

CONSULTATION PAPER

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Consultation Paper on Proposed Amendments to the Requirements for REITs

MAS

Monetary Authority of Singapore

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1 Preface

1.1 MAS is consulting on the proposed amendments to the Code on Collective Investment Schemes (“CIS Code”) to provide Singapore’s REITs with more flexibility to manage their capital structure and to streamline the fundraising process for REITs.

1.2 REITs are currently subject to a leverage limit of 45%. The leverage limit seeks to ensure that REITs do not over-extend themselves by pursuing highly geared property acquisitions. MAS is reviewing the leverage limit, and invites views and suggestions on the possible approaches to recalibrate the leverage limit. One possible approach is to use a combination of leverage limit and minimum interest coverage requirement in determining the amount of leverage that REITs should be allowed to take on. Under this approach, REITs may take on higher leverage if they are able to meet a minimum interest coverage ratio. This approach provides REITs with more flexibility to optimise their capital structure when bidding for assets, with the minimum interest coverage requirement serving as an additional safeguard by encouraging REITs to carefully assess their debt-servicing ability when taking on additional debt.

1.3 Separately, MAS is proposing to streamline the fundraising process for REITs by removing the requirement for REITs to submit a notification to MAS to obtain a “Restricted Scheme” status when they make an offer of units to accredited and other investors. This will make the fundraising process for REITs more efficient, and bring it in line with the fundraising process for companies and business trusts.

1.4 MAS invites comments from interested parties on the proposals set out in this consultation paper, including the proposed amendments to the Securities and Futures (Offers of Investments)(Collective Investment Schemes) Regulations 2005 (“SF Regulations”) in Annex B.

Please note that all submissions received will be published and attributed to the respective respondents unless they expressly request MAS not to do so. As such, if respondents would like (i) their whole submission or part of it (but not their identity), or (ii) their identity along with their whole submission, to be kept confidential, please expressly state so in the submission to MAS. MAS will only publish non-anonymous submissions. In addition, MAS reserves the right not to publish any submission received where MAS considers it not in the public interest to do so, such as where the submission appears to be libellous or offensive.

1.5 Please submit written comments by 1 August 2019 via email to: reits@mas.gov.sg. We would appreciate that you use this suggested format for your submission to ease our collation efforts. You can access the [template](#) here.

2 Defined Terms

Authorisation Regime	The regulatory regime governing the offers of collective investment schemes, including REITs, to the general investing public
CISNet	Online notification system that allows fund managers to notify MAS of their intention to offer Restricted Schemes to accredited investors and other investors (as defined under section 305 of the SFA)
CIS Code	Code on Collective Investment Schemes
MAS	Monetary Authority of Singapore
Notification Regime	The regulatory regime governing the offers of collective investment schemes to accredited investors and other investors as defined in section 305 of the SFA
Restricted Scheme	A collective investment scheme or REIT that is exempted under section 305 of the SFA from authorisation and prospectus registration requirements
REIT	A real estate investment trust that invests primarily in real estate and real estate-related assets as specified in the CIS Code, and listed on the SGX-ST
SFA	Securities and Futures Act (Cap. 289)
SGX-ST	Singapore Exchange Securities Trading Limited

3 Review of the Leverage Limit

Background

3.1 REITs are currently subject to a leverage limit¹ of 45%. The leverage limit seeks to ensure that REITs do not over-extend themselves by pursuing highly geared property acquisitions. The limit also helps to mitigate the risk of a REIT having to liquidate a major asset in its portfolio, at the bottom of a property market cycle, in order to service or repay debts.

3.2 While the regulatory limit is at 45%, REITs would in practice maintain a 5% buffer from the regulatory limit so that they are better able to respond to changing market conditions, for instance, declining property prices. The need to maintain such a buffer means that REITs would generally keep their leverage to within 40%. Given this, MAS has received feedback that REITs be afforded a higher leverage limit so that they have more flexibility to optimise their capital structure as debt tends to be a cheaper source of capital compared to equity and takes less time to raise. This flexibility is particularly important when REITs acquire overseas assets from third parties, which has been the trend in recent years driven partly by the search for assets with higher yield spreads. Unlike acquisitions from a REIT's sponsor, such acquisitions tend to involve a competitive bidding process and are highly time-sensitive.

Safeguards against over-leveraging

3.3 In evaluating the credit profiles of REITs, the key indicators that investors, analysts and credit rating agencies would normally consider are the REITs' debt levels and their ability to service the debt obligations on an on-going basis².

3.4 A number of REIT jurisdictions have imposed safeguards that are tied to leverage ratio (i.e. debt-to-asset ratio, which is a measure of how well a REIT is capitalised) or interest coverage ratio (or "ICR", which is a measure of a REIT's ability to service its debt obligations from regular sources of income).

3.5 Singapore and Hong Kong impose a leverage limit of 45% while Malaysia imposes a 50% limit. Thailand allows REITs to leverage up to 60% if they have an investment grade credit rating. Belgium, Germany and Netherlands have limits ranging from 60% to 66.25%. The US, Canada, Australia, France and Japan, on the other hand, do not impose any

¹ Total borrowings and deferred payments of a REIT divided by the REIT's deposited assets.

² Other indicators include debt maturity profile, fixed/floating interest rate liability profile and net debt to recurring operating EBITDA.

leverage limit. The UK also does not impose any leverage limit but requires REITs to maintain a minimum ICR of 1.25 times.

3.6 Leverage limit and minimum ICR serve different objectives – leverage limit seeks to ensure that a REIT is well-capitalised while a minimum ICR helps to strengthen the REIT’s debt-servicing ability. A case could therefore be made that in addition to leverage limit, REITs should also be encouraged to maintain a certain level of interest coverage. In this regard, MAS seeks views on whether the use of ICR in combination with leverage limit is appropriate, and what are the other possible approaches or credit metrics that could be considered in determining the amount of leverage.

Question 1. (a) MAS seeks views on whether the use of ICR in combination with leverage limit is appropriate; (b) Are there any other approaches or credit metrics that could be considered in determining the amount of leverage?

Possible approach to recalibrate the leverage limit

3.7 If the use of a combination of leverage limit and ICR is appropriate, one possible approach to recalibrate the leverage limit is to allow REITs to take on more debt only if they are able to meet a minimum ICR. This approach encourages REITs to carefully assess their ability to generate sufficient operating income to service interest payments, before they take on additional debt.

3.8 To strike a balance between providing REITs with more flexibility to optimise their capital structure and the need for them to carefully assess their debt-servicing ability, MAS is considering the option of allowing a REIT’s leverage to exceed 45% but not more than 50% if the REIT has a minimum ICR of 2.5 times after taking into account the interest payments arising from the new debt³ (“ICR Threshold”). The leverage limit is not considered to be breached if the REIT’s ICR subsequently falls below the ICR Threshold due to circumstances beyond the control of the REIT manager. However, the REIT should not incur additional borrowings or enter into further deferred payment arrangements.

3.9 MAS would also like to seek views on whether it is appropriate for a REIT that has demonstrated good financial discipline, such as having a higher ICR Threshold, to be allowed a higher leverage, say 55%.

³ The ICR should be computed based on (i) the REIT’s published financial statements for the most recent completed financial year, and (ii) assuming that the acquisition and the new debt had occurred at the beginning of that financial year and the interest payments under the new debt that had been made for that financial year.

Question 2. MAS seeks views on the option of allowing a REIT's leverage to exceed 45% but not more than 50% if the REIT has a minimum ICR of 2.5 times after taking into account the interest payments arising from the new debt.

Question 3. MAS seeks views on whether it is appropriate for a REIT that has demonstrated good financial discipline, such as having a higher ICR Threshold, to be allowed a higher leverage, say 55%.

Promoting market transparency

3.10 To promote market transparency, MAS proposes to require REITs to disclose both their leverage ratios and ICRs in interim result announcements and annual reports. MAS notes that this is already the practice for some REITs.

3.11 For comparability across the sector, the computation of the ICR should be standardised. MAS proposes that the ICR be defined as earnings before interest, tax, depreciation and amortisation (EBITDA) (excluding effects of any fair value changes) divided by interest expense.

Question 4. MAS seeks views on the proposal to require REITs to disclose both their leverage ratios and interest coverage ratios in interim financial results and annual reports.

Question 5. MAS seeks views on the proposal to define the interest coverage ratio as earnings before interest, tax, depreciation and amortisation (EBITDA) (excluding effects of any fair value changes) divided by interest expense.

4 Proposed Removal of the Notification Requirements for REITs

4.1 A REIT that intends to raise funds from the general investing public must first be authorised by MAS under the Authorisation Regime and must issue a prospectus that is registered by MAS.

4.2 Where a REIT undertakes a fundraising exercise by making an offer that is specifically targeted at accredited investors (as defined in section 4 of the SFA) and certain other persons (as defined in section 305 of the SFA), the REIT may rely on the exemption under section 305 of the SFA from the authorisation and prospectus registration requirements, provided it meets the following conditions:

- (a) It has a REIT manager that is licensed by MAS; and

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- (b) It submits an online notification to MAS to obtain a “Restricted Scheme” status under the Notification Regime. The notification must be accompanied by an information memorandum setting out salient information about the REIT and the offer (“Notification Requirements”).

4.3 MAS notes that the Notification Requirements make the fundraising process for REITs (both pre-IPO and post-IPO) more cumbersome than that for companies and business trusts, in two main aspects:

- (a) **Pre-IPO cornerstone process:** A REIT normally starts the discussion with cornerstone investors at an early stage of the IPO process. However, at this stage of the process, the REIT would not be in a position to file the notification as a Restricted Scheme given that the prospectus would not have been finalised and the REIT manager would not have received the Capital Markets Services licence. Hence, the REIT/underwriters would not be able to rely on the section 305 exemption to approach accredited investors. This means that the REIT and its underwriters can only approach accredited investors under the private placement exemption (i.e. limited to 50 investors) or under the exemption for offers to institutional investors. This limits the ability of the REIT and its underwriters to approach corporates and ultra-high net worth individuals and family offices at the cornerstone stage.
- (b) **Post-IPO private placements:** Following IPO, REITs (like other listed issuers) may undertake private placements to raise funds. REITs would typically invoke the section 305 exemption for such private placements. In order to comply with the Notification Requirements under section 305, REITs would have to incur additional time and costs to prepare the information memorandum and submit the CISNet notification to be a Restricted Scheme.

4.4 MAS is of the view that it would not be necessary to subject REITs to the Notification Requirements, given that they are (i) authorised by MAS under the Authorisation Regime, and (ii) required under SGX-ST’s listing rules to disclose all material information in a timely manner. MAS also notes that unlike REITs, companies and business trusts that are relying on the equivalent exemption (i.e. section 275 of the SFA) are not subject to any notification requirements. Given that the substance of the exemptions under sections 305 and 275 of the SFA is the same (i.e. to exempt offers that are limited in scope), MAS is of the view that the fundraising process and the approach to invoke the exemption for all the three types of listed vehicles should be consistent.

4.5 To streamline the fundraising process for REITs and bring it in line with the fundraising process for companies and business trusts, MAS proposes to remove the requirement for REITs to comply with the Notification Requirements when they rely on the section 305 exemption. This will be effected by way of an amendment to the SF Regulations⁴.

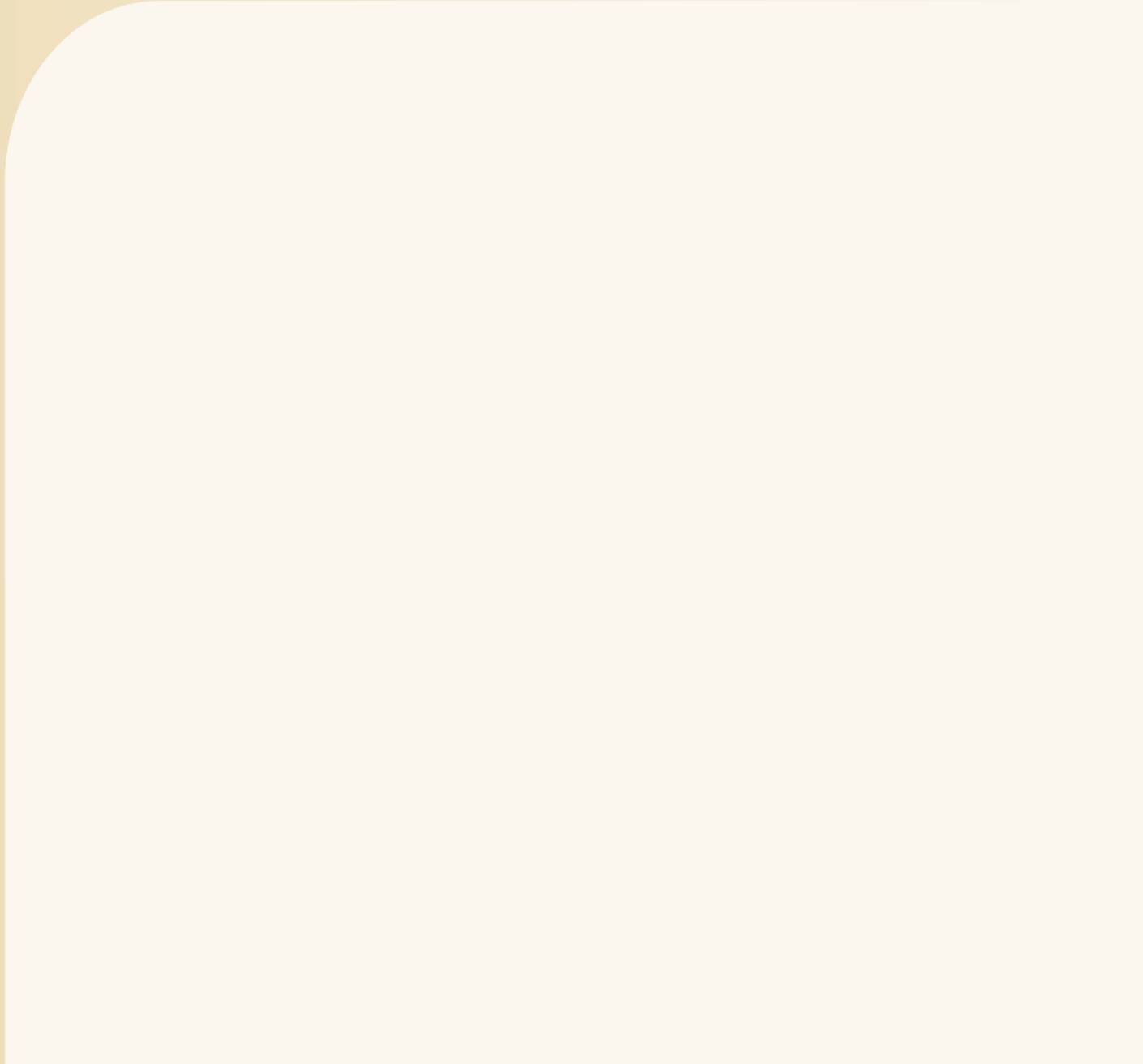
Question 6. MAS seeks views on the proposed removal of the requirement for REITs to comply with the Notification Requirements when they rely on the section 305 exemption.

⁴ The Notification Requirements reside in this set of regulations.

Annex A

LIST OF QUESTIONS

- Question 1.** (a) MAS seeks views on whether the use of ICR in combination with leverage limit is appropriate; (b) Are there any other approaches or credit metrics that could be considered in determining the amount of leverage?6
- Question 2.** MAS seeks views on the option of allowing a REIT's leverage to exceed 45% but not more than 50% if the REIT has a minimum ICR of 2.5 times after taking into account the interest payments arising from the new debt.....7
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