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A REIT STRUCTURE FOR IRELAND

October 2011

REITs Forum

- REITs Forum established to consider the principle of introducing REITs in Ireland
- Significant work performed on various matters including structure, taxation, listing requirements, marketing / demand
- Met and received support from European Public Real Estate Association (EPRA) – main real estate association in Europe with 200 members including REITs / property companies, investors and banks

Company	Focus
W.K. Nowlan & Associates	Property
NCB	Capital Markets / Marketing / Governance
IPUT	Property / Structure
Byrne Wallace	Legal / Structure
Eversheds O'Donnell Sweeney	Legal / Structure
A&L Goodbody	Legal / Structure
William Fry	Legal / Structure
Matheson Ormsby Prentice	Legal / Structure
KPMG	Taxation
Irish Life Investment Managers	Institutional Investors
Irish Stock Exchange	Listing Requirements

Purpose

- Purpose of presentation:

1. Discuss benefits of a REIT structure for Ireland & NAMA
2. Considerations for an Irish REIT regime
   - Structure / Governance
   - Taxation
   - Investor appetite
3. Consider the initial Irish REIT

A REIT Structure For Ireland

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- Irish property market is experiencing huge challenges
  - Substantial reductions in property values in recent years
  - Little or no liquidity in the current market
- The substantial expansion of REIT structures around the world – in the US and Australia in the early 1990s and in Japan in the late 1990s – typically coincided with an overhang of property investments and a shortage of capital
- Fine Gael Manifesto 2011 – *"open to considering new types of investment vehicles – such as U.S. style Real Estate Investment Trusts – that can help create a new, liquid investment market in commercial property for Irish pension funds and smaller investor"*
- Main task of NAMA over the next 7 to 10 years is to recover the €30 billion plus paid to acquire property loans
- For this to occur the property market needs to be re-activated and transactions need to be generated
- Inflow of capital from abroad will be a crucial part of any recovery plan – need to capitalise on the appetite of those with funds for investing in Irish property
- NAMA is looking to be creative in identifying solutions to get the market moving

What is a REIT?

- Real Estate Investment Trusts ("REITs") are publicly traded companies that own and manage investment-grade real estate
- Taxes are paid at the shareholder level once certain criteria are met, for example:
  - Company must be in the real estate business
    - At least 75 percent of assets must be real property
    - At least 75 percent of revenue must come from real estate
  - High percentage (90%) of taxable income must be distributed annually to shareholders
- REITs provide a simple and inexpensive way to invest in real estate without buying property directly
- Full-time professional management teams
- Business plans designed to maximise shareholder value
- High standard of financial reporting and transparency
- Traditional corporate governance and accountability

The REIT Industry in 2011

- REITs are firmly established in the global Real Estate market
  - Approx 500 REITs globally
  - Market Cap of €450bn – USA makes up over 50%
  - US REITs made up of Equity REITs (92.1%), Mortgage REITs (7.5%) and Hybrid REITs (0.4%)
- REITs represent a liquid, transparent and professionally managed asset class
- Offer diversified exposure to real estate returns and high cash dividends
- Regimes vary globally, however, have one common feature – tax transparency at corporate level
- The substantial expansion of REIT structures around the world – in the US and Australia in the early 1990s and in Japan in the late 1990s – typically coincided with an overhang of property investments and a shortage of capital

Country	Date Introduced	Number of Companies	Sector Market Cap €bn	% of Global REIT Market
Belgium	1995	14	4.6	1.0%
Finalnd	2009	0	-	-
France	2003	44	43.1	9.6%
Germany	2007	2	0.5	0.1%
Greece	1999	2	0.3	0.1%
Israel	2006	0	-	-
Italy	2007	1	0.3	0.1%
Luxembourg	2007	0	-	-
Netherlands	1969	7	7.9	1.8%
Spain	2009	0	-	-
Turkey	1995	15	1.5	0.3%
United Kingdom	2007	23	30.0	6.7%
USA	1960	175	236.9	52.6%
Canada	1995	35	19.5	4.3%
South Africa	1969 / 2003	5	3.0	0.7%
Australia	1985	60	50.0	11.1%
Hong Kong	2003	7	7.6	1.7%
Japan	2000	36	24.3	5.4%
Malaysia	2002 / 2005	14	2.3	0.5%
New Zealand	1960 / 2007	8	1.8	0.4%
Singapore	2002	21	16.6	3.7%
South Korea	2001	6	0.2	0.1%
Thailand	1992	6	0.2	0.1%
Total		481	450.5	100.0%

Source: EPRA, September 2010. UK REIT data updated for new REITs since Sept 2010

Benefits of REITs

1. **Regular high-yield returns** – c.7%; a minimum 90% of income profits must be distributed to shareholders. Particularly attractive for investors that have seen yields eroded over the last few years
2. **Liquidity** – easier to buy/sell than direct property. Ownership of direct property left to the professionals
3. **Experienced managers** – day-to-day operations are conducted by full-time experienced property managers with the expertise to manage property/increase value
4. **Economies of Scale** – one property team can manage multiple assets
5. **Diversification** – greater ability for diversification as a result of a spread of tenants and lease covenants
6. **Capital Preservation** – capital preservation and protection from inflation
7. **Long-term performance** – outperformance of other investment asset classes
8. **Tax transparency** – there is taxation at the investor level only, attractive to gross funds, charities, private pensions
9. **Controlled gearing** – leverage restrictions control gearing and help to protect equity holders
10. **Strong corporate governance –** REIT must comply with conditions set out in tax legislation or risk additional tax charges / expulsion

Irish Listed Property Sector

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- Ireland does not have a listed property sector
- Wide range of benefits arising from having a proper listed property sector:

1. Increased transparency – Listed property companies exercise the highest standards of financial reporting due to need to respond to investors demand for high quality information
2. Stability and liquidity – No defaults by European REITs following the crisis and successful equity raisings
3. Sustainability reporting and practices – evidence shows that listed property/REITs are being pioneers for the sector – leading the way in both developing sustainable practices and reporting these to investors in a consistent and comparable way
4. Increased liquidity going forward
5. Improved quality of built environment
6. Access to indices like the EPRA FTSE NAREIT index

- Opportunity to create an international friendly REIT structure – attracting foreign REITs to list/domicile in Ireland

Time for Irish REITs

- Correctly structured REIT regime can provide benefits for investors, government, Irish real estate market and the wider Irish economy
- Fine Gael Manifesto 2011 – *“open to considering new types of investment vehicles – such as U.S. style Real Estate Investment Trusts – that can help create a new, liquid investment market in commercial property for Irish pension funds and smaller investor”*
- €300-500m REIT could be launched in the short term with a target of achieving an Irish REIT industry of €2bn in 5 years

<u>Time has come for REIT in Ireland because:</u>

1. Only country in Europe without some form of REIT regime or established listed property market
2. REITs would get the market moving by generating transactions and reinvigorating the property market
3. Foundation for a functioning, mature listed property sector in Ireland
4. Tax receipts for exchequer on increased share liquidity
5. Vehicle to assist unwinding of NAMA’s ‘warehouse’ of assets, avoids fire sale and disruption of markets. Good asset recovery story with the ability for NAMA to retain a stake and partake in potential upside
6. Appetite for rental property from investors – private and institutional; domestic & foreign; yield hungry investors. Good dividend yield for investors seeing regular income – approximately 7%

Benefits for NAMA

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1. Vehicle to unwind assets/loans

- Ability to unwind large tranches of assets/loans
- Ability to include smaller assets/loans that may otherwise require significant resources to sell
- Structure which can be repeated
- Good asset recovery story

2. Receive Value for Property Assets

- Avoids fire sale and disruption of markets
- Provides NAMA with alternative route to market than direct sales/auctions
- Investors should recognise value of investing in focused REIT vehicle which will provide environment for assets to reach their full potential

3. Stabilise the Irish Property Market

- REITs would bring stability and liquidity back to the Irish commercial real estate market
- Attract international investors into the Irish property market
- Bring domestic investors back to the Irish property market

4. Ability to retain stake

- Retaining stake demonstrate confidence in REIT structure
- Benefit from high dividend yields and potential future upside
- Transfer listed shares to NPRF, reduces balance sheet of NAMA
- Stock can be sold down in tranches as demand builds up
- Suitable warehouse for assets to realise their full potential

Proposed Structure / Listing Rules

- REITs would be listed on the Irish Stock Exchange
- Irish Stock Exchange to develop a standalone listing regime for "Property Investment Companies"
  - Will not require 3 year track record as required for Property Trading Companies seeking to list
  - Will not be regulated by the Central Bank as required for CEIF's
- On the condition that a company falls within the definition of a REIT under Irish tax legislation (next slide) then it can be listed under the Property Investment Company regime
- Appropriate governance of REITs will be essential from an investor confidence perspective
- Domestic and International investors are familiar with the Irish Stock Exchange
  - Listing procedures
  - Rules / Governance
  - Reporting requirements
- Research coverage, market making by the Irish brokers and overseas specialists

Definition of REIT for Tax Purposes

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- Suggest that a REIT should be a company which is:

1. Quoted on a recognised exchange
2. Irish resident
3. Is not a 'close company'
4. Carries on a property rental business in Ireland , but may hold assets worldwide
5. Meets the acceptable distribution policy of ➔ 90% of its exempt income (not gains) from its rental business
6. At least 75% of its assets must relate to its property rental business
7. Maintains a profit/financing ratio of 1.25/1
8. Should, perhaps, have a debt/equity limit of 1/1 at the time of each material property acquisition
9. And, has elected to be a REIT under Irish tax legislation.

- Definition is substantially based on the UK model
- Recommend adopting legislation and Revenue practice on a similar basis to deal with compliance with the REIT rules, (including how to deal with minor breaches or technical matters) which benefits from the UK's extensive experience in these matters

Proposed Taxation of Irish REITs

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Company Level

1. Exempt from CGT and income /corporation tax on its property rental business provided it meets acceptable distribution rules
2. Obliged to operate dividend withholding tax 20% from all income distributions
3. May also carry on a normal taxable business
4. Would pay normal stamp duty on property purchases once initially established
5. May include all 75% subsidiaries in its REIT exemption

Shareholder Level

1. Irish resident shareholders are liable to income tax /corporation on all distributions and CGT on share sales
2. Non resident shareholders are entitled to exemption from/ refund of dividend withholding tax if treaty based, and are exempt from CGT

Demand for Irish REITs

- Sufficient demand from foreign and domestic investors – need to capitalise on those with funds for investing in Irish property
- Core base of investors in Irish REITs likely to be local and foreign institutional investors – many institutional investors in European REITs are already investors in Irish equities
- €300-500m REIT could be launched in the short term with a target of achieving an Irish REIT industry of €2bn in 5 years

Key attractions for investors:

1. REIT structure widely accepted by investors
2. Reliable and significant current income which grows over time
3. Highly transparent structure with strong corporate governance and reporting standards
4. Ownership of direct property left to the professional management teams
5. Attracted to high yield offered versus other real estate investment structures and other securities – particularly attractive for those investors that have seen yields eroded over the last few years
6. Absence of other yield alternatives in the Irish market (bonds / equities)
7. Attractive entry point into high grade Irish property assets
8. Domestic and International investors are familiar with the Irish Stock Exchange

REIT Seed Portfolio – Key Considerations

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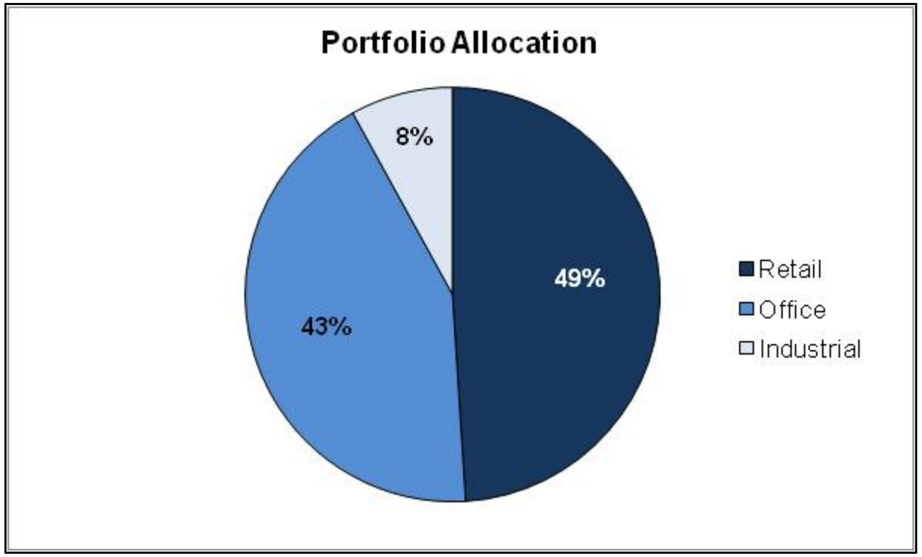
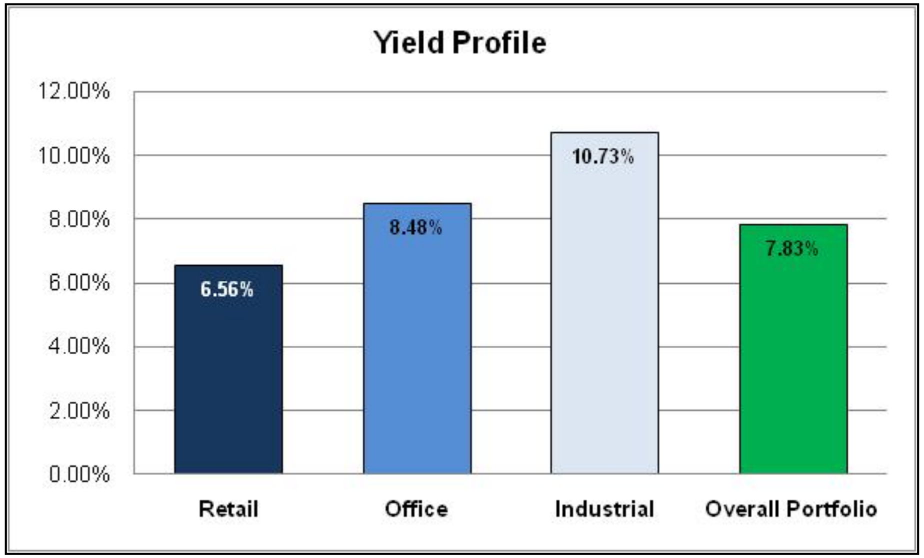
Key Consideration	Overview
Pricing	• Initial pricing of REITs and the assets held would need to hold up to robust scrutiny • Could be marketed on the fact that investors would be getting in at prices which are back at 2000 levels • Attractive entry point pricing should limit the extent of any discount to NAV in secondary market trading
Source of Properties	• Nama • Certain non-Nama banks • Other property owners
Asset Composition	• Quality property assets to be sourced • Diversified across all property types – office, retail, industrial • Allocation to residential to be carefully considered
Geographic Location	• Location is key consideration • Specific geographic focus i.e. Ireland • Main cities – Dublin, Cork, Galway, Limerick
Size / Market Cap	• €300-500m REIT assuming Nama and non-Nama banks participation, with a target of achieving an Irish REIT industry of €2bn in 5 years

Sample REIT Portfolio

- Sample Investment Portfolio with a total value of €500M
- Sample portfolio contains 29 properties
- Average value of c.€17 million
- Majority of portfolio split across Offices and Retail
- 8% industrial allocation to portfolio
- Residential to be carefully considered as part of portfolio
- All properties located in Dublin
- Initial Yield of 6.56%, 8.48% and 10.73% for Retail, Office and Industrial respectively
- Overall portfolio yield of 7.83%



Source: WK Nowlan



Source: WK Nowlan

Conclusion

- Irish property market is currently experiencing significant challenges
- Correctly structured REIT regime can provide benefits for investors, government, Irish real estate market and the wider Irish economy
- Wide range of benefits arising from having a proper listed property sector – transparency, stability & liquidity
- REITs would get the market moving by generating transactions and reinvigorating the property market
- Foundation for a functioning, mature listed property sector in Ireland
- REITs would be listed on Irish Stock Exchange – subsequent listing elsewhere could be considered, as could potential inclusion in real estate indices (e.g. FTSE EPRA/Nareit Europe REIT Index)
- Similar structure and taxation to overseas REITs, tried and tested structure internationally
- Benefits for NAMA:
  - Potential vehicle to assist unwinding 'warehouse' of assets
  - Receive value for property assets
  - Stabilise the Irish property market in which NAMA now plays a significant role
  - Ability to retain a stake and gain from potential upside
- €300-500m REIT could be launched in the short term with a target of achieving an Irish REIT industry of €2bn in 5 years