Linklaters

REITs in Asia.

While real estate investment trusts ("REITs") have become established investment vehicles in both the U.S. and Australian markets, REITs only arrived in Asia in late 2001, with Japan being the first Asian country to introduce REITs. This article looks at the current state of play in Korea, India, Malaysia, Taiwan, Singapore, Hong Kong and Thailand and summarises the REIT offerings that have been made public to date in these jurisdictions.

Contents

Korea	1
India	4
Malaysia	6
Taiwan	10
Singapore	11
Hong Kong	16
Thailand	21
Contacts	24

Korea

Overview

The Korean Real Estate Investment Trust Act ("K-REIT Act") came into effect on 1 July 2001, making indirect investments in real estate possible and allowing companies and their creditors to dispose of real estate as part of the corporate restructuring process.

Structuring K-REITs and CR-REITs

The K-REIT Act provides for two types of real estate investment trusts ("REITs"). The first category are K-REITs, which can invest in all types of real estate-related assets and the second category are corporate restructuring REITs ("CR-REITs"), which can invest in real estate assets being sold by companies undergoing restructuring due to insolvency or reorganisation, or companies that intend to use the proceeds of the sale to retire debt obligations.

Under the K-REIT Act, K-REITs are established as limited liability joint stock companies which must be perpetual corporations. CR-REITs, on the other hand, must be paper companies with a corporate life, the length of which is set out in the CR-REIT's Articles of Incorporation (which is typically five years with an option to extend) and are prohibited from hiring employees and full-time directors. The five-year life-span has led to difficulties in establishing a trading price for their stock, especially during the last two years of corporate existence. The minimum paid-up capital of a K-REIT or a CR-REIT is 50 billion Won (approximately U.S.$40 million).

To incorporate a K-REIT, a licence will need to be obtained from the Ministry of Construction and Transportation. 30 per cent. or more of the shares of the K-REIT must be issued through a general public offering and the shares of the K-REIT must be listed on the Korea Stock Exchange ("KSE") or on the Korea Securities Dealers Automated Quotation ("KOSDAQ"). The percentage shareholding of the largest shareholder must not exceed 10 per cent. Contribution in-kind of real property in return for shares of the K-REIT is prohibited before the K-REIT's shares are listed.

To incorporate a CR-REIT, a licence will also need to be obtained from the Ministry of Construction and Transportation. A minimum of 90 per cent. of the taxable income of a CR-REIT must be distributed as dividends. A CR-REIT can be converted to a K-REIT at the end of its five-year life-span. A CR-REIT is not required to issue shares by way of a general public offering at the time of incorporation, but the K-REIT Act requires that a CR-REIT should be listed as soon as it would be able to meet the listing requirements of the KSE or KOSDAQ, in terms of the number of stockholders, minimum shareholding by minority shareholders, etc.

Permissible Investments

K-REITs are required to have a minimum of 70 per cent. of their total assets invested in real estate (which can be freehold, leasehold or buildings in the process of construction). Of the remaining 30 per cent., 20 per cent. of their assets may be invested in cash and real property-related marketable securities (as defined in the K-REIT Act), which includes shares of on-shore REITs, housing bonds, trust certificates issued by real estate trust companies, subway bonds (bonds issued by the government to fund the construction of subways), and mortgage bonds (together "Marketable Securities").

CR-REITs are required to have 70 per cent. of their total assets invested in:

- real estate which has been sold to it by a company to repay debts to financial institutions;
- real estate which has been sold to it by a company to discharge its obligations under a financial restructuring agreement entered into with financial institutions;
- real estate which has been sold to it by a company pursuant to judicial proceedings as a consequence of a corporate restructuring or compulsory composition plan; and
- real estate which has been sold to it by a company to bolster its liquidity, if this has been deemed necessary by the Financial Supervisory Commission.

CR-REITs are permitted to invest the remaining 30 per cent. of their assets in cash and securities generally.

Mandatory Outsourcing of Operations and Conflict of Interests

Under the K-REIT Act, K-REITs may manage their own business activities, including asset management, accounting and administrative functions. CR-REITs, however, must assign such business activities to asset management corporations ("AMCs"). For an AMC to be eligible to manage a CR-REIT, it must have seven billion Won in equity and employ five full-time real estate experts, such as licensed brokers or real estate appraisers. AMCs must be licensed by the Ministry of Construction and Transportation. In order to be licensed, the AMC must be a Korean-incorporated company, although foreign equity ownership of up to 100 per cent. is permitted.

Borrowing Limits

In general, K-REITs and CR-REITs are not permitted to borrow, although they are allowed to borrow funds to meet temporary mismatches in cashflows or to fund the assumption of lease liabilities on the purchase of real estate.

Taxation

The K-REIT Act does not provide for the "pass-through" of taxes to the end-investors in a K-REIT or a CR-REIT, unlike the position with U.S.-style REITs. Dividends paid by CR-REITs are tax deductible if the CR-REIT distributes 90 per cent. or more of its profits to investors.

K-REITs enjoy a 50 per cent. exemption on both acquisition tax which is currently 2.2 per cent. and registration tax which is currently 3.6 per cent., whilst CR-REITs are fully exempt from acquisition tax and registration tax.

K-REIT and CR-REIT Offerings

K-REITs are not preferred by investors as the dividend income is subject to taxation at both the K-REIT and investor levels, unlike CR-REITs. CR-REITs have, as such, been more popular with the first CR-REIT, Kyobo-Mertiz First, being listed on the KSE on 30 January 2002. Kyobo-Meritz First was set up by Meritz Securities Co. Ltd. The second CR-REIT in Korea was Kocref CR-REIT I which was set up by Meritz Securities Co. Ltd., Hyundai Securities Co. Ltd and SK Securities Co. Ltd and was listed on the KSE on 30 May 2002. On 7 January 2003, Macquarie Bank listed a CR-REIT, The Macquarie Central Office Corporate Restructuring REIT or MCO CR-REIT, on the KSE. This was the seventh listing in Korea and the first CR-REIT managed by an asset management company, which is wholly-owned by a foreign company.

This section on Korea has been prepared in consultation with Kim & Chang. If you have further questions as to matters of Korean law, please contact Yon Kyun Oh on (82) 2 3703 1062 or by email at ykoh@kimchang.com.

India

Overview

At present there are no regulations specifically governing real estate investment trusts in India. The Securities and Exchange Board of India ("SEBI") is responsible for the regulation of the investment fund market in India and the promulgation of the governing regulations. Mutual funds in India are regulated by the Securities and Exchange Board of India (Mutual Funds) Regulations 1996 (the "SEBI Regulations") which set out the requirements as to investment objectives, restrictions placed on making investments and the constitution and management of mutual funds. The SEBI Regulations currently provide that moneys invested in a mutual fund should only be invested in the money markets or the capital markets by way of transferable securities, privately-placed debentures or securitised debt. In the case of securitised debt, mutual funds are permitted to invest in asset-backed securities and mortgage-backed securities, provided such securities have an investment grade credit rating, and in the case of mortgage-backed securities, such securities represent investments in mortgages secured by real estate collateral rather than a direct investment in real estate itself.

In December 1999, the Association of Mutual Funds of India ("AMFI") appointed a committee chaired by Mr Deepak Satwalekar (the "Satwalekar Committee") to consider the possibility of introducing real estate investment schemes for mutual funds in India. After a detailed study of REITs in a number of jurisdictions and a review of the existing regulatory structure in India, the Satwalekar Committee submitted a report to AMFI in October 2000 (the "Report"). Subsequently AMFI set up a sub-committee to further investigate how, based on the findings of the Report, REITs might be introduced in India. The sub-committee formulated a working plan (the "Working Plan") which was submitted to AMFI in August 2002.

Structuring Real Estate Mutual Funds

The Working Plan recommends that REITs in India should be structured as Real Estate Mutual Funds ("REMFs"). Mutual funds would be able to launch one or more "real estate schemes" which would own, manage and develop pools of properties, so that a mutual fund may have a number of different real estate schemes, all investing in real estate. The Working Plan further recommends that the existing regulatory structure relating to mutual funds be extended to permit REMFs and that a trust structure would be the most appropriate vehicle. The form of the REMF recommended by the Working Plan is a type of interval fund which would be closed-ended for a minimum period of three years and open at the end of each quarter for a minimum period of 15 days to allow for the fresh sale of units based on the quarterly net asset value calculation. As the REMF would be an interval fund, offering redemption at the end of three years, the REMF may be listed on any stock

exchange to offer investors liquidity. It is envisaged that at some point in the future, REMFs could be open-ended once the marketability of the underlying assets and investments has improved.

Permissible Investments

As regards the types of investments which REMFs could invest in, the Working Plan suggests that permitted investments could include shares, bonds and debentures of listed companies dealing in real estate and undertaking property development, as well as mortgage-backed securities (when available). It is also proposed that REMFs should be able to purchase income-generating rental properties, engage in real estate project financing and construction financing and undertake the speculative purchase of property under construction with a view to resale at a later date, as well as investing in privately-placed debt securities issued by development and construction companies. The Report also proposes a number of restrictions which should be placed on investments, including:

- a prohibition on any mutual fund under all its real estate schemes having an exposure of more than 25 per cent. to all real estate projects developed, marketed, owned or financed by a group of companies;
- a prohibition on any mutual fund under all its real estate schemes having an exposure of more than 15 per cent. to a single real estate project; and
- unless otherwise stated in the offer document, a prohibition on any mutual fund owning real estate assets in excess of 30 per cent. of its total assets in any one city.

Mandatory Outsourcing of Operations and Conflicts of Interests

Only asset management companies with the requisite expertise, should be permitted to launch REMFs. The Report recommends that either the sponsor or the asset management company should possess at least five years experience in real estate management. Alternatively an adviser with a minimum of five to seven years experience in real estate development or management can be appointed on a fee-sharing basis. An asset management company is required to be an Indian company incorporated pursuant to the Companies Act 1956. The SEBI Regulations also stipulate that the asset management company should have a net worth of at least 100 million rupees. Net worth is calculated by aggregating the company’s paid-up capital and available reserves.

Borrowing

The SEBI Regulations provide that Indian mutual funds are not permitted to borrow, other than in circumstances where borrowing is necessary to meet temporary liquidity needs for the purpose of repurchasing or redeeming units or to pay interest or dividends to unitholders. A mutual fund is not permitted

to borrow more than 20 per cent. of the net asset value of the fund and the period of the borrowing may not exceed six months.

Taxation

The Report also recommends that the present provisions of the Income Tax Act 1961 (the “IT Act”) which are applicable to mutual funds, should also be applicable to REMFs. Pursuant to the IT Act, any income distributed by a mutual fund to its unitholders is chargeable to income tax payable at a rate of 10 per cent. The profits of mutual funds are currently not subject to tax. The acquisition of real estate will give rise to a charge to stamp duty on the deed of conveyance and the payment of a registration fee to register the deed of conveyance with the central land registry.

Issues inhibiting the establishment of a market for REMFs in India are the lack of a sufficiently deep market for mortgage-backed securities and the difficulty of acquiring real estate on long leases for sub-letting, as well as the onerous stamp duties levied on leases and property sales and purchases. The lack of adequate property valuation guidelines has also been cited as a problem and the Report recommends that AMFI should work with SEBI to produce guidelines to assist with the valuation of real estate portfolios. The Report also suggests that registered valuers valuing property for the purpose of REMFs should be approved by SEBI. SEBI is expected to approve the recommendations set out in the Working Plan and to amend the SEBI Regulations, although at this juncture no specific time-frame has been established.

This section on India has been prepared in consultation with Little & Co. If you have further questions as to matters of Indian law, please contact Mr R.K. Kulkarni on (91) 22 2265 2739 or by email at rkk@littlecompany.com or Meenal Kulkarni on (91) 22 2265 2739 or by email at meenal.kulkarni@littlecompany.com.

Malaysia

Overview

In the Malaysian context, Property Trust Funds are a class of unit trust schemes (as defined in the Securities Commission Act 1993) and are regulated by the Securities Commission, a body set up under the Securities Commission Act 1993 to regulate matters relating to securities and futures contracts and unit trust schemes. The guidelines on property trust funds issued by the Securities Commission in June 1995 were replaced by the new Guidelines on Property Trust Funds (the “Guidelines”) with effect from 13 November 2002.

Structuring a Property Trust Fund

A Property Trust Fund, in common with other unit trust schemes, has to be constituted by a trust deed and must have an approved trustee holding the assets of the Property Trust Fund which are managed by an approved management company (the “Manager”). The establishment of a Property Trust Fund, the Manager, its board of directors, the appointment of its chief executive officer and the trustee must be approved by the Securities Commission.

A Property Trust Fund may be listed on the Bursa Malaysia, which would require compliance with the listing requirements of the Bursa Malaysia applicable to listed Property Trust Funds. The Guidelines require that at least 25 per cent. of the units of a listed Property Trust Fund must be held by public shareholders (excluding the Manager, its directors, the merchant bank advising the Property Trust Fund and connected persons), provided that there is a minimum of 1,250 public shareholders holding not less than 1,000 units each. At initial launch the minimum size of a Property Trust Fund must be 100 million units.

The Guidelines do not clearly state whether Property Trust Funds may be open or closed-ended. Structures will be approved by the Securities Commission on a case-by-case basis.

Permissible Investments

A Property Trust Fund is permitted to invest in real property (which is defined to include rights, interests and benefits related to the ownership of real estate which meet certain requirements prescribed by the Guidelines), single-purpose companies (unlisted companies whose principal assets comprise real estate), real property-related assets, liquid assets, non-real property assets (each of which is specifically defined in the Guidelines) and asset-backed securities.

At least 70 per cent. of the total assets in the investment portfolio must be in real property, single-purpose companies or real property-related assets (with at least 50 per cent. of the total assets invested in real property or single-purpose companies (as described above)) and at least 20 per cent. of the total assets must be invested in liquid assets at all times.

A listed Property Trust Fund must invest at least 75 per cent. of its total assets in real property, single-purpose companies, real property-related assets or liquid assets (and at least 50 per cent. of its total assets must be invested in real property or single-purpose companies).

The Guidelines also limit holdings of “securities” (undefined in the Guidelines) by listed and unlisted Property Trust Funds of:

- any single issuer to 5 per cent. of the Property Trust Fund’s total assets;
- a group of companies to 10 per cent. of the Property Trust Fund’s total assets; and

– the same class of security issued to 10 per cent. of the Property Trust Fund's total assets.

Further, a Property Trust Fund must not be involved in granting loans or any other credit facilities, forward purchases or sales of any currency or money (except in instances where it has acquired or holds foreign properties, subject to exchange control regulations and certain conditions), and property development (except in instances where such development is viewed as a viable investment and specific criteria are met).

Mandatory Outsourcing of Operations and Conflicts of Interest

A Manager has to be appointed in respect of each Property Trust Fund to manage the investments of, and administer, the Property Trust Fund. The Manager must be a public company incorporated in Malaysia and must be a subsidiary of either (i) a financial services company; (ii) an investment holding company that has subsidiaries substantially involved in the financial services industry (by virtue of which the activities of the group of companies as a whole is substantially involved in the financial services industry); (iii) a property-development company; or (iv) a property investment holding company.

In addition, there must not be more than 30 per cent. foreign equity participation in the Manager. The Manager must also have net shareholders' funds unimpaired by losses of not less than RM1,000,000.

In addition to the Trustee and the Manager, a Property Trust Fund must make the following appointments:

– each trustee of a Property Trust Fund must appoint an independent approved company auditor for that Property Trust Fund;

– real properties held by a Property Trust Fund must be managed by a property management company appointed by the Manager; and

– valuations of real property must be conducted by an independent qualified valuer satisfying the criteria for independence set out in the Guidelines.

Related Party Transactions

The Guidelines do not generally allow property acquisitions from, or disposals of property to, a related corporation or an associated person ("related parties") of the Manager. However, a Property Trust Fund may acquire property from, or dispose of its property to, related parties if:

– a valuation of the property has been undertaken by an independent qualified valuer within six months of the proposed acquisition or disposal provided that (i) no circumstances have arisen after that valuation which would materially affect the valuation; (ii) the Securities Commission has not revised the valuation; and (iii) a valuation report is given to the trustee;

- the property is acquired at a price which is not more than the value in the valuation report or the property is disposed of at a price which represents not less than 90 per cent. of the valuation;
- the consent of the trustee has been obtained; and
- an announcement has been made by the Manager to the unitholders prior to acquisition or disposal.

Borrowing Limits

The Guidelines restrict the borrowings of the Property Trust Fund to 30 per cent. of its net asset value at the time of the borrowing. However, if approved by the trustee of the Property Trust Fund and the Securities Commission, that limit may be extended. Borrowings may be used for investment or redemption purposes and a Property Trust Fund may pledge its assets to secure such borrowings.

Taxation

Property Trust Funds are taxed as unit trusts and are liable to pay income tax in accordance with the provisions of the Income Tax Act 1967. Tax is paid at the Property Trust Fund level and income distribution from the Property Trust Fund will carry a tax credit in respect of the tax paid by the Property Trust Fund which unitholders (including non-Malaysian tax-resident unitholders) may utilise against the tax payable on the income distribution received from the Property Trust Fund. Where the investments represent shares in real property companies, profits from such investments will generally be subject to real property gains tax unless specifically exempted.

Currently, a Property Trust Fund, being a unit trust, is exempted from income tax on interest income earned from the following private debt securities:

- securities or bonds issued or guaranteed by the Government of Malaysia; or
- debentures, other than convertible loan stock, approved by the Securities Commission; or
- Bon Simpanan Malaysia issued by Bank Negara Malaysia.

The 2004 Malaysian Budget had proposed that:

- gains from disposal of real property by individuals or companies to Property Trust Funds be exempted from real property gains tax; and
- instruments of transfer of real property from individuals or companies to Property Trust Funds be exempted from stamp duty.

The above proposals in the 2004 Malaysian Budget are to be gazetted by way of a statutory order. However, to date, only the exemption of stamp duty on instruments of transfer of real property to a Property Trust Fund has been gazetted.

Property Trust Fund Offerings

There are presently four listed Property Trust Funds in Malaysia. They are (i) Amanah Harta Tanah PNB which is managed by Pelaburan Hartanah Nasional Bhd and was listed on 28 December 1990; (ii) First Malaysia Property Trust which is managed by Amanah Property Trust Managers and was listed on 23 November 1989; (iii) AmFirst Property Trust which is managed by AmProperty Trust Management Bhd and was listed on 28 September 1989; and (iv) Mayban Property Trust Fund One which is managed by Mayban Property Trust Management Bhd and was listed on 25 March 1997.

The Guidelines came into force on 13 November 2002. However, where compliance is not immediately possible, provision is made for an application to the Securities Commission within one month from 13 November 2002 for a transition period.

This section on Malaysia has been prepared in consultation with Shearn Delamore. If you have further questions as to matters of Malaysian law, please contact Christina S C Kow on (603) 2076 2009 or by email at christina@shearndelamore.com.

Taiwan

Overview

The Executive Yuan (Taiwan's Cabinet) announced on 13 December 2001 that it intended to draft a securitisation of real estate property bill (the "Securitisation Bill"). The Securitisation Bill was finalised in April 2002 and passed by the Legislative Yuan (Taiwan's Legislative) on 9 July 2003. The Real Estate Statute (the "Statute") took effect on 23 July 2003. The Statute permits the establishment of special purpose trusts ("SPTs") which are able to issue securities backed by underlying real estate assets.

The Statute follows the introduction of the Financial Assets Securitisation Statute (the "Securitisation Statute") which was passed by the Legislative Yuan on 21 June 2002 and adopted on 24 July 2002. The Securitisation Statute permits securities backed by underlying financial assets to be issued by special purpose companies and SPTs.

Structuring SPTs

The Statute permits two types of SPTs, namely the Real Estate Investment Trust ("REIT") and the Real Estate Assets Trust ("REAT"). The SPTs can be open-ended or closed-ended. Listing SPTs on the Taiwan Stock Exchange is optional under the Statute. REITs, based on the U.S. model, will enable SPTs to raise funds from investors and invest such funds in real estate and

real estate-related assets. Investors will receive in return beneficiary certificates representing beneficial interests in the trust assets.

REATs, based on the Japanese model, will enable SPTs to acquire real estate and real estate-related assets from their proprietary owners. REATs will issue beneficiary certificates to investors representing beneficial interests in the trust assets.

Permissible Investments

The investments which an SPT is permitted to make under the Statute include real estate (including real estate in the process of development), rights relating to real estate, such as mortgages, the securities of companies engaged in real estate activity and other investments permitted from time to time by the Ministry of Finance which is the competent authority in Taiwan.

Mandatory Outsourcing of Operations and Conflict of Interests

There are no provisions in the Statute requiring the asset management and administration functions of the SPT to be outsourced. The SPT should be managed by a trustee, although the Statute does not specify any minimum criteria as to the suitability or financial standing of entities acting as trustees.

Taxation

Income tax will be imposed on any dividends paid to investors who have purchased beneficiary certificates issued by the SPT. Foreign investors will be subject to withholding tax on dividends at a rate of 20 per cent. The SPT will also be subject to income tax on its net income. For SPTs investing in real estate, land and housing taxes will also be payable. Investors and SPTs will be exempt from securities transaction tax when trading beneficiary certificates.

This section on Taiwan has been prepared in consultation with Yang Ming Partners. If you have further questions as to matters of Taiwanese law, please contact Danny Liu on (886) 2 8725 6677 or by email at dannyliu@yangminglaw.com.

Singapore

Overview

Singapore Real Estate Property Funds ("Singapore Property Funds") are generally governed by Division 2 of Part XIII of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA") and the Code on Collective Investment Schemes (the "Code") and specifically governed by the guidelines relating to property funds set out in Appendix 2 of the Code (the

"Property Funds Guidelines"). Division 2 of Part XIII of the SFA and the Code came into effect on 1 July 2002.

The Property Funds Guidelines were first issued in May 2002 by the Monetary Authority of Singapore ("MAS") as part of the legislative and regulatory changes surrounding the proposed enactment of the SFA, resulting in a common set of guidelines that would apply to Singapore Property Funds, whether established as unit trusts or companies (see “Structuring Singapore Property Funds” below). The Property Funds Guidelines were subsequently amended on 29 August 2002, 28 March 2003 and 22 December 2003. Prior to this, separate guidelines governed Singapore Property Funds established as unit trusts and those that were established as companies.

Structuring Singapore Property Funds

Singapore Property Funds may take the form of a property fund established as a unit trust, otherwise popularly referred to as a Singapore Real Estate Investment Trust or “S-REIT”, or a company. The four Singapore Property Funds to date (see “Singapore Property Fund Offerings” below) have been constituted as unit trusts.

A Singapore Property Fund established as a unit trust will be constituted by a trust deed entered into by a manager and a trustee on behalf of holders of units in the unit trust (“unitholders”). The trustee must be a Singapore public company that is independent of the manager and has been approved by the MAS in accordance with certain prescribed criteria. The Singapore Property Fund must also appoint a manager to manage and administer the fund (see “Mandatory Outsourcing” below). A Singapore Property Fund established as a unit trust may or may not be listed on Singapore Exchange Securities Trading Limited (the "SGX-ST"). With a unit trust structure, investors purchase interests representing undivided interests in the property fund.

The Property Funds Guidelines provide that a Singapore Property Fund established as a company, whether listed or unlisted, must have a Board of Directors with at least two independent members and appoint a manager to manage and administer the fund (see “Mandatory Outsourcing” below). Such a Singapore Property Fund must be listed on SGX-ST unless the MAS is satisfied that there is a ready market for shares of a Singapore Property Fund established as a company. With a corporate structure, investors purchase interests similar to shares in ordinary companies.

Under the listing rules of the SGX-ST (which generally requires compliance with the Code of Corporate Governance submitted by the Singapore Corporate Governance Committee and accepted by the Singapore Government), at least one-third of the Board of Directors of the manager, in the case of a Singapore Property Fund established as a unit trust, or the company itself, in the case of a Singapore Property Fund established as a company, must comprise of independent directors.

Permissible Investments

Singapore Property Funds may, subject to certain restrictions on the investments and activities that they may undertake, invest in real estate; listed and unlisted debt securities and listed shares of, or issued by, property corporations, mortgage-backed securities, other property funds and assets incidental to the ownership of real estate (collectively known as "real estate-related assets"); listed or unlisted debt securities and listed shares of, or issued by, local or foreign non-property corporations; government and quasi-government securities; and cash and cash equivalents.

A Singapore Property Fund is subject to the following restrictions on the investments and activities that it may undertake:

- a Singapore Property Fund should invest at least 35 per cent. of its deposited property in real estate (being the value of the Singapore Property Fund's total assets based on the latest valuation);
- at least 70 per cent. of the Singapore Property Fund's deposited property should be invested, or proposed to be invested, in real estate and real estate-related assets;
- a Singapore Property Fund's investment in uncompleted non-residential developments in Singapore or uncompleted property developments outside Singapore may not exceed 20 per cent. of a Singapore Property Fund's deposited property. Of the 20 per cent. limit, not more than half may be invested in uncompleted property developments by a single developer; and
- in relation to investments in listed or unlisted debt securities and listed shares of or issued by property and non-property companies and other locally-registered/incorporated property funds, not more than five per cent. of the Singapore Property Fund's deposited property can be invested in any one issuer's securities or any one manager's funds.

In addition, Singapore Property Funds should not engage or participate in property development activities nor invest in unlisted property development companies and should also not invest in vacant land and mortgages, other than mortgage-backed securities.

Mandatory Outsourcing of Operations and Interested Party Transactions

Under the Property Funds Guidelines, Singapore Property Funds are required to have a manager who will manage and administer the property fund. The manager must (i) have at least five years of experience in managing property funds; or (ii) with the approval of the trustee of the Singapore Property Fund or the Board of Directors, as the case may be, appoint adviser(s) or employ persons who have at least five years of experience in investing in and/or advising on real estate.

Moreover, under the Listing Manual of the SGX-ST (the "Listing Manual"), the manager of the Singapore Property Fund must be reputable and have an established track record in managing investments. Generally, the manager must have been in operation for at least five years. In addition, the persons employed by the manager to manage the investments of the Singapore Property Fund must be reputable, must also have a track record of managing investments for a minimum of five years and must have satisfactory experience in managing funds of a similar nature.

The Property Funds Guidelines regulate, among other things, transactions entered into by an "interested party" relating to a Singapore Property Fund's acquisition of assets from or sale of assets to an "interested party", a Singapore Property Fund's investment in securities of or issued by an "interested party" and the engagement of an "interested party" as property management agent or marketing agent for a Singapore Property Fund's properties. Depending on the materiality of transactions entered into, the Property Funds Guidelines may require that an immediate announcement to the SGX-ST be made for public release for listed Singapore Property Funds and for unlisted Singapore Property Funds that announcements be made either through paid advertisements in at least one newspaper that is widely circulated in Singapore or by sending a circular to unitholders. The Property Funds Guidelines may also require that the approval of the unitholders be obtained. In addition, the Listing Manual regulates all "interested person transactions" (as defined in the Listing Manual) for Singapore Property Funds listed on the SGX-ST, including transactions governed by the Property Funds Guidelines.

Borrowing Limits

The Property Funds Guidelines restrict the borrowings of a Singapore Property Fund to 35 per cent. of its deposited property at the time the borrowing is incurred. A Singapore Property Fund may borrow more than 35 per cent. of its deposited property if (i) all the borrowings (including the new borrowings) of the Singapore Property Fund are rated at least A (including any sub-categories or gradations therein) by Fitch Inc., Moody's or Standard & Poor's taking into account the new borrowings, or (ii) the credit rating of the Singapore Property Fund is rated at least A (including any sub-categories or gradations therein) by Fitch Inc., Moody's or Standard & Poor's taking into account the new borrowings. Borrowings may be used for investment or redemption purposes subject to certain conditions, and a Singapore Property Fund may mortgage its assets to secure such borrowings.

Mandatory Prospectus Disclosure

The revisions to Property Funds Guidelines in March 2003 also made a number of amendments in the area of disclosure, requiring that the

prospectus must disclose the risks specific to investing in property funds. A non-exhaustive list of examples of such risks include:

– a lack of diversification in comparison to general securities funds;
– Singapore Property Funds tend to be more highly geared than general securities funds, which could pose risks if interest rates rise significantly;
– property valuations which affect the offer price of units in a Singapore Property Funds tend to be subjective; and
– underlying properties in a Singapore Property Fund are often illiquid making it difficult for these underlying properties to be sold if the need arises.

Taxation

Subject to a Singapore Property Fund which is established as a unit trust obtaining a tax transparency ruling from the Inland Revenue Authority of Singapore, generally Singapore Property Funds will be taxed as ordinary trusts or companies in accordance with normal tax principles. In the case of a unit trust, tax will be paid at the unit trust level and any tax paid can, subject to certain conditions, be passed on to unitholders as a tax credit when income from the Singapore Property Fund is distributed. In the case of a company, under the old tax regime, tax paid at the corporate level could be passed on to shareholders as a credit upon distribution of dividends. However with effect from 1 January 2003, the corporate tax system in Singapore was (subject to certain transitional rules) changed to a single-tier tax system whereby tax on a company will be a final tax and tax credits can no longer be passed on to shareholders.

In respect of gains realised on a sale of real properties of a Singapore Property Fund or on a disposal of units, while there is no capital gains tax in Singapore, such gains would be subject to income tax if they are considered to be trading gains.

There should be no stamp duty payable on transfers of shares or units in Singapore Property Funds where the transfers are effected on a scripless basis under the Central Depository (Pte) Ltd clearing system. However, if a transfer of shares in scrip form is effected by an instrument of transfer, stamp duty will be payable at the rate of 0.2 per cent. Stamp duty would also be payable on transfers of property into a Singapore Property Fund.

The Singapore Government announced in the 2004 Budget on 27 February 2004 that distributions from Singapore Property Funds that are authorised under Section 286 of the SFA (excluding distributions out of franked dividends) and paid to individuals will be exempted from tax. This tax exemption only applies to distributions made from taxable income of such Singapore Property Funds earned from 1 January 2004 and does not apply to distributions that are derived through a partnership or are considered as gains or profits from any trade, business or profession i.e. distributions

assessable to tax under Section 10(1)(a) of the Income Tax Act, Chapter 134 of Singapore. Following this announcement, and subject to the legislation enacting the tax exemption as announced, distributions made to individuals, irrespective of their nationality or tax residence status, who hold the units of such Singapore Property Funds as investment assets will be tax exempt. This is provided the units are not held through a partnership.

Singapore Property Fund Offerings

CapitaLand Limited launched CapitaMall Trust as the first successful Singapore Real Estate Investment Trust ("REIT") in July 2002. Linklaters Allen & Gledhill acted as international legal counsel and Allen & Gledhill acted as Singapore legal counsel to the offering and to CapitaLand Limited on this first international initial public offering of units.

In November 2002, Ascendas Real Estate Investment Trust, Singapore's second REIT, was successfully launched and listed on the SGX-ST, with Linklaters Allen & Gledhill advising on the offering as international legal counsel and Allen & Gledhill advising on the offering as domestic legal counsel.

In August 2003, Fortune Real Estate Investment Trust (sponsored by Hong Kong conglomerate Cheung Kong (Holdings) Limited), Singapore's third REIT and first REIT containing foreign assets, was successfully launched and listed, with Allen & Gledhill acting as Singapore legal counsel to the offering and to the manager of the REIT and Linklaters (Hong Kong) acting as Hong Kong legal counsel to the manager.

In May 2004, CapitaCommercial Trust, Singapore's fourth REIT and first REIT containing mainly commercial office properties, was successfully launched and listed. Units in CapitaCommercial Trust were distributed amongst the shareholders of CapitaLand Limited pursuant to a capital reduction and distribution *in specie* of CapitaLand Limited. Allen & Gledhill acted as legal counsel to the transaction, to the manager of the REIT and to CapitaLand Limited.

Hong Kong

Overview

The Securities and Futures Commission (the "SFC") published the Hong Kong Code on REITs (the "Code") on 30 July 2003. Prior to the enactment of the Code, the existing regulatory regime set out in the Hong Kong Code on Unit Trusts and Mutual Funds prohibited authorised funds from investing in any type of real estate. REITs ("HK-REITs") are now permissible in Hong Kong provided that they comply with the provisions of the Code.

Structuring HK-REITs

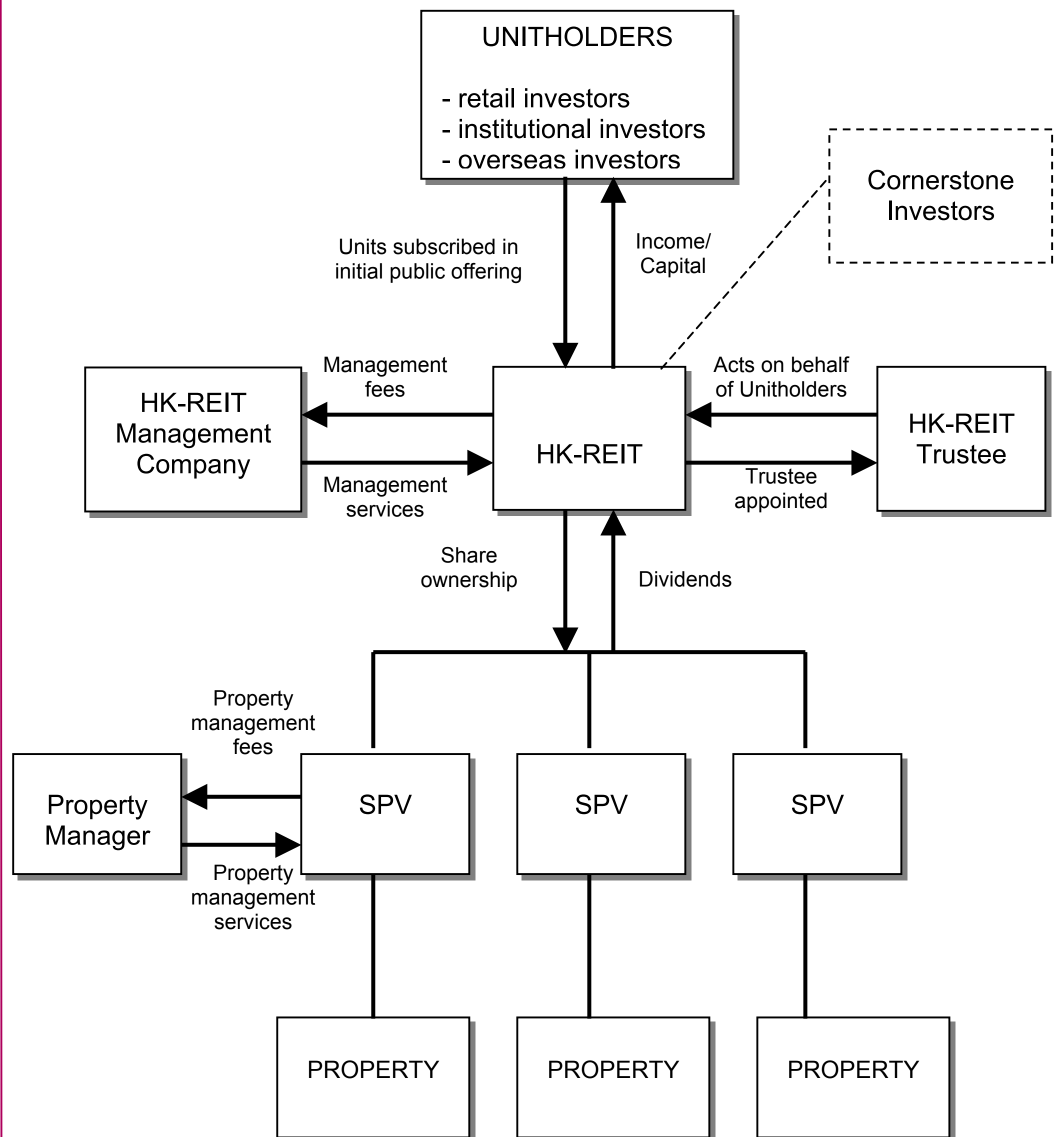
The Code permits HK-REITs to hold and acquire properties by two methods:

- direct ownership of real estate assets by the HK-REIT; and
- ownership of real estate assets through a special purpose vehicle.

The ability to structure HK-REITs using special purpose vehicles may result in stamp-duty savings if a significant portion of the real estate is currently already held through special purpose vehicles. In addition, it will enable HK-REITs to benefit from the same tax treatment as companies (see "Taxation" below).

Where the HK-REIT is structured so that it directly holds and acquires the real estate assets, the unitholders will subscribe for units in an initial public offering and receive income/capital from the HK-REIT in return. The management company, trustee and property manager (see "Mandatory Outsourcing of Operations and Conflict of Interests" below) will all be employed by the HK-REIT.

Where the HK-REIT is structured so that it holds and acquires real estate assets through special purpose vehicles, the unitholders will similarly subscribe for units in an initial public offering and receive from the HK-REIT income/capital in return. The management company and the trustee will be employed by the HK-REIT but the property manager will be employed by the special purpose vehicle(s). The shares in the special purpose vehicle(s) will be wholly-owned by the HK-REIT who will receive all dividends paid by the special purpose vehicle(s). HK-REITs which hold and acquire assets through special purpose vehicle(s) may be structured as set out in the diagram below.



The Code provides that HK-REITs may only hold real estate through special purpose vehicles if certain conditions are met, including:

- the special purpose vehicle is 100 per cent. legally and beneficially owned by the HK-REIT;
- there are no more than two layers of special purpose vehicles;
- the special purpose vehicles are incorporated in jurisdictions which have established laws and corporate governance standards equivalent to those of Hong Kong;
- the board of directors of each special purpose vehicle are appointed by the HK-REIT trustee; and

– both the HK-REIT and the special purpose vehicle(s) appoint the same auditors and adopt the same accounting principles and policies.

Permissible Investments

The Code contains a list of investment restrictions which include requirements that a HK-REIT shall:

– only invest in real estate located in Hong Kong;

– only invest in real estate which is generally income-generating (although the HK-REIT may hold non-income generating real estate which constitutes not more than 10 per cent. of its total net asset value);

– only invest in hotels, recreation parks or serviced apartments where such investments are held by special purpose vehicle(s);

– not invest in vacant land or engage in property development activities with the exception of refurbishment, retrofitting and renovation; and

– not acquire any asset which involves the assumption of any liability that is unlimited.

Mandatory Outsourcing of Operations and Conflict of Interests

In order to ensure a clear segregation of the HK-REIT's assets, the Code provides that the HK-REIT should be structured in the form of a trust. Accordingly, the HK-REIT must appoint a trustee that is functionally independent of the HK-REIT management company and acts in the best interests of the unitholders. The trustee must be:

– a bank licensed under Section 16 of the Hong Kong Banking Ordinance; or

– a trust company which is a subsidiary of such a bank; or

– a banking institution or trust company incorporated outside Hong Kong which is acceptable to the SFC.

Furthermore, the trustee must employ key personnel with the knowledge, organisational resources and experience relevant to holding real estate under HK-REITs or similar schemes or belong to a corporate group of good repute which has acted as trustees for REITs, or similar schemes, overseas and can provide the trustee with adequate support.

The management company of the HK-REIT must be licensed under Part V of the Securities and Futures Ordinance and approved by the SFC to manage the HK-REIT. The SFC will consider overseas REIT managers from acceptable jurisdictions in order to develop HK-REIT management expertise in Hong Kong. The management company must employ at least two responsible officers with a track record of at least five years in managing collective investment schemes. The management company may own or have an interest in the HK-REIT that it manages but it may not be paid in HK-REIT units.

The HK-REIT management company may perform property management services itself or may delegate this function to a professionally qualified property manager. The property management company must employ key personnel who are professionally qualified to manage real estate and who have at least five years of experience in managing real estate.

The Code contains provisions regulating connected person transactions and if the relevant transaction exceeds 5 per cent. of the latest net asset value of the HK-REIT, the Code requires that all connected party transactions be subject to prior approval by unitholders by way of an ordinary resolution at an EGM.

Borrowing Limits

The Code restricts the borrowing of a HK-REIT (either directly or through its special purpose vehicle(s)) to not more than 35 per cent. of the total gross asset value of the scheme. The HK-REIT may also pledge its assets to secure such borrowings and should disclose in its offering document its borrowing policy.

Taxation

While the Code is largely silent on the taxation treatment of HK-REITs, by allowing HK-REITs to hold and acquire real estate assets through special purpose vehicles, the SFC has made available potential taxation and stamp duty savings.

The potential stamp duty savings arise from the fact that a significant portion of real estate in Hong Kong is currently held through special purpose vehicles. Any transfer of such real estate from a special purpose vehicle to direct ownership by a HK-REIT would incur stamp duty of up to 3.75 per cent. However, if the HK-REIT is able to acquire shares in the special purpose vehicle itself, as opposed to acquiring the real estate itself, the stamp duty arising from the transfer of shares in the special purpose vehicle would amount to only 0.2 per cent.

From a taxation standpoint, there may be advantages if the HK-REIT holds the real estate through a special purpose vehicle. In such a structure, the HK-REIT may pay profits tax, reflecting the corporate structure, as opposed to property tax if the HK-REIT owned the real estate directly. The principal advantage of being subject to profits tax is that the HK-REIT may be able to deduct a number of expenses against its profits, including debt interest payments and management fees. Certain of these expenses are not deductible against property tax.

At the individual investor level, under existing tax rules in Hong Kong, there are no capital gains tax or dividend income tax payable by individuals.

Thailand

Overview

Thai law does not recognise the concept of trusts. Investment vehicles that resemble REITs, available in other jurisdictions, are mutual funds established specifically with the intention of investing in real property. In Thailand, a real estate mutual fund can be set up under the principal regulation of the Thai Securities and Exchange Commission ("SEC") that regulates real estate mutual funds.

Structuring a Real Estate Mutual Fund

Currently, the principal regulation applicable to the establishment of real estate mutual funds in Thailand is the SEC Regulation No. GorNor. 1/2545 (the "General Regulation"), which provides for the establishment of a closed-end mutual fund to invest a minimum of Baht 500 million in a specific piece of real estate, or certain prescribed types of real estate. The General Regulation requires that at least two-thirds of the units be offered and sold to at least 250 retail investors within one year of the establishment of the fund. In addition, where the fund acquires a particular holding of real estate which constitutes more than one-third of the net asset value of the fund, the General Regulation limits the number of units that can be subscribed by the person from whom the fund acquires such real estate to one-third of the total units. The units of the fund are required to be listed on the Stock Exchange of Thailand ("SET").

Apart from the establishment of the mutual fund under the General Regulation, a number of real estate mutual funds in Thailand have been established under SEC Regulation No. GorNor. 54/2543 ("Type IV Regulation") and predecessor regulations known as "Type I", "Type II" and "Type III". These Regulations were introduced in the period following the onset of the Asian financial crisis in 1997 as part of an attempt to boost the sagging property market and tackle problems affecting the country's ailing financial system at that time. However, the period allowed for applications for the establishment of new mutual funds under the Type IV Regulation and its predecessor regulations has now closed.

A mutual fund established under the Type IV Regulation is a closed-end fund with a minimum capital of Baht 500 million invested specifically in real estate and the rights of claim owned by distressed financial institutions. The units were required to be offered and sold to a minimum of 10 qualified institutional investors within six months of the establishment of the fund. The Type IV Regulation also contains rules similar to those described above limiting the holdings of units by investors from whom a fund acquires a substantial amount of its property. The units in Type IV funds can, but are not required to, be listed on the SET.

Permissible Investments

A fund established under the General Regulation may invest only in Thai real properties constructed before 20 October 1997 and other approved assets, including bonds and government treasury bills. Real estate investments must comprise of at least three-quarters of the fund's net asset value and at least 75 per cent. of the fund's income must be derived from real estate.

A fund established under the Type IV Regulation must invest at least three-quarters of its net asset value in Thai real properties and rights of claim within six months and may continue to make further investments in Thai real properties and rights of claims for three years after its launch. After this period, no such investments may be made. A fund may also invest in other authorised assets including bonds and treasury bills.

Mandatory Outsourcing of Operations and Conflict of Interests

Assets of both types of fund, whether established pursuant to the General Regulation or the Type IV Regulation, must be put into the custody of an SEC-approved fund supervisor and managed by an SEC licensed fund manager. Typically, commercial banks, finance companies, securities companies or insurance companies with the relevant licence from the SEC may act as fund supervisors or fund managers. The fund supervisor must (a) hold no more than five per cent. of the shares in the fund manager; (b) not share with the fund manager any shareholder who holds at least 10 per cent. of the shares in each of the fund supervisor and the fund manager; and (c) not share any director, manager or executive with the fund manager. A fund manager is prohibited from investing the capital of the fund in its shares or units of other funds of which it is also a manager.

Taxation

A mutual fund established pursuant to either the General Regulation or the Type IV Regulation is exempt from corporate income tax throughout its life. The Thai Revenue Code (the "Code") imposes corporate income tax on "a company or a registered partnership" as defined under Section 39 of the Code. Since a mutual fund is not regarded as a company or a registered partnership pursuant to the definition, it falls outside the definition of taxable entities under Section 39 of the Code. As the fund is the beneficial, as well as the legal owner of the assets, income of the fund is not deemed to be income of the unitholders unless and until there is a distribution of profits.

A mutual fund established under the SEC rules applicable to "standard" mutual funds (i.e. other than those established under the General Regulation, the Type IV Regulation, or predecessor regulations relating to Type I, Type II and Type III funds), is generally subject to value added tax ("VAT"), specific business tax ("SBT") and stamp duty, depending on the nature of the income and the transaction (for example, interest and discounts

are subject to SBT at a rate of 3.3 per cent.). However, there is a special exemption from VAT, SBT and stamp duty given to a mutual fund established pursuant to the General Regulation or the Type IV Regulation to attract foreign investments. In addition, such a fund is also entitled to a reduction of the standard property transfer registration fee.

Real Estate Fund Offerings

To date, two funds have been established under the General Regulation and fifty six funds have been established under the Type IV Regulation, with aggregate net asset values of approximately Baht 1,879 million and Baht 70,655 million, respectively.

Linklaters

Contacts

Please contact any of the following members of our Capital Markets Group at Linklaters if you would like to discuss anything in this article:

Bangkok
Thanathip Pichedvanichok
Tel: (66) 2305 8021
E-mail: thanathip.pichedvanichok@linklaters.com

Nick Thwaites
Tel: (66) 2305 8023
E-mail: nick.thwaites@linklaters.com

Hong Kong
Simon Davies
Tel: (852) 2842 4821
E-mail: simon.davies@linklaters.com

Dean Lockhart
Tel: (852) 2842 4141
E-mail: dean.lockhart@linklaters.com

Graham Turl
Tel: (852) 2842 4854
E-mail: graham.turl@linklaters.com

Christopher Stonehill
Tel: (852) 2842 4869
E-mail: christopher.stonehill@linklaters.com

Singapore*
Swain Roberts
Tel: (65) 6890 7388
E-mail: swain.roberts@linklaters.com

Kevin Wong
Tel: (65) 6890 7333
E-mail: kevin.wong@linklaters.com

Lucien Wong
Tel: (65) 6890 7702
E-mail: lucien.wong@allenandgledhill.com

Tokyo**
Mark Brown
Tel: (81-3) 3568 3813
E-mail: mark.brown@linklaters.com

David Deck (U.S. Law)
Tel: (81-3) 3568 3871
E-mail: david.deck@linklaters.com

Tony Grundy
Tel: (81-3) 3568 3827
E-mail: tony.grundy@linklaters.com

**In Singapore, Linklaters operates a joint law venture with Allen & Gledhill (Linklaters Allen & Gledhill) providing clients with legal advice on Singapore, English and U.S. law through a single entity.*

***In Tokyo, Linklaters practises English and U.S. law but not Japanese law. Should you have any questions which relate to Japanese law, Linklaters can refer you to Japanese qualified legal advisers.*

Editor: **Gabrielle Grieves**
Email: **gabrielle.grieves@linklaters.com**

This publication is intended merely to highlight issues and not to be comprehensive, nor to provide legal advice. Should you have any questions on issues reported here or on other areas of law, please contact one of your regular contacts at Linklaters, or contact the editors.

© Linklaters. All Rights reserved 2004

Please refer to www.linklaters.com/regulation for important information on the regulatory position of the firm.

We currently hold your contact details, which we use to send you newsletters such as this and for other marketing and business communications.

We use your contact details for our own internal purposes only. This information is available to our offices worldwide and to those of our associated firms.

If any of your details are incorrect or have recently changed, or if you no longer wish to receive this newsletter or other marketing communications, please let us know by emailing us at acmbulletin@linklaters.com

Bangkok
20th Floor Capital Tower All Seasons Place
87/1 Wireless Road Bangkok 10330
Tel: (66) 2305 8000
Fax: (66) 2305 8010

Beijing
25th Floor China World Tower 1
No 1 Jian Guo Men Wai Avenue
Beijing 100004 China
Tel: (86-10) 6505 8590
Fax: (86-10) 6505 8582

Hong Kong
10th Floor, Alexandra House
Chater Road
Hong Kong
Tel: (852) 2842 4888
Fax: (852) 2810 8133/2810 1695

Shanghai
28th Floor, HSBC Tower
101 Yin Cheng East Road
Pudong New Area
Shanghai 200120
People's Republic of China
Tel: (86-21) 6841 5858
Fax: (86-21) 6841 5656

Singapore
One Marina Boulevard #28-00
Singapore 018989
Tel: (65) 6890 7300
Fax: (65) 6890 7308

Tokyo
Akasaka 1-chome Center Building 12F
1-11-30 Akasaka
Minato-ku, Tokyo 107-0052
Tel: (81-3) 3568 3800
Fax: (81-3) 3568 3888

A03567268/1.0/25 Jun 2004