on the proposal to extend the ambit of interested parties to include the trustee of REITs.

#### **E Enhancing the Role of the REIT Trustee**

3.14 CIS structured as a unit trust are required to have a trustee that is independent of the manager. The trustee is required, as matter of law, to exercise due diligence and vigilance to safeguard the interests of unitholders. The trustee also needs to ensure that the CIS is managed in accordance with the provisions laid out in the trust deed to minimize the risk of mismanagement by the manager.

3.15 The Securities and Futures (Offers of Investments) Regulations set out the duties that a CIS trustee must fulfill. Some of the key obligations are:

- (a) The trustee must exercise due diligence in safeguarding interests of unit holders;
- (b) The trustee must take custody of assets and ensure that assets are properly accounted for;
- (c) The trustee must ensure that the property of the scheme is kept distinct from its own property and the property of its other clients; and
- (d) The trustee must send or cause to send accounts and reports of the CIS to unitholders.

3.16 Ownership of properties is different from ownership of securities. Recognizing this difference, MAS recommends placing additional obligations on a REIT trustee to ensure that it performs the necessary due diligence when the REIT is initially set up and on an on-going basis. The proposed guidelines require the trustee to ensure that:

- (a) a REIT has proper legal title to its properties;
- (b) the properties have a good marketable title<sup>4</sup>;
- (c) the contracts (such as rental agreements) entered into on behalf of the REIT by the REIT manager is legal, valid and binding and enforceable by or on behalf of the REIT in accordance with its terms; and
- (d) the REIT manager arranges adequate property insurance and public insurance coverage in relation to the REIT's properties.

3.17 Other than the obligations proposed in paragraph 3.16, a REIT trustee should exercise all necessary due diligence to protect the rights and interests of unitholders.

Q8: MAS seeks your views on whether a REIT trustee should be required to perform additional obligations as follows:

- (a) a REIT has proper legal title to the properties it owns;
- (b) the properties have a good marketable title;

<sup>4</sup> A good marketable title is a title free and clear of objectionable liens or other title defects. It also enables its owner to sell the property freely to others and allows others to accept without objection.

- (c) the contracts (such as rental agreements) entered into on behalf of the REIT by the REIT manager is legal, valid and binding and enforceable by or on behalf of the REIT in accordance with its terms; and
- (d) the REIT manager arranges adequate property insurance and public insurance coverage in relation to the REIT's properties.

MAS seeks your views on whether the REIT trustee should be required to perform any other specific duties.

## **SECTION 4: INTRODUCING SAFEGUARDS TO ADDRESS CONCERNS OVER PARTIAL OWNERSHIP OF PROPERTIES**

4.1 As our REIT market develops further, it will be increasingly common for REITs to invest in overseas properties in the future.

4.2 REITs investing in overseas properties may not be able to or may not wish to own fully the properties in its portfolio. This is because the laws and regulations in some jurisdictions disallow 100% foreign ownership of real estate. It may also be commercially more expedient and less risky for a REIT to enter into a joint venture in an overseas jurisdiction with local partners who are more familiar with the local business environment.

4.3 A REIT consisting of partially owned properties may not have control over the management of the properties, changes in dividend distribution policies, and the decision to dispose of the properties. The possibility that its joint venture partners may unilaterally make such key decisions may negatively impact the REIT and its unitholders.

4.4 In order to protect the interests of the REIT and its unitholders, we propose to establish five general guidelines for REITs that invest in properties as a part owner. First, in order to facilitate the entry and exit of its investment, a REIT should make its investment through a single purpose property holding company ("SPC"), which holds or is formed to hold the property. Second, the REIT should have freedom to dispose of its investment in the SPC. Third, the REIT should have veto powers over certain key operational issues of the SPC:

- (a) amendment of the memorandum and articles of association or other constitutive document of the SPC;
- (b) cessation or change of the business of the SPC;
- (c) winding up or dissolution of the SPC;
- (d) changes to the capital structure of the SPC;

- (e) changes to the dividend distribution policy of the SPC;
- (f) issue of securities by the SPC;
- (g) incurring of borrowings by the SPC;
- (h) creation of security over the assets of the SPC;
- (i) transfer or disposal of the assets of the SPC;
- (j) approval of the annual budget of the SPC;
- (k) approval of asset enhancement and capital expenditure plans for the assets of the SPC;
- (l) entry into related party transactions; and
- (m) appointment of external advisers such as auditors and lawyers.

Such veto rights should be encapsulated in the joint venture agreement, memorandum and articles of association or other constitutive document of the SPC.

4.5 Fourth, a REIT should agree upfront with its joint venture partners on the minimum percentage of distributable profits of the SPC that will be paid to its shareholders, and the REIT should be able to receive its pro rata share of such dividends.

4.6 Fifth, the REIT should have the right to sell its shares to the joint venture partners at a price arrived at using a predetermined basis, and should have the first right of refusal if its joint venture partners wish to dispose of their stake in the SPC. These rights should be encapsulated in the joint venture agreement, memorandum and articles of association or other constitutive document of the SPC.

Q9: MAS seeks your views on allowing less than 100 per cent ownership of properties and whether the proposed guidelines for part-ownership of properties is sufficient to enable effective control of any properties held by the REIT.

When a REIT intends to invest in a property as a part-owner, it should:

- (a) make its investment by acquiring shares in a SPC;
- (b) have freedom to dispose of its investment;
- (c) have veto powers over certain key operational issues of the SPC;
- (d) agree upfront with its joint venture partners on the minimum percentage of the distributable profits of the SPC that will be paid to

- its shareholders, and the REIT should be able to receive its pro rata share of such dividends; and
- (e) have the right to sell its shares to joint venture partners at a price arrived at using a predetermined basis, and should have the first right of refusal if its joint venture partners wish to dispose of their stake in the SPC. These rights should be encapsulated in the joint venture agreement, memorandum and articles of association or other constitutive document of the SPC.

MAS seeks your views on whether the above criteria are appropriate for partial ownership of properties. If you do not agree with the above criteria, please suggest alternatives that will address the risks of partial ownership of properties.

## **SECTION 5: ENHANCING DISCLOSURE ON TENANT PROFILE**

5.1 The tenant profile of a REIT provides important information on the diversification and stability of operations. Major tenant concentrations, their respective credit quality, and exposure of a REIT to scheduled lease rollovers provide indications of the REIT's exposure to potentially volatile portfolio cash flows. Such material information should be disclosed to current and potential investors and updated periodically. In this regard, MAS proposes enhanced disclosure requirements on the tenant profile of REITs.

5.2 To better empower investors in making informed decisions, the offering documents and annual reports of a REIT should disclose, on a portfolio basis, the:

- (a) total number of tenants;
- (b) top ten tenants, and the percentage of total net rentable area and gross rental income attributable to each of these top ten tenants;
- (c) trade sector mix of tenants, in terms of the percentage of total net rentable area and gross rental income attributable to major trade sectors (for example, a REIT investing in retail malls would have tenants in trade sectors such as food & beverages, electronics goods and fashion).
- (d) lease maturity profile, in terms of the percentage of total net rentable area and gross rental income, for each of the next five years.

Any expected significant changes to the above should also be disclosed.

Q10: MAS seeks your views on the proposal to require the following disclosures in offering documents and annual reports of REITs:

- (a) total number of tenants;
- (b) top ten tenants, and the percentage of total net rentable area and gross rental income attributable to each of these top ten tenants;
- (c) trade sector mix of tenants, in terms of the percentage of total net rentable area and gross rental income attributable to major trade sectors.

(d) lease maturity profile, in terms of the percentage of total net rentable area and gross rental income for each of the next five years.

MAS welcomes suggestions on other disclosures in relation to tenant profile that may be useful to investors.

## **SECTION 6: AMENDING PROVISIONS ON INVESTMENTS IN PROPERTY DEVELOPMENTS**

6.1 The Fund Guidelines currently provide that a REIT should not engage in property development activities and that investments in uncompleted property developments should not exceed 20% of a REIT's deposited property. These guidelines are intended to limit the REIT's exposure to risks and uncertainties associated with property development activities and to ensure that investments of a REIT are substantially income producing.

6.2 Engaging in property development activities (which is prohibited) and investing in an uncompleted property development (which is currently allowed subject a cap of 20% of a REIT's deposited property) entail similar risks. Both activities involve the anticipation of future demand, and assumptions of market conditions may shift within the time taken to develop a property.

6.3 In addition, it may not be fair to prohibit REITs from engaging in property development activities when they are allowed to invest in uncompleted property developments developed by third parties.

6.4 MAS proposes to rationalise the position such that a REIT is allowed to engage in the development of a property that it intends to hold in its own portfolio when completed, subject to the condition that not more than 10% of the REIT's assets are tied up in property development activities or investments in uncompleted property developments. This will provide increased investment discretion for REITs. The 10% restriction will help to ensure that a REIT's exposure to non-income producing assets is limited.

Q11: MAS seeks your views on:

- (a) the proposal to allow a REIT to engage in the development of a property that it intends to hold in its own portfolio when completed; and
- (b) whether the proposed 10% aggregate limit on commitments in

property development activities and investments in uncompleted  
property development is reasonable.

## **SECTION 7: INTRODUCING FLEXIBILITY IN BORROWING LIMITS**

7.1 Currently, a REIT is subject to a gearing limit of 35% of its deposited property. A REIT may borrow more than 35%, with no upper limit, if the REIT or all of its borrowings obtain a credit rating of at least “A” from a major rating agency. MAS proposes to amend the circumstances under which a REIT is allowed to exceed the current borrowing limit.

7.2 As the REIT market grows, it will be increasingly common for REITs to invest in overseas properties. We have received feedback from market participants that to manage currency risk, REIT managers of overseas properties would prefer to finance a higher percentage of overseas property investments by borrowing foreign currency<sup>5</sup>. In terms of currency exposure, borrowing in the REIT’s operational currency would result in a better matching of assets and liabilities, and of income and expenses. The higher interest expenses incurred may also be deducted from a REIT’s income tax liability, and such tax deductibility could have a significant effect on the profitability of a REIT that operates in a jurisdiction with high income tax rates. Thus the preferred capital structure of a REIT investing in overseas properties may be skewed towards the incurrence of more debt as a proportion of total assets than that of a REIT that invests solely in Singapore properties.

7.3 However, increased borrowing results in higher debt servicing costs, which may have a significant impact on a REIT’s distributions in a rising interest rate environment. Also, raising the borrowing limit from the current 35% to a higher threshold may encourage the listing of properties which are only able to meet market yield expectations because they are highly leveraged.

7.4 In order to enable REITs to have more room in determining their debt ratios and simultaneously take into account the associated risk of higher borrowings, MAS proposes to retain the current 35% borrowing limit where

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<sup>5</sup> For example, in Australia, REITs investing in overseas properties such as USA are generally geared between 35% to around 50% in order to align with the financing structure of REITs in USA.

the REIT is not rated. A REIT may exceed the current 35% borrowing limit so long as it obtains and discloses a credit rating from a major rating agency. Total borrowings shall in no case exceed 60% of the REIT's deposited property. This is in contrast to the current guideline where there is no upper limit on borrowings if a REIT obtains a credit rating of at least "A".

7.5 A credit rating is an independent assessment of the ability to service and repay debt. Ratings are also regularly reviewed and published, and provides additional information to investors in assessing the risks of investing in REITs and exerts market discipline on REIT managers. Thus, information on a rated REIT would help empower investors to make a more informed evaluation of the risks of their investment.

Q12: MAS seeks your views on the proposal to retain the current 35% borrowing limit where the REIT is not rated. A REIT may exceed the current 35% borrowing limit so long as the REIT obtains and discloses a credit rating from a major rating agency. Total borrowings shall in no case exceed 60% of the REIT's deposited property.

MAS welcomes suggestions on other disclosures that should be required to apprise investors of the risks associated with increased levels of borrowing.