CONSULTATION PAPER ON PROPERTY TRUST FUNDS AND REAL ESTATE INVESTMENT TRUSTS

Issued By:

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Securities Commission

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CONTENTS

Section 1: Introduction and Overview

Background

On 25 October 1999, the SC, via a consultation paper known as a Consultation Paper on the Guidelines of Property Trust Funds, embarked upon a consultation process in relation to property trust funds (PTFs) vis-à-vis the likes of similar products in other jurisdictions, such as REITs in United States of America and property funds in Singapore. This consultation paper is available on the SC's website at www.sc.com.my. Whilst the results of the consultation process is pending, developments have since arose which has now led the SC to embark upon another consultation process in relation to PTFs and real estate investment trusts (REITs), which is targeted to discuss and tackle certain specific issues.

Issues

1.1 The purpose of this paper is to seek the public's response to certain identified issues and concerns, as well as to seek the public's perception and comments on the matters elaborated upon in Section 2 of the paper. The issues arising in this consultation process should not however be viewed in isolation from the areas consulted upon in the earlier consultation process, but as additional and related issues which has since come to the fore arising from policy developments and the Government's initiative to boost the economy, as well as revive the property market and property-related industries.

1.2 There are many aspects in which the existence of vehicles such as REITs can assist to address the economic situation in Malaysia. The existence of these investment vehicles can facilitate to reduce the exposure of the banking system to non-performing loans related to property-related lending, via the acquisition of such collateralised properties from financial institutions. Not least also is the role to be played by a REIT as a prospective "purchaser" of properties, which could serve to address and the property overhang situation in Malaysia. Based on a report by the Valuation and Property Services Department of the Ministry of Finance, the total value of property overhang by sector stood approximately at RM26.6 billion as at June 2001.

1.3 Apart from being instruments that can directly be utilised to revive the property market situation in Malaysia, pooled property investment vehicles such as REITs also provide for alternative financing mechanisms particularly in facilitating the corporate restructuring efforts of distressed public listed companies (PLCs). The Minister of Finance, in his budget speech for 2002, last October, advocated the establishment of REITs to facilitate corporate restructuring efforts. There are several ways in which REITs can contribute toward this end. The most obvious means is where REITs, like PTFs, can be used as a vehicle to invest in properties and property-related assets of distressed PLCs. The establishment of a corporate restructuring type of REIT can be undertaken, which would essentially be a vehicle which is devised for companies to dispose real estate for the purposes of corporate restructuring. Alternatively, property securitisation could be undertaken in order to generate consistent income-stream for the distressed PLCs, whilst at the same time, achieving the more macro objective of reviving the property market. In this way, the property assets of the PLC can be securitised in order for these asset-backed securities to form as investible instruments for which vehicles like PTFs and REITs can invest in. Another option to be explored is the possibility of the distressed PLC (which can satisfy certain criteria) being made to convert into a REIT (in a corporation form), thus eliminating the other aspects of the business of the PLC which is non/low income yielding and thus detrimental to the income-flow of the company.

1.4 Needless to say, corporate restructuring efforts of distressed PLCs vis-à-vis REITs would have many implications over the property trust industry in Malaysia. Further, the conversion of a distressed PLC into a REIT (in a corporation form), whether for a permanent or temporary period, would have a significant impact over the membership of the property trusts industry, in that it would result in other players partaking in the collective investment schemes industry, in addition to those involved in financial services. The views of the stakeholders of the property trust industry, namely the property trust management companies, towards this exercise are thus sought. Views are also sought on the feasibility of such an exercise, the interest shown towards such a route and other practical issues arising, from the property PLCs' and practitioners' perspective.

1.5 Related to the issue of corporate restructuring would also be the recurring issue of whether property development should be allowed as an activity for these REITs. The concerns over property development as an activity were deliberated on extensively in the earlier consultation process. The possible conversion of distressed PLCs involved in property development/management into REITs further begs the question as to whether such should be allowed in light of the same already being a core business activity of these companies.

1.6 Another issue, which is to be highlighted for discussion in this consultation process, is the issue of the tax treatment to be accorded in relation to PTFs and/or REITs. Investments in property-related collective investment schemes, which are accorded with appropriate tax-relief, could serve as an incentive to retail investors to invest in these instruments. In order to generate public interest in instruments which are made subject to specific tax policies relating to real estate (as the underlying assets are burdened with real property gains tax and stamp duties), the package must be preceded with tax-attractive relief/incentives to the end-investor. Only in this way would the instrument appeal to retail investors as a larger amount of the vehicle's distributable income (ex-the taxes) would be available for retained capital or distribution purposes. Having said this however, any incentives proposed to be accorded in relation to PTFs or REITs must take into consideration the resulting impact of the relief ultimately on the Government's tax revenue.

<u>Consultation Period:</u>

Parties wishing to comment on any issue raised in this Consultation Paper are requested to do so **in writing**. Comments should be addressed to:

Securities Commission
3 Persiaran Bukit Kiara
Bukit Kiara
50490 Kuala Lumpur
Attn: Trusts and Investment Management Department
Issues and Investment Division

and received by the SC on or before **18 March 2002**.

<u>Note:</u>

This Consultation Paper is purely for discussion and consultation purposes.

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Section 2: Policy Issues to be considered

The purpose of this Consultative Paper is to highlight a number of areas in the present Guidelines that is **proposed** for review.

2.1 Corporate Restructuring

2.1.1 To facilitate corporate restructuring efforts, particularly those undertaken by distressed PLCs, the SC envisages the following roles to be assumed by PTFs/REITs:-

(i) As a vehicle to acquire real property assets belonging to distressed PLCs/companies undertaking restructuring exercise. The acquisition exercise may also involve acquiring the shares of the distressed PLC;

(ii) As a vehicle to acquire securitised real property assets (in the form of mortgage backed securities or asset backed securities); and

(iii) The conversion of a distressed PLCs into a REIT set up.

2.1.2 Clause 4.3.1 of the Guidelines on Property Trust Funds stipulate the conditions that a to-be-acquired property must fulfill, namely being specifically identified, possess a good track record and/or good prospects of future net rental income of reasonable levels, and chosen from those which have been shown by studies to be competitive and located within good catchment areas. In view that a distressed PLC may possess real property assets that do not comply with the requirements of Clause 4.3.1, the allowance of existing PTFs facilitating a corporate restructuring exercise may be somewhat limited. On the other hand, this objective could transpire in the case of a REIT, which is established solely for the purpose of corporate restructuring with some form of flexibility granted in the profile of properties that the REIT can acquire. This form of REIT is also known as a Corporate Restructuring REIT (CR REIT), which is ultimately a vehicle devised for companies to dispose real estate for the purposes of corporate restructuring. Alternatively, a direct conversion by a distressed PLC into a REIT is also a possibility. Notwithstanding the quality of assets to be acquired or already inherent (in the case of a conversion) in the portfolio of the REIT, flexibility in terms of less-stringent requirements pertaining to the property can be imposed, provided that the risk is mitigated by the presence of substantial portion of regular income-generating assets.

2.1.3 In addition to a direct acquisition of real property assets owned by distressed PLCs, a more extensive approach would include allowing the acquisition of a stake in the equity of the distressed PLC. Clause 4.3.3 of the Guidelines on Property Trust Funds permit the acquisition of the equity of a company that owns property, provided that the following is satisfied:-

(i) The company to be acquired should be an unlisted company whose principal assets comprise real property ("single purpose companies);
(ii) The company should be wholly-acquired by the fund;
(iii) The fund should not assume any liabilities of the company it proposes to acquire;
(iv) The valuation of the acquiree company must be backed by the value of the property;
(v) There are valid commercial reasons for acquiring the company instead of the property; and
(vi) The acquisition is in the best interests of the unit holders.

Applying distressed PLCs into the equation could witness the following discrepancies; they are listed, their principal assets may not be real property, the non-absorption of their liabilities would require a compromise to be established with its creditor(s) and its valuation may not be backed by property-derived values. Hence, whilst PTFs are restrained from acquiring a distressed PLC, REITs may be used as an alternative. However, such a move will require REITs to assume a higher degree of risk and require larger amount of investible funds. Further, the "wholly acquire" condition would require further liberalisation in view of the huge paid-up capital of a listed company and the legal implications involved in the process (i.e. mandatory general offers).

2.1.4 The SC is also evaluating the feasibility of distressed PLCs securitising their real property assets via a special purpose vehicle. This option would see PTFs/REITs emerging as a potential investor in the securitised instrument.

2.1.5 On the issue of allowing distressed PLCs to convert into REITs as part of their corporate restructuring plan, thorough deliberation on this matter is required as this option may possibly be wrought with legal, practical and administrative impediments. Firstly, by virtue of its listed status, conversion/restructuring plans involving distressed PLCs would require obtaining the consensus of its shareholders and creditors, including processes allowing existing shareholders the option of opting-out from the investment. Next, not all distressed PLCs possess sufficient amount of quality real property assets to justify being converted into a REITs set-up. There is also the issue of possessing relevant expertise, particularly in areas pertaining to real estate and fund management (to cater for investments in equities). The move to secure such specific resources may also result in the termination of existing employees, particularly those whose services do not coincide with a REITs set-up. Lastly, a distressed PLC may already have in place other non-REIT related activities that will not complement a REITs set-up. For example, a distressed PLC may be involved in the services industry, which is deemed as incompatible with REITs' activities.

2.1.6 An ideal situation for conversion would require unanimous support from shareholders and creditors, and the distressed PLC originating from the properties industry or already owning a significant amount of real property, particularly in the case of an investment holding company. To further complement this foundation, the distressed PLC needs to source the relevant expertise and resources to manage its REITs activities and divest its non-related REITs activities. On the SC's part, further liberalisation of Clause 5.2 of the Guidelines on Property Trust Funds, which stipulate the qualifications of a management company, would be required as presently only subsidiaries of financial institutions (supervised by Bank Negara Malaysia) are permitted to be a management company of a PTF. Further liberalisation of the eligibility requirements to be a management company of a REIT would involve streamlining the requirements as per the Guidelines on Unit Trust Funds, where the eligibility to be a management company is extended to subsidiaries of investment holding companies that are substantially involved in the financial services industry. In view of the rigorous procedures and multiple expectations required in converting distressed PLCs into REITs, further deliberation into the technicalities involving this approach is required.

2.1.7 It is noted in South Korea the concept of corporate restructuring can be very much tax-driven, as in the case of Corporate Restructuring REITs (CR REITs). Details on the tax advantages obtained by CR REITs is explained further in the Taxation section of this paper. The essence of this approach involves using REITs as an acquirer of the assets belonging to companies undertaking corporate restructuring. Considering the difficulties arising from a conversion process, restricting corporate restructuring activities to this method may seem more feasible.

Views are thus sought on the following: –

- **Should corporate restructuring exercises facilitated by REITs be restricted to companies categorised as distressed PLCs only?**
- **Apart from the three options highlighted, are there other options for REITs to assist in facilitating corporate restructuring?**

If the conversion process is undertaken -

- **Should the conversion exercise be confined to distressed PLCs involved in the property sector, construction sector or investment holding companies (with substantial ownership in properties)?**
- **What should be the time frame allocated for the entity to divest its non-REITs related activities?**
- **Would a distressed PLC be required to change its listing status upon conversion?**

Acquisition of real property assets from distressed PLCs -

- **In the event low-quality assets are acquired from a distressed PLC, should there be a stipulated time frame for the assets to be “turned around”?**

Acquisition of securitised instruments -

- **Should investment limits on this investment type be further liberalised?**

Acquisition of equity of distressed PLCs -

- **Should the definition of “single purpose companies” be widened to include listed companies whose principal assets comprise real properties?**

2.2 Taxation

2.2.1 Under the present tax regime applicable, tax charges affecting PTFs can be separated into two categories, namely –

(i) Relating to the acquisitions/transfer/disposals of properties

- Real property gains tax (RPGT), whereupon rates between 5% to 30% (dependent on the year of disposal) are taxed on the chargeable gain arising from the disposal of real property; and
- Stamp duty, where rates of duty vary according to the nature of the instruments and transacted values.

(ii) Relating to the income of the corporation

- Corporate tax of 28%.

In addition to the above tax charges, dividends paid out by PTFs are subjected to the requirements of a tax imputation system. Based on this, shareholders receive pre-tax dividends and the tax credits can be used to offset against the recipient's taxable amount. The core feature of the tax imputation system is that it avoids double taxation of corporate profits.

2.2.2 In contrast, tax incentives accorded to PTFs comprise the following:-

(i) Exemption from income tax on gains from realization of investments, interest income from specified securities and deposits with licensed financial institutions;

(ii) Capital allowance on plant and machinery used in property-letting business;

(iii) Deduction of up to 25% on certain “permitted expenses” not normally deducted for income tax purposes; and

(iv) Distributions to unit holders out of exempt income are exempt from income tax.

2.2.3 The SC has received feedback requesting that the tax environment for PTFs be revisited, with emphasis placed on developing a tax-attractive environment for PTFs/REITs. In addressing this area, SC is presently evaluating existing tax charges and accorded incentives, coupled with comparison against other jurisdictional practices. In line with the introduction of REITs to complement PTFs, the United States (US) model takes center stage in the jurisdictional study.

2.2.4 Amongst the tax changes highlighted is the need for PTFs/REITs to be accorded a "tax transparent" status. Bearing linkage to the US model, it is noted that the success of the REITs industry there is synonymous with its “tax-transparent” status, where the income of the real estate investment trust is only taxed at the shareholders-level (upon receipt of dividends). This “flow-through” concept enhances the amount of income received by an investor/shareholder, in light of exemption from other forms of capital gains tax, which is eminent in other investment instruments in the US. However, to qualify for this “tax-transparent” status, REITs are required to disburse 90% (previously 95%) of its income/profits as dividends to its shareholders.

2.2.5 The high reliance placed on the “tax-transparent” status is also emulated in Canada and Australia. However, the lack of this incentive in Singapore when its Guidelines on Property Funds were released in 1999 was said to have affected the development of the industry. Nevertheless, criticisms on Singapore’s approach failed to incorporate the presence of its existing tax imputation system – where dividends are taxed at the PTF level (instead of the shareholders’ level) and recipients are allowed to claim a tax credit on the taxes paid. In essence, the difference in tax approach is in terms of the primary source responsible for paying the tax liability. Further, the role reversal (from shareholders to the property trust fund) does not result in double or additional tax charges incurred.

2.2.6 The situation in Malaysia is similar to Singapore where PTFs are not accorded "tax transparent" status due to the presence of the tax imputation system. In addition, the varying tax rates for personal and corporate tax can result in additional income, particularly for retail investors. For example, dividend/distributions paid by PTFs are taxed at a corporate rate of 28% and investors (retail and institutional) are entitled to claim tax credits from these dividends. In the case where the retail investor’s tax liability is less than the tax credit, he/she is entitled to a refund of the difference. In addition, the current tax incentive exempting dividends paid out of exempt income is already tax-free in nature. Hence, the requirement for a "tax transparent" status may not be essential.

2.2.7 In line with corporate restructuring, especially in the case of a distressed property PLCs converting into a REIT or disposing of its real property assets to a REIT, there have been suggestions that tax relief be granted to facilitate such cases. Based on the tax charges present, exemption from real property gains tax would provide the vendor higher proceeds or may even result in the negotiation of a lower disposal price. The approach proposed to be adopted here is similar to the South Korea experience, where Corporate Restructuring REITs (CR REITs) are accorded preferential tax treatment in comparison with its counterpart, the Ordinary REITS. It is noted that CR REITs are granted full exemptions from acquisition tax, registration tax and corporation tax. The disparity with Ordinary REITs is substantial, as in a 50% more tax exemption for all three tax components. Whilst, such a move has elevated demand for CR REITs, it has resulted in Ordinary REITs being deemed as unattractive. Relating to this, it should be noted that the benefits reaped from having in place differential tax treatments should not come at the expense of creating a substantial uneven playing field for the rest of the industry (namely PTFs).

2.2.8 Taking into consideration the mandated investment objectives of existing PTFs, the likelihood of them being used as corporate restructuring vehicles is restricted. Hence, the direct establishment of corporate restructuring-type REITs would seem the most viable alternative. Accordingly, additional tax incentives could be accorded to this CR-REITs, in view of its specific-purpose. For example, full/partial exemptions from RPGT would facilitate disposal activities undertaken with the view of corporate restructuring.

2.2.9 As highlighted earlier, three tax charges impact PTFs, namely RPGT, Stamp Duty and Corporate Tax. Ignoring existing incentives accorded, exemption (be it partially or fully) from all three tax components would ensure the presence of a bigger pool of income to be retained within the scheme or to be paid out as dividends. However, this tax advantage to PTFs/REITs comes at the expense of reduction in tax revenues to the Government.

2.2.10 In terms of tax incentives, apart from exempting dividends sourced from exempt income, existing incentives are focused on increased income derived from investments and capital deductions. The current state of the PTF industry serves as a testament towards the need for revival, vis-à-vis increasing the amount of participation. A proposal towards achieving this vision is tied to according tax deductions on amounts invested in PTFs/REITs.

Views are thus sought on the following -

- **Should tax relief granted be tied to a dividend payment requirement? If agreeable, what should be the level/amount of dividend required to be paid?**
- **In view of the existence of the tax imputation system, is there still a need to accord a "tax transparent" status to PTFs/REITs?**
- **Should different tax treatments (benefits and relief) be accorded amongst PTFs, REITs and CR-type REITS?**
- **Based on present tax incentives accorded to PTFs, are there any other tax incentives useful to develop a tax-attractive framework for PTFs/REITs?**
- **If exemption on tax charges is deemed necessary, should full or partial exemption be granted to PTFs, REITs and CR-type REITs?**
- **Exemption from tax charges and creation of new tax incentives would result in loss of tax-revenues for the Government, will the benefits arising outweigh the cost?**
- **Should investors be allowed to claim as a tax deduction, amounts invested on PTFs/REITs and CR-type REITs? If yes, should a maximum limit (i.e. RM5,000) be determined?**
- **Apart from the "corporate restructuring" angle, should different tax treatments be accorded for other reasons/objectives?**

2.3 Property Development

2.3.1 At present, PTFs are prohibited from being involved in property development except for transactions falling within the ambit of Clause 4.3.6 of the Guidelines. Under Clause 4.3.6, an agreement may be entered into at any stage in the development of the property to purchase the property upon its completion subject to the following criterion:

(i) only a listed property trust with a proven track record can enter into such arrangements and the returns from the fund's existing investments should be sufficient to tide over the construction period;

(ii) the purchase agreement should be subject to the completion of the building with proper cover for construction risks. The fund must be able to withdraw from the agreement at minimal cost if the transaction is no longer in the interests of unit holders;

(iii) the development/construction of the property must be on terms which are competitive and not unfavourable to the fund; and

(iv) the prospects of the property upon completion can be reasonably expected to be favourable.

2.3.2 In other jurisdictions such as property trust funds in Australia these entities are permitted to invest in properties being developed, but not undertake property development activities per se. Similarly, property funds in Singapore are prohibited from engaging or participating in property development activities, whether on its own, in a joint venture with others or by investing in unlisted property development companies. In the US however, there are no restrictions imposed for REITs to invest or engage in property development activities.

2.3.3 In view that PTFs are prohibited from engaging in property development activities, the same stance would most likely be extended to REITs as well. Whilst the establishment of REITs is synonymous with corporate restructuring, its presence as a publicly available collective investment scheme warrants the need to ensure that it does not unjustifiably increase its risk profile. Generally, property development activities are deemed as high risk in view of its long payback/gestation periods, difficulties in securing tenants and the requirement of securing the right (i.e. property development) expertise. A flipside to the argument however, would be that a higher risk profile could translate to higher returns and if adequate disclosures are made to potential investors, REITs could be allowed to engage in property development activities.

Views are thus sought on the following:-

- **If distressed PLCs are permitted to convert into REITs, there is a possibility that some of them may originate from the property-development business or possess abandoned projects. Should they be allowed to continue their property development activities, vis-à-vis requiring the REIT to engage in property development activities?**

- **As completing abandoned projects can be deemed as a corporate restructuring task, apart from directly engaging in property development activities, are there any other methods for PTFs/REITs to assist in this area?**

2.4 Management and Structure

2.4.1 At present, PTFs can be established in a listed or unlisted form, where the participants involved in the running of the scheme's operations are confined to the management company, the trustee and the property management company. In the case of the management company, the following requirements (as per Clauses 5.2 and 5.3 of the Guidelines on Property Trust Funds) are to be complied:-

(i) It should be incorporated in Malaysia;

(ii) It should not be a property development company or a subsidiary of such a company;

(iii) It should be linked to a financial institution supervised by Bank Negara Malaysia and shall initially be a subsidiary of such a financial institution, which would have the option to divest part of its shareholding in the future;

(iv) It should have shareholders' funds of at least RM1 million unimpaired by losses;

(v) It should have at least 30% Bumiputera ownership. In addition, its foreign ownership shall not exceed 30%; and

(vi) At least one member of the board of directors should be an independent member.

2.4.2 In comparison, the US-REITs framework (as dictated by the Internal Revenue Code provisions) stipulates the following:-

(i) REITs can be structured as a corporation, business trust or similar association;

(ii) It must be managed by a board of directors or trustees;

(iii) The board must be independent of management; and

(iv) It must possess a minimum of 100 shareholders, of which no more than 50% of the shares can be held by five or fewer individuals during the last half of each taxable year.

2.4.3 With respect to the eligibility requirements to be a management company of a PTF, the SC is presently revisiting the requirement that it must be a subsidiary of a financial institution. A possible route of liberalisation would involve expanding this requirement to allow participants whom are subsidiaries of an investment holding company whose subsidiaries are substantially involved in the financial services industry. The possible move is in line with the requirements presently imposed on unit trust management companies. However, in the case of REITs the eligibility requirements for its participants may require further liberalisation, in view of its role in facilitating corporate restructuring activities. The possibility of distressed PLCs' involvement, be it directly (via a conversion) or indirectly (via the disposal-cum-property management of real property assets) is imminent, requiring further evaluation of the merits of widening such participation.

2.4.4 Cognisant of the pressing emphasis on facilitating corporate restructuring, it is proposed that distressed PLCs (wanting to convert into REITs) be restricted to managing only Corporate Restructuring-type of REITs. Elaborating on this approach would see distressed PLCs conducting the following:-

(i) Converting its operations into a management company of a REIT; or

(ii) Disposing its real property assets to a REIT, managed by an independent party, and holding a stake in the REIT.

The REIT can be in a listed or unlisted form. However, if it is unlisted, it must be in the form of a PTF in order to enable it to cater for redemptions. Additionally, the requirement to have in place proper expertise and a larger independent composition for its board is deemed necessary, in view of the vested interest at stake.

2.4.5 Relating to allowing distressed PLCs becoming management companies is the issue of possessing adequate shareholders' funds, i.e. unimpaired by losses of RM1 million. In view of its already "distressed" situation, it is highly unlikely that the PLC will be able to fulfill this requirement. Apart from ensuring that the distressed PLC is of financially sound position to conduct its functions, another issue of concern is the fear that the funds invested by investors are diverted from its actual purpose. A possible way of mitigating this would involve the appointment of a custodian/trustee to safeguard the assets of the REIT. However the shareholders funds' requirement may still remain as an uphill task considering the long overdue financial-state of the distressed PLC.

Views are thus sought on the following:-

- **What is the view and implication of deeming distressed PLCs eligible as management companies of REITs?**
- **Should the management companies (and its delegates) of REITs be required to possess certain qualifications (i.e. real estate management) relating to REITs?**
- **Should the conversion into REITs be restricted to Distressed PLCs originating from certain business backgrounds (i.e. property development, construction, etc) ?**
- **From a corporate restructuring standpoint, are there any other alternatives for Distressed PLCs to participate in REITs/PTFs?**
- **In the case of a REIT managed by a distressed PLC, should a regular dividend repayment be made compulsory, in view of the vested interest at stake? Are there any other controls required to put in check these vested interests?**
- **In view that distressed PLCs are not able to conform with the minimum shareholders funds' requirement, should they be granted a full exemption on this requirement or should other controls be effected?**

2.5 Distribution Practices

2.5.1 At present, dividends declared by PTFs are made at the discretion of the management company. Hence, the declaration of dividends is not compulsory and if declared, the dividends paid out are not on a consistent scale.

2.5.2 This is unlike the scenario in the US, where REITs are required by tax laws to pay out (as dividends) at least 90% of its income to its shareholders, in order to enjoy tax breaks (particularly the "tax transparent" status). On a related note, despite the high dividend yield (i.e. between 6% - 10% per annum) offered by

REITs, in comparison to other investment instruments (i.e. bonds, preferred stocks and utilities), shareholders may not received impressive gains in terms of net wealth, as REITs are mostly traded on the open market - hence, its capital value is not reflected by its actual net asset value but by market forces instead. For example, a 10% dividend income obtained may be eroded by a 10% fall in the market value of the REITs, resulting in little/no effect to an investor's net wealth.

2.5.3 As dividend payout is an issue that has always been left to the management company's prerogative, the 90% dividend requirement rule need not be made compulsory for PTFs/REITs. Furthermore, the management company (and its delegate(s), being the party(ies) responsible for the investment/real estate management of the scheme, should be given a free hand in determining the investment plans for the scheme and not be restricted by a specified dividend payment target unless specified in its objectives. Further, the requirement to consistently declare dividends is not flawless, as the following issues arise: -

(i) The high dividends payout comes at the expense of retained earnings, thus restricting the fund from sourcing new investment opportunities with internally generated funds. Applying this to the Malaysian context, the situation is further compounded by gearing restrictions as stipulated in the Guidelines on Property Trust Funds. Hence, investments in new properties that costs substantially may not be possible, in view of the shortage of retained earnings and the prohibition on maintaining a high gearing ratio; and

(ii) High dividend payouts do not translate to an increase in net wealth for investors. Whilst the fund pays out a high dividend its actual net asset value reduces proportionately. The impact may not be evident in the case of listed PTFs/REITs (as they are traded based on demand and supply) but is clearly reflective in the case of open-ended/unlisted PTFs/REITs. This situation is similar to the emphasis on distribution for unit trust funds, which ignores the fact that it does not increase the net wealth of its unit holders unless its fund's trading values are pegged.

2.5.4 On the contrary, if the objective of the PTF/REIT is to provide regular dividend payments, resulting in investment decisions being fine-tuned to cater for this requirement, then under such circumstances it would be legally right for the scheme to comply with a regular dividend payout requirement.

Views are thus sought on the following:-

- **Should PTFs/REITs be required to consistently declare distributions?**
- **Should tax relief/incentives be restricted to PTFs/REITs that declare distributions?**
- **In the case of a Distressed PLC converting into REITs, how would a requirement to consistently declare distributions be consistent with its need to conserve funds, particularly during the initial years ?**