

Insights

REAL ESTATE INVESTMENT TRUSTS IN HONG KONG MAY SOON BENEFIT FROM ENHANCED INVESTMENT AND BORROWING POWERS

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As noted in the Consultation Paper issued by the Securities and Futures Commission (“**SFC**”) on 9 June 2020, an SFC-authorized REIT is currently allowed by the SFC to have less than ‘majority ownership and control’ of real estate subject, in aggregate, to a cap of 10% of its gross asset value (“**GAV**”) and provided:

- (1) the manager of the REIT can demonstrate on a case by case basis (to the satisfaction of the SFC) that an investment in each such property is in line with the REIT’s investment strategy and objectives and is in the best interests of Unitholders; and
- (2) there is prominent disclosure of risk warnings to Unitholders in respect of each such property regarding the lack of majority ownership and control.

In addition to (1) and (2) above, the SFC is now proposing that REITs can include the value of minority interests in income-generating real estate (where the joint ownership arrangement confers veto rights over certain key management issues and the right to receive at least 50% of the net income generated from such real estate) to satisfy the existing requirement that at least 75% of GAV is invested in income-generating real estate (“**Core Investments**”).

Under a totally separate limb, the SFC is proposing to allow a REIT to hold minority-owned real estate which does not qualify for inclusion in the calculation of its Core Investments provided that the value of such non-qualifying minority-owned real estate:

- (a) is included in the calculation of ‘non-core investments’ which term also includes investments in listed securities and real estate funds, property development projects and other ancillary investments, the aggregate of which must be less than 25% of GAV (the “**Non-Core Investment Cap**”); and
- (b) accounts for less than 10% of GAV (i.e. the Single Investment Cap).

The SFC’s Consultation Paper also invites comments on the following proposals:

- Property development – should a REIT be given more freedom, subject to Unitholders’ approval and the Non-Core Investment Cap, to invest in property development projects in excess of the existing limit of 10% of GAV?
- Connected party transactions and notifiable transactions – should the requirements for REITs be aligned with the requirements for companies listed on the Hong Kong Stock Exchange?
- Borrowing limit – should a REIT be given more freedom to borrow in excess of the existing borrowing limit of 45% of GAV, subject to a cap of 50% of GAV?

Other miscellaneous amendments to the REIT Code are proposed, including:

- (i) codifying the public float requirement i.e. 25% or such other minimum percentage as the SFC may agree, which is currently an authorisation condition;
- (ii) clarifying that a REIT may engage another qualified property valuer to value a particular property where its principal valuer is conflicted out;
- (iii) enabling REITs to display documents for inspection by uploading them to their websites; and
- (iv) removing the limitation on the use of two layers of special purpose vehicles.

The deadline for the submission of comments in response to the SFC’s Consultation Paper is 10 August 2020.

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