



MAS Issues Revised REIT Guidelines

The Monetary Authority of Singapore ('MAS') recently revised the guidelines ('Guidelines') for Real Estate Investment Funds ('REITs') contained in the Code on Collective Investment Schemes. The revisions implement a number of the proposals first set out in a consultation paper on the revised Guidelines released by the MAS on 23 March 2007. In brief, the revised Guidelines are intended:

- to establish measures to safeguard the interests of unitholders;
- to provide greater clarity and flexibility on investment guidelines;
- to rationalise guidelines where compliance costs exceed benefits; and
- to introduce a licensing framework for REIT managers under the Securities and Futures Act ("SFA").

The Changes at a Glance

In issuing the revised Guidelines, the MAS incorporated in full some of the proposal set out in the Consultation Paper and modified some others. The table below provides a snapshot of which proposals were incorporated in full, and which were modified pursuant to public feedback.

Proposal in Consultation Paper	Whether Implemented or Modified
Enhanced disclosure for short-term yield enhancing arrangements	Implemented as proposed.
Arrangements that entrench REIT managers	Implemented with modifications: Arrangements that provide for compensation for early termination allowed subject to certain conditions.
Prohibiting discounts to institutional investors at IPOs	Implemented with modifications: Discounts allowed for investors who assume risks different from those of IPO investors, and subject to certain conditions.



Proposal in Consultation Paper	Whether Implemented or Modified
Distribution of dividends in excess of current income to be permitted only if certain conditions satisfied, including certification by REIT manager that the REIT is able to pay its liabilities as they fall due.	Implemented with modification: Certification by REIT manager is to be made on reasonable grounds.
REITs to invest at least 75% of their assets in income-producing real estate.	Implemented as proposed.
Removal of 5% single party limit for investments in real-estate-related securities.	Implemented as proposed.
Allowing joint ownership through investments as tenants-in-common.	Implemented as proposed.
10% limit on revenue from non-rental operations.	Implemented as proposed.
Removal of prohibition against payments of more than S\$200,000 to valuers of a REIT's assets from buyers or sellers to the REIT.	Implemented as proposed.
Trustee to provide certain confirmations with respect to interested party transactions if price of property higher or lower than the average of the valuations obtained.	Implemented as proposed.
Enforceability confirmation only required for material contracts and not all contracts.	Implemented as proposed.
Removal of requirement for desktop valuations in certain circumstances, and subject to certain confirmations by the REIT manager.	Implemented with modifications: Requirement for confirmation by REIT manager has been dropped.
Removal of requirement for an opinion by an independent expert where the value of an interested party transaction is more than 5% of the REIT's net asset value.	Implemented as proposed.



Proposal in Consultation Paper	Whether Implemented or Modified
Removal of aggregation rule for transactions with the same interested party.	Implemented as proposed.
Modifying the definition of 'interested party' to bring it in line with the SGX Listing Manual.	Implemented as proposed.
Introducing a licensing and examination framework for REIT managers.	To be implemented as proposed and the Securities and Futures Act will be amended.

The changes effected by the revised Guidelines are discussed in greater detail below.

Short-Term Yield Enhancing Arrangements

Disclosure of short-term yield enhancing arrangements

The revised Guidelines stipulate that where forecasts of distribution yields are provided in offering documents, circulars, announcements and marketing materials of a REIT, these documents must clearly and prominently disclose any existing or proposed arrangement that materially enhances short-term yields while potentially diluting longer-term yields. In addition, offering documents and circulars should disclose:

- the risks associated with such arrangements,
- an analysis of how the arrangements may affect current and future yields, and
- a computation of the forecast distribution yield assuming that the arrangements are not in place.

For clarity, the MAS has explained that these requirements do not apply to arrangements which are entered into purely for hedging purposes, such as plain vanilla interest rate swaps and currency forwards.

Entrenching Terms in Management Agreements

In the Consultation Paper, the MAS had raised its concerns with management agreements that had the effect of entrenching



managers of REITs. To tackle this, the MAS had initially proposed only permitting arrangements that would tend to entrench REIT managers if these are approved by unitholders post-listing.

REIT managers need to recoup costs

However, during the public consultation, it was highlighted that REIT managers incur substantial costs in setting up a REIT, and hence measures that could prevent them from recovering these costs could ultimately discourage REITs from being established. We had suggested that a more nuanced approach might usefully strike a sustainable balance between imposing market discipline and providing certainty to the market.

Compensation provisions for early termination alright

In response to such feedback, the revised Guidelines now allow managers, prior to the listing of a REIT, to enter into management agreements with it that contain compensation provisions for early termination. Such provisions, however, must satisfy the following requirements:

- it should be clearly related to the commercial services provided by the manager in the performance of its duties;
- it should not be for more than five years;
- the compensation amount should be determined on an objective basis, and should not, in any event, exceed the sum of the fixed component of unearned management fees (excluding variable and performance fees) over the remaining term of the provision;
- the compensation should not be payable to the manager if its services are terminated for just cause such as fraud, insolvency or negligence; and
- the basis for computing such compensation must be clearly and prominently disclosed in the offering documents, circulars, or other relevant reports or documents to the participants.

The revised Guidelines remind managers that they need to carefully consider all such arrangements bearing in mind their responsibilities to act in the interests of REIT's participants.

Unitholders must approve provisions that restrict removal

On the other hand, arrangements that materially restrict the ability of participants to remove the manager cannot, at the time of the listing of the REIT, be included in management agreements. Such



arrangements may only be introduced after the REIT's listing. Furthermore, any such arrangements are subject to the following conditions:

- they should be specifically approved by way of a resolution passed by a simple majority of participants present and voting at a general meeting;
- the resolution must be a separate stand-alone resolution, independent of other resolutions;
- the manager, its associates and other interested parties should not vote on the resolution; and
- an independent financial adviser appointed by the trustee of the REIT should have provided an opinion stating whether the arrangement is on normal commercial terms and is prejudicial to the interests of participants.

Call options over REIT's assets may be a restrictive provision

It was also noted during the public consultation that a REIT may sometimes be established via a joint venture company. In such situations, the joint venture agreement may provide the joint venture partner with a call option to acquire the joint venture assets in the event that the services of the REIT manager are terminated. The MAS has clarified that it may regard this as a form of entrenchment of the REIT manager, and will generally do so if the call option is on more than 25% of the REITs assets.

Discounts to Institutional Investors

Commercial reasons for discounts highlighted

The MAS had proposed prohibiting REIT managers from offering discounts to institutional investors for subscribing to substantial amounts of REIT units issued at a launch. However, we had suggested that there was a sound commercial rationale for such discounts. It is, namely, that such discounts are offered as a "sweetener" to institutional investors to lock themselves into subscribing to units in the REIT some three to four weeks before its launch. The take-up of units by institutional investors is commercially useful as a signal to the market that the investment is sound and attractive, and provides guidance to retail investors on the quality of the REIT.



Discounts allowed under certain circumstances

In response to this feedback, the revised Guidelines now provide that discounts may be offered to institutional investors at the time of the listing of the REIT where:

- subscriptions by the institutional investors are made prior to the listing; and
- such investors assume risks of non-completion of the listing and/or have to pay for the units regardless of whether the REIT is subsequently listed.

Payment of Dividends in Excess of Current Income

Manager to certify and provide disclosure

The revised Guidelines provide that a REIT manager may make payment of dividends in excess of current income, provided that:

- it certifies, in consultation with the trustee, that it is satisfied on reasonable grounds that, immediately after making the distribution, the REIT will be able, from its deposited property, to fulfil its liabilities as they fall due; and
- it discloses its distribution policy and the measures and assumptions for deriving the amount available to be distributed from the REIT's deposited property.

Limits on Investments that May Be Made by a REIT

The revised Guidelines amend the previous limits on the types of investments which REITs can make (as a percentage of the REIT's assets). The new limits are discussed below.

Minimum 75% in income-producing real estate

Under the revised Guidelines, a minimum of 75% of a REIT's assets must be in income-producing real estate. The following will also be considered to be income-producing real estate for this purpose:

- income-producing real estate held through special purpose vehicles (so long as certain conditions in the Guidelines are satisfied); and
- investments in other authorised REITs.

Maximum 25% in other permissible assets

The remaining 25% of a REIT's assets may be invested in real-estate related assets (e.g., shares in real estate companies) and such other



permissible investments as may be specified in the revised Guidelines. In addition, any such investments—if made in securities issued by a single party—must be limited to 5% of the REIT's assets. This 5% limit, however, does not apply to the following:

- real-estate related securities issued by a single party;
- deposits with appropriately rated financial institutions;
- high quality money market instruments; and
- high quality debt securities.

10% limit on property development

The total contract value of property development activities undertaken and investments in uncompleted property developments remain restricted to 10% of the REIT's deposited property.

10% limit on non-rental revenue

Finally, the revised Guidelines provide that a REIT should not derive more than 10% of its revenue from sources other than:

- rental payments (including, as clarified by the MAS, ancillary or incidental income such as maintenance contributions, income from the use of signage space, and advertising contributions); and
- interest, dividends, and other similar payments from special purpose vehicles and other permissible investments of the REIT.

This requirement applies throughout the life of the REIT, and not just at the time of its listing.

Joint Ownership

REITs can own property jointly

The revised Guidelines allow REITs to jointly own real estate directly instead of through a special purpose vehicle. The REIT may own the property as tenant-in-common. This is to allow a REIT to continue, under such circumstances, to take advantage of the waiver of stamp duty that applies where a REIT purchases real estate directly.

Requirement for Desktop Valuations Removed

The Guidelines previously required that a desktop valuation be conducted for all the real estate assets of a REIT where:



- new units in the REIT were to be issued post-listing; and
- the last valuation was more than six months old.

The revised Guidelines remove this requirement. Furthermore, while it had been proposed that the REIT manager confirm that there is no material change in the value of the properties since they were last valued, this proposal has not been adopted in the revised Guidelines.

Requirement for Enforceability Confirmation Relaxed

Only material contracts require confirmation

The Guidelines previously required REIT trustees to ensure that all contracts entered into on behalf of the REIT are legal, valid, binding, and enforceable by or on behalf of the REIT in accordance with its terms. The revised Guidelines provide that this requirement for a review only applies to material contracts. These are stipulated to include the following:

- contracts which constitute 5% or more of the REIT's gross revenue; and
- contracts which are not in the ordinary course of business.

Prohibition Against Payments of More Than S\$200,000 Removed

Payment limits removed

The Guidelines previously prohibited a valuer of a REIT's assets from receiving payments of more than S\$200,000 in a financial year from parties who buy or sell assets to the REIT. This requirement has been removed in the revised Guidelines.

Definition of 'Interested Party'

Definition amended for consistency with Listing Manual

For consistency, the definition of 'interested party' in the revised Guidelines has been amended to bring it line with the SGX Listing Manual. The definition now provides that the following are 'interested parties':

- the manager for the REIT;
- the trustee for the REIT;
- the director/CEO of the manager for the REIT;
- the controlling unitholder of the REIT; and



- an associate of the manager, trustee, director, or controlling unitholder.

For the purposes of determining whether a person is an associate, the threshold percentage of interest to be held by the manager, trustee or controlling unitholder in that person must be at least 30% (and not 25% as previously specified). On the other hand, the sponsor of the REIT has been removed from the definition of 'interested party'.

Trustee to Provide Confirmations of Certain IPTs

Confirmations to be provided if out of line with average

The Guidelines previously required two valuations to be obtained for all acquisitions from or disposals to interested parties. If the acquisition price was more than the lower of the two valuations, or the disposal price was less than the higher of the two valuations, the Guidelines previously provided that the trustee provide a written confirmation that the transaction was carried out on normal commercial terms and was not prejudicial to the interests of unitholders. The revised Guidelines still require that the written confirmation be provided, but only where:

- the acquisition price is higher than the average of the two valuations; or
- the disposal price is lower than the average of the two valuations.

Removal of Certain Requirements as to IPTs

Expert opinion and unitholders' approval no longer required

The following requirements in relation to interested party transactions ("IPTs") have been removed:

- the requirement for an independent expert to opine on whether the transaction is carried out on normal commercial terms and is not prejudicial to the interests of unitholders where the value of a proposed IPT is equal to or greater than 5% of a REIT's net asset value; and
- the requirement for unitholders' approval for IPTs with values equal to or greater than 5% of the REIT's net asset value in a financial year.



Regulatory Framework for REIT Managers

REIT managers to be licensed

The Consultation Paper had proposed establishing a new regulatory framework for REIT managers. This proposal will be implemented and amendments will be made to the Securities and Futures Act to effect it. Accordingly, they are not dealt with in the revised Guidelines.

The framework will be similar to that for providers of capital markets services and, accordingly, will consist of the following key aspects:

- REIT managers must be licensed to act as such;
- REIT managers will be subject to capital and other requirements; and
- professional employees of REIT managers must hold a capital markets services representative's licence and meet minimum entry and examination requirements similar to those applicable to existing capital markets services representatives conducting other regulated activities.

The MAS has clarified that the regulatory framework will also catch managers of REITs that hold cash reserves or derivative contracts within the limits specified in the Guidelines.

When implemented, existing REIT managers will be migrated over to the new regime. In addition, the MAS will waive the examination requirement for their professional employees. These individuals will instead undergo a non-examinable course covering the same topics as the proposed exam.

If you would like information on this or any other area relating to the listing of REITs, you may wish to contact the lawyer at WongPartnership that you normally deal with or contact the following partners from the ECM Practice:



RACHEL ENG

DID: +65 6416 8002

Email:

rachel.eng@wongpartnership.com.sg

[Click here to see Rachel's CV](#)



RAYMOND TONG

DID: +65 6416 8207

Email:

raymond.tong@wongpartnership.com.sg

[Click here to see Raymond's CV](#)