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What are REITs & what role can the Isle of Man play?

By Carolyn Gelling, Head of Isle of Man Office, The International Stock Exchange Group

A Real Estate Investment Trust (REIT) is a company that owns, and in most cases operates, income-producing real estate. REITs own many types of commercial real estate, ranging from office and apartment buildings to warehouses, hospitals, shopping centres, hotels and agricultural land.

History

REITs have been around for some time. They were created in the United States in 1960 and since then, more than 35 countries around the world have established REIT regimes.

The legislation laying out the rules for REITs in the United Kingdom came into effect in January 2007. Significant changes to the UK REIT regime in 2012 and smaller changes in 2013 and 2014, have continued to enhance the attractiveness of the UK's REIT regime for property company holdings and investors.

Why REITs?

REIT status affords a number of commercial and tax benefits, including access to the Global REIT brand which is known and accepted by investors and analysts worldwide. This can attract international capital where specific investment pools are designated for investment into REITs and REIT conversion can therefore often unlock new sources of funding.

> *"The number of UK REITs has risen to around 70 and more than a quarter of these are listed on TISE."*

REITs are attractive to investors for several reasons including easier access to property investment, improved liquidity, greater diversification, lower costs and potentially enhanced return. REITs provide property exposure without purchasing a property directly and can seek investment in areas of the property sector that private investors cannot usually access. Indirect investment into property through REITs is generally more liquid than traditional investment into 'bricks and mortar' and REITs can provide diversification across a range of property assets, as well as a generally more regular and stable income stream.

In terms of cost, investment through a REIT involves lower transaction costs, i.e. up to 0.5% stamp duty on shares compared to up to 5% stamp duty land tax on commercial property. In terms of return, after-tax returns for shareholders may be improved as profits are generally only taxed at the shareholder level, REITs are exempt from corporation tax on rental income and capital gains and there is a tax rebasing of the properties used for the rental business to market value on entry to the REIT regime.

The rise of REITs

A series of factors have come together in the past few years to drive up interest in UK real estate as an asset class, including a low interest rate environment and currency changes post-Brexit vote, as well as investment in REITs as a vehicle for that investment. The number of UK REITs has risen to around 70 and more than a quarter of these are listed on The International Stock Exchange (TISE).

Why TISE?

The UK REIT regime requires that a vehicle is admitted to trading on a recognised stock exchange and either 'listed' on such an exchange, or 'traded' on such an exchange in every accounting period. TISE is deemed a recognised stock exchange and listing venue by HMRC under section 1005 of the Income Tax Act (2007). It is this same recognition which also enables investment into TISE-listed products by Self-Invested Personal Pensions (SIPPs) and Individual Savings Accounts (ISAs).

"TISE's Listing Rules specifically exempt REITs from the free-float rule."

Similar to the UK REIT regime itself, TISE's Listing Rules specifically exempt REITs from the free-float rule requiring 25% of the issued share capital to be held in public hands. This has proved particularly attractive for those REITs where there are a smaller number of increasingly international institutional investors and especially, where they are likely to hold for the long term and therefore do not require significant levels of liquidity. Having said that, there has been a recent trend towards TISE also proving attractive to more widely held REITs, such as 'club' deals of high net worth individuals and retail offerings.

Why Isle of Man?

While UK REITs must be tax resident in the UK, they can be and often are incorporated in other jurisdictions. Using Isle of Man incorporated companies to avail of the UK REIT regime has some advantages. These include company law enabling, for example, distributions to be made on a solvency test basis, there being no stamp duty payable on the transfer of shares and the recognition of protected and incorporated cell companies, which may be useful for ring-fencing REIT assets and liabilities within underlying subsidiaries. The Isle of Man is also part of the VAT Union with the UK, which would be relevant for REITs that are registered for VAT purposes.

The Isle of Man has a long standing reputation for its expertise in administering and advising upon real estate assets for international clients. This, coupled with access to TISE for listings, as well as the island's abundance of expertise across professional services firms to help facilitate and support a listing, means that REITs now present another offering upon which the Isle of Man can promote itself on the international stage.

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