

**"Study on Amending the Securities Investment Trust and  
Consulting Act to Allow REIT to Adopt the Fund Structure  
(Draft)"  
Consultation Paper**

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## **I. Background Information**

- (I) On July 23, 2003, Taiwan announced the implementation of the "Clauses of the Real Estate Securitization Act" and introduced the Real Estate Investment Trusts (REIT) system. REIT issued under the Regulations mainly adopt the "trust type" investment structure, with the trustee (trust enterprise) as the issuing entity. In practice, the real estate management and operation functions are entrusted to the real estate management organization, and the trustee will make the final decision.
- (II) However, the growth of Taiwan's REIT market has stagnated in recent years. In order to revitalize Taiwan's real estate securitization market, the FSC has revised the "Securities Investment Trust and Consulting Act" (hereinafter referred to as the SITE & SICE Act) with reference to the real estate investment trust systems in Japan, Singapore and Hong Kong, and studied the adoption of the fund structure for REIT issuance, with the plan to allow "real estate investment trust enterprises" (hereinafter referred to as REIT enterprises) to issue REIT in parallel with the current trust structure REIT. Under the dual-track system, market participants can choose to issue REIT through the fund structure or the trust structure in the future to make the operation structure more flexible.
- (III) The biggest difference between the fund structure and the trust-structure REIT is that the trust enterprise manages the trust-structure REIT, and then entrusted to appoint a real estate management institution (such as a construction management company) to provide investment advice. In the future, the fund structure REIT of Taiwan will be issued and managed by REIT enterprises, which should have the specialty of real estate investment management. There is no need to appoint another real estate management agency to provide investment advice.
- (IV) The Ministry of Finance and other government agencies were contacted on September 26, 2020 to provide their opinions on this case. A public hearing was held on October 6, 2020 to listen to external opinions. The 60 day advance notice period of laws and regulations was handled on January 20, 2021, and the expiration

date of the advance notice was March 22, 2021. In addition to the opinion of the Ministry of Finance on tax benefits, other government agencies and public hearing participants generally agreed with the direction of the fund structure REIT planning.

## **II. Items for Consultation at Public Hearing**

### **Topic 1: Qualification for the establishment of a “REIT enterprise”**

Description:

(I) **Description of the current situation:** According to Article 4 of the Real Estate Securitization Act, a trustee institution refers to an institution that can be entrusted with the management and disposal of trust assets and the offering or private placement of beneficiary securities, and is limited to the trust enterprise referred to in the Trust Enterprise Act. It shall have been established for more than three years and have at least a certain level of credit rating by a credit rating institution approved by the competent authority. In addition, in accordance with Article 3 of the Standards for the Establishment of Trust Enterprises, a minimum paid-in capital of NT\$2 billion is required to apply for the establishment of a trust enterprise. Still, the minimum paid-in capital required of a trust enterprise only handling real estate investment trust business is NT\$1 billion. In addition, the professional promoters of trust enterprises shall be banks, insurance companies or fund management institutions with certain qualifications, and the total number of shares subscribed shall not be less than 40% of the paid-in capital.

(II) **Description of promotional measures:**

1. **The minimum paid-in capital of a REIT enterprise is proposed to be NT\$200 million:**

(1) At present, the minimum paid-in capital of a securities investment trust enterprise (hereinafter referred to as a SITE) is NT\$300 million. Unlike a securities investment trust fund which has diversified investment objects, the investment objects of REIT are real estate or real estate related rights, the number of REIT issued and managed by the same REIT enterprise is small, and the management fee rate is lower than that of a

securities investment trust fund. Moreover, under the current trust structure, the minimum paid-in capital required of a real estate management institution is only NT\$50 million.

(2) Referring to the situations in Hong Kong, Singapore and Japan, the thresholds for the establishment of REIT management organizations are not high; for example, HKD5 million for Hong Kong, SGD1 million for Singapore and JPY50 million for Japan. Among them, in Hong Kong, the capital requirement for a general mutual fund manager is HKD10 million, while the capital requirement for a REIT manager is only HKD5 million.

2. **Specialized REIT enterprises are required to have investment from professional shareholders:** REIT enterprises are professional real estate management organizations, and the business shall be participated in by professional shareholders with professional knowledge, experience and skills in real estate investment. It is proposed that the professional shareholders of REIT enterprises shall have real estate investment management experience and be approved by the FSC. The total number of shares they subscribe to shall not be less than 50% of the shares issued for the first time.
3. **It is proposed to allow SITEs to concurrently operate the REIT business:** REIT enterprises are engaged in the investment management business of REIT funds, while SITEs are engaged in the investment management business of securities investment trust funds. Considering that the nature of both of their businesses is investment management, and the issuance and management of REIT in other countries is handled by fund companies with asset management licenses that have a similar nature to that of SITEs, it is proposed to allow SITEs which meet certain qualifications to concurrently operate the REIT business.

(III) **Comments of Participants:**

1. As the amount of investment in the real estate market is huge, it is suggested that REIT enterprises should follow the

trust enterprises and set a minimum paid-in capital of NT\$1 billion.

2. The NT\$200 million minimum paid-in capital for REIT enterprises is too high, and is inconsistent with the foreign situation. It is recommended to set it at NT\$30 million, and limit each management organization to manage only one REIT.
3. The purpose of the minimum paid-in capital requirement is to protect investors. If the paid-in capital set for the REIT enterprise is too low, there may be a risk that they are unable to bear the legal responsibility involved. Although the capital requirement of Singapore REIT management institutions is not high, Singapore requires REIT management institutions to purchase insurance policies to reduce legal risks. The minimum paid-in capital of NT\$200 million may be high if each management institution only manages one REIT, but too low if it may manage multiple REITs.
4. Other countries' low paid-in capital requirement should be due to their domestic conditions, but it is more persuasive to set a higher paid-in capital when revising the law. In addition, it is suggested that tax benefits for REIT (such as the benefits on the land price tax, income tax and asset transfer tax generated by merger) should be given to facilitate the development of the REIT market.
5. Chartered enterprises need a certain amount of capital support. There is professional liability insurance in foreign countries, but such insurance is not available in Taiwan. Although the NT\$1 billion paid-in capital requirement for REIT enterprises is high, the capital requirement still needs to be higher than that in foreign countries, because there is no special insurance in Taiwan.
6. Insurance companies hold a large number of real estate objects. Insurance companies can activate the real estate securitization market if they can act as professional shareholders of REIT enterprises.
7. The real estate of a fund structure REIT is registered in the name of the custodian, and too much responsibility is placed

on the custodian.

8. The custodian will sign a contract with the REIT management institution. If the custodian institution has doubts about the operation and management mode of the management institution, it will first clarify with the management institution, and there should not be the problem of too much responsibility on the custodian.
9. REITs do not have a legal personality, so it will be difficult to register the property rights of REIT loans. The reason why Japanese REITs are companies is to solve this problem.
10. Funds always had no legal personality, and current trust-structure REITs do not have legal personality either, so there should be no problem in registering the property rights of REIT loans. Singapore REIT loans are mainly based on the qualification of the sponsor behind the REIT, so the qualifications of professional shareholders are the key to the success of REIT.

**(IV) Initial response of the Bureau:**

1. It is understood that although the capital of REIT management institutions in Japan, Singapore and Hong Kong is only about NT\$20 million, such management institutions in these countries are only allowed to manage one REIT. In the future, for Taiwan's fund structure REIT it is planned not to limit the number of REIT under management, so a higher paid-in capital will be set.
2. As REIT enterprises are chartered businesses, they still need a certain amount of capital support to protect the rights and interests of the investing public. As for the minimum capital requirement of REIT enterprises, the Bureau will refer to the participants' opinions when developing detailed regulations such as the conditions for the establishment of REIT enterprises in the future.
3. Considering that the setting of qualifications for professional shareholders by business type (such as requiring the professional shareholders of REIT to be real estate developers or life insurance companies) will make other enterprises with real estate investment management experience unable to issue and manage REIT, in order to

make REIT issuance management more flexible, the option of not limiting the professional shareholders of REIT by business type, but reviewing whether the shareholders have real estate management ability, experience and track records when they send in application documents may be considered.

## **Topic 2: Proposal to allow fund structure REIT to conduct related party transactions and relevant supporting measures**

Description:

### **(I) Description of the current situation:**

1. Although trust-structure REITs do not prohibit the REIT and the real estate management institution from being related parties, the REIT sponsor and the trustee (trust enterprise) shall not be related parties. In addition, according to subparagraph 2, paragraph 1, Article 25 of the Trust Enterprise Act, a trust enterprise shall not purchase its own or its related parties' property with the trust assets.
2. After visiting Japan and Singapore, it is found that the sponsors of foreign REITs are the key to the success or failure of REIT. Most of them are developers who are the main participants and real estate providers of REIT, and most of them are related parties with REIT management organizations; in addition, most of them will provide preemptive rights (if the sponsor wants to sell an object of a similar type as the REIT's property, it will first ask the REIT for its purchase intention) and income support (such as assisting the REIT to achieve the projected rate of return or converting the income from unstable objects into a stable source of interest distribution) to REIT.

### **(II) Description of promotional measures:**

1. **It is proposed to allow fund structure REIT to conduct related-party transactions:** After referring to the foreign model of allowing REIT to conduct related-party transactions, it is proposed to allow REIT enterprises to use REIT assets to acquire or sell real estate or real estate related rights from or to the professional shareholders of the REIT enterprise.
2. **Ensure that fund structure REIT obtain the preemptive right and income support:** It is proposed that when reviewing the public offering or private placement cases of fund structure REIT in the future, the REIT enterprises are required to obtain the commitment of the real estate sellers to provide the preemptive right and income support to the



REIT.

3. **Strengthening investment decision-making procedures and information disclosure:** In order to prevent conflicts of interest in related-party transactions, it is proposed to supplement relevant supporting management measures, including strengthening investment decision-making procedures (requiring that related-party transactions be approved by the audit committee composed of independent directors of the REIT enterprise, and the resolution of the beneficiaries' meeting be obtained if the related-party transaction price is above a certain ratio), strengthen information disclosure, and strengthening the responsibilities of the owner of the REIT property or the REIT's real estate related rights as well as the responsibilities of professional appraisers such as real estate appraisers.

(III) **Comments of participants:**

1. Restrictions on related-party transactions can be relaxed, but there should have supporting measures and attention needs to be paid to the transfer of interests. In addition, related-party transactions have the problem of transfer pricing; whether a transfer pricing report is required for any real estate transaction regardless of the amount is to be considered.
2. If the professional shareholders are not developers, are income support and preemptive right still required of them? It is suggested that income support and preemptive rights not be included in the requirements.
3. There are mechanisms such as preemptive rights and income support, which will help the growth of the REIT scale, but the application of relevant mechanisms should still be clearly defined. For example, for targets that cannot be surely acquired even with the preemptive right, the preemptive right shall apply only when no one offers a better price.
4. The preemptive right has a time limit. It is suggested that the review process of REIT IPO and supplementary offering be more efficient.

5. Is it necessary to provide REIT income support? It is hoped to have a clear definition of income support. If income support cannot be fulfilled, is it easy to cause disputes?

(IV) **Initial response of the Bureau:**

1. The main purpose of requiring REIT to provide the preemptive right and income support is to ensure that REITs have a sustainable growth plan and maintain a stable revenue. For example, Singapore requires REIT to have the preemptive right and income support when reviewing REIT applications. Japan also requires REIT to put forward a growth strategy plan when reviewing REIT applications.
2. This section involves detailed regulations for REIT application review, and the external parties believe that there should be specific requirements to follow. The Bureau will take into account foreign regulations and external opinions when developing detailed regulations in the future.

### **Topic 3: independent director and audit committee requirement for REIT**

Description:

- (I) **Description of the current situation:** According to the Trust Enterprise Act, a trust enterprise is not allowed to purchase the property of itself or its related parties with trust assets for a trust-structure REIT, nor is the trustee (trust enterprise) required to set up independent directors or an audit committee.
- (II) **Description of promotional measures:**
  - 1. **REIT enterprises are required to set up independent directors and an audit committee:** In line with the opening of related-party transactions to fund structure REIT, with reference to Article 136 of the Insurance Act, it is proposed to require REIT (including specialized and concurrently operated) to set up independent directors. The number of independent directors should account for more than 1/3 of all directors but not less than 3; major proposals such as related-party transactions shall be reviewed by the audit committee composed of independent directors and then submitted to the board meeting for resolution.
  - 2. **Regulations on the functions and powers of independent directors and the audit committee:** For the relevant regulations on the independent directors and audit committee of REIT enterprises, it is proposed to refer to the Regulations Governing Appointment of Independent Directors and Compliance Matters for Public Companies and the Regulations Governing the Exercise of Powers by Audit Committees of Public Companies, and appropriate professional requirements for the independent directors or audit committee of the REIT enterprise need to be formulated as necessary (for example, requiring that at least one independent director of the REIT enterprise shall have passed the national examination of real estate appraisers, and have a certificate and more than 5 years of working experience in real estate appraisal practice).
- (III) **Comments of participants:**
  - 1. It is suggested that the qualification of independent directors of REIT enterprises be changed to have more than 10 years

of experience in real estate appraisal. In addition, other than the appraisal report, it is suggested that there should be a review mechanism for real estate appraisal.

2. It is suggested to relax the shareholding restriction on REIT sponsors to allow them to give financial support to REIT.
3. I support the establishment of independent directors, but it is suggested that independent directors should not be required to qualify as real estate appraiser; the appraisal should return to the market mechanism and the professionalism of appraisal should be respected. In addition, I do not support the establishment of an audit committee, and REIT investment should also return to the market mechanism. For example, currently, the opinion of the Tourism Bureau, Ministry of Transportation and Communications needs to be obtained to establish a tourist hotel, which will only prolong the review time and be detrimental to the development of REIT.
4. The purpose of improving corporate governance is to prevent fraud. The supporting measures for related-party transactions are mostly to monitor through information disclosure and independent third-party supervision, so I support the establishment of independent directors. I have no opinion on whether independent directors need to have the appraiser qualification; their independence and professional qualification can be standardized for the REIT industry, but the management organization should still have the appraisal expertise.
5. It is necessary for independent directors to have the appraiser qualification. The value is the core of the investment process, and independent directors can assist in assessing whether the investment income can be achieved. In addition, it is suggested that independent directors should have at least 8 to 10 years of practical experience in real estate appraisal.

(IV) **Initial response of the Bureau:** There is no objection from the external parties in this section, but only slightly different views on the qualification requirement of independent directors (for example, whether independent directors should have the

qualification of real estate appraiser). The Bureau will take into account external opinions when developing detailed regulations for the qualifications of independent directors of REIT enterprises in the future.

#### **Topic 4: Proposal to standardize the investment principles and core nature for fund structure REIT**

Description:

- (I) **Description of the current situation:** According to the order of the Ministry of Finance referenced Tai-Tsai-Rong (IV) No. 0924000790 on September 2, 2003, the total amount of a REIT fund's investment in cash (including bank deposits), government bonds and investment targets in items 1 to 3, paragraph 1, Article 17 of the Clauses of the Real Estate Securitization Act shall not be less than 75% of the net asset value of the fund. In addition, in accordance with Article 12 of the Regulations Governing the Public Offering or Private Placement of REIT and REAT Beneficiary Securities by a Trustees, the annual interest distribution ratio of a trust structure REIT shall be more than 90% of the distributable income.
- (II) **Description of promotional measures:** A REIT mainly raises funds from investors based on the income generated by real estate. Although the scope and principle of the investment objects of a fund structure REIT are the same as that of a trust-structure REIT, which mainly include real estate, real estate related rights and real estate related securities. Considering the core nature of a REIT is to obtain a stable source of income by investing in real estate or real estate related rights, it is proposed to have the core nature of the fund structure REIT stipulated in the Securities Investment Trust and Consulting Act that at least a certain ratio (e.g. 75%) should be invested in real estate or real estate related rights with stable income. The annual distribution income should reach a certain ratio (e.g. 90%) of the distributable income. In addition, as the fund structure REIT is based on the principle of sustainable operation, in order to avoid liquidation and delisting in the short term after the establishment of REIT, it is proposed to require the REIT enterprise to put forward a REIT related business plan and financial plan during the application review process, so as to ensure that the REIT can obtain stable income within at least a certain period (e.g. 5 years) and sustainable operation in the future.
- (III) **Comments of participants:**
  - 1. The distributable income of the trust structure REIT now

includes capital gains from the disposal of real estate, which is different from the international practice. It is suggested that the income from the disposal of real estate can be retained for 1 to 5 years for REIT reinvestment.

2. The purpose of asset disposal is to buy better assets. If the disposal proceeds must be distributed, the distributed income of the year the real estate is disposed of will be greatly increased, which may mislead investor expectations.
3. There must be a certain standard for distributable income, and compulsory distribution will reduce management flexibility. The distributed income of Hong Kong REIT is not necessarily cash, but may be income certificates (similar to stock dividends). It is suggested to handle income distribution in a similar way.
4. Foreign countries require more than 90% of the income to be distributed due to tax considerations. It is suggested to refer to the treatment of REIT capital gains in the United States, Japan and other countries.
5. REIT must be able to expand their scales for sustainable operation. It is suggested to distribute beneficiary units instead of cash for income distribution, and capital gains can be retained and reinvested to be conducive to the sustainable operation of REIT.

(IV) **Initial response of the Bureau:** Regarding whether capital gains from the disposal of real estate can be retained and not distributed, and whether the distribution of beneficiary units is allowed for income distribution in this section, the Bureau will take into account foreign practices and external opinions when developing detailed regulations in the future.

## **Topic 5: Proposal to adopt a single upper limit of the borrowing ratio of fund structure REIT, with the limit temporarily set at 40%**

Description:

- (I) **Description of the current situation:** The trustee of a trust structure REIT may borrow money with the trust assets in accordance with the agreements of the REIT trust deed, and the upper limit of the borrowing ratio is the upper limit of borrowing differentiation set according to the REIT's credit rating. In accordance with Article 11 of the Regulations Governing the Public Offering or Private Placement of REIT and REAT Beneficiary Securities by a Trustee, the trustee shall comply with the following provisions when borrowing funds with the trust assets of the REIT fund:
1. Where the REIT is rated grade 1 by at least two credit rating agencies listed in the attached table, the total amount of borrowing shall not exceed 50 percent of the total amount of trust assets.
  2. Where the REIT is rated grade 2 by at least one credit rating agency listed in the attached table, the total amount of borrowing shall not exceed 35 percent of the total amount of trust assets.
  3. Where the REIT is rated grade 3 by at least one credit rating agency listed in the attached table, the total amount of borrowing shall not exceed 25 percent of the total amount of trust assets.
  4. Where the REIT's credit rating is below the grades provided in the attached table or the REIT is not rated, the total amount of borrowing shall not exceed 15 percent of the total amount of trust assets.
- (II) **Description of promotional measures:** After investigation, the upper limit of the borrowing ratio applicable to most trust structure REIT according to the credit rating results is 35%. After consulting the REIT analyst of Taiwan Ratings, although the borrowing ratio is only one of the factors considered for credit rating, the increase of a REIT's borrowing amount will increase its debt ratio. This will indeed affect the financial soundness and reduce the rating of the REIT. Industry



practitioners also reflected the fear that credit rating downgrade will make their borrowing exceed the limit, and their borrowing methods tend to be conservative. It is proposed to refer to the regulations in foreign countries (Hong Kong and Singapore adopt a single borrowing ratio of 45%) as well as taking into account the current loan status and financial risks of REIT, and apply a single borrowing ratio and set the upper limit of the borrowing ratio at 40%.

- (III) **Comments of participants:** The purpose of REIT borrowing is suggested to be moderately relaxed (for example, permitting real estate related securities investment). In addition, the maximum borrowing ratio of the current trust structure REIT is 50%. If a single upper limit of 40% is adopted for the borrowing of the fund structure REIT, it seems to be a downward adjustment, and it is suggested to adopt a single upper limit of 50%.
- (IV) **Initial response of the Bureau:** The proposal to raise the upper limit of the borrowing ratio to 50% involves the formulation of REIT sub-regulations. When formulating REIT management measures in the future, the Bureau will take into account the regulations of Japan, Singapore and Hong Kong as well as external opinions.