



全國工商聯房地產商會
China Real Estate Chamber of Commerce

香港分會有限公司
Hong Kong Chapter Limited

February 26, 2014

The Securities and Futures Commission
35/F Cheung Kong Center
2 Queen's Road Central
Hong Kong

Dear Sir

Re: Consultation Paper on Amendments to the Code on Real Estate Investment Trusts

China Real Estate Chamber of Commerce Hong Kong Chapter Limited (hereinafter called "CRECCHK") was established on August 21, 2002 as a non-profit making Hong Kong-registered Chapter of the China Real Estate Chamber of Commerce (hereafter called "CRECC"). CRECC currently has more than 4,500 members across the mainland China. CRECCHK has over 160 members including real estate developers/investors, real estate funds, REIT Managers, commercial banks, development management companies, surveying firms, planning consultants, architectural firms, investment banks and private equity funds and other professional services. Most of our members are active and influential players in the real estate industry across Asia. To know more about our Chapter, please visit our web site www.crecchk.hk for details.

We refer to your Consultation Paper on Amendments to the Code on Real Estate Investment Trusts, we would like to submit our comments on the seven questions raised in the Consultation Paper. Please withhold our submission from publication.

Question 1: Do you consider that flexibility in respect of property development investments and related activities should be introduced for REITs?

Comments: We agreed flexibility would be a very good thing for the future competitiveness of the sector and related activities are desirable in order to build a more suitable and cost effective portfolio for REITs. While we welcome the property development flexibilities, REIT investors do understand that recurrent income generation is one of REITs' fundamental characteristics as an investment vehicle.

We are open to the idea of outsourcing. For large REITs with a pool of qualified development professionals, outsourcing does not seem absolutely necessary. By contrast, for smaller REITs, we suggest outsourcing of the development related functions to independent professional firms with relevant expertise. It is envisaged that such way of external management may help reduce risk exposure for the REITs and to lessen the temptation of REIT Manager into continuously looking for development projects as part of its core business or competence.

As far as "expertise" is concerned, Hong Kong has well qualified professionals with development experience. Some of the existing REITs in the territory have senior employees with experience in managing development projects.

Question 2: Do you consider that the 10% GAV Cap is set as an appropriate threshold?

Comments: We understand that in the United States, REITs are allowed to own, operate, manage and develop real estate for its own portfolio without any threshold restriction. If it develops real estate for third parties, the resulting income is a) disqualified for an income tax that requires "at least 95% of gross income of a REIT must be from real estate and passive sources" and b) the disposal is subject to disposal gain tax.

In Australia, REITs are allowed to develop properties through the form of stapled-securities. In Singapore, the total contract value of property development activities and investments in uncompleted property developments should not exceed 10% of the REIT's deposited property.

Taking into account the above comparable overseas regimes, and balancing the concerns as mentioned in Question 1 above, we consider that an initial 10% GAV Cap is appropriate for now. We consider that if the development function is outsourced to independent third parties instead of internally managed, 15% of GAV Cap can be applied.

In the longer term, to facilitate the development of the local REITs market, Hong Kong may consider further relaxing the threshold to be more in line with the United States and Australia. REIT investors should enjoy tax benefits. This will bolster further market growth.

Question 3: Do you have any comments on how the Property Development Costs should be calculated?

Comments: It is proposed that Property Development Costs would be the total project costs borne and to be borne, inclusive of the costs for the acquisition of land (if any) and

the development or construction costs of the project. We consider that financing costs should be excluded from the calculation of the total project costs.

Question 4: Do you have any comments on the frequency of periodic updates that should be provided to unitholders on the status of property development investments and related activities?

Comments: We agree with the proposal of providing periodic updates to investors about the status of property development investments and related activities half-yearly in the interim and annual reports of REITs.

Question 5: What additional safeguards do you consider appropriate to ensure there will not be any material change to overall risk profile of a REIT despite the flexibility to engage in a limited extent of property development investments and related activities?

Comments: We consider the suggested 10-15% GAV threshold, and regular reporting are adequate safeguards. Further, under the listing rules, acquisitions may be subject to unitholders' approval, depending on the size of the deals. As REITs are required to distribute at least 90% of their distributable income, they normally do not hold a significant amount of cash. For material acquisitions, unitholders' approval will be necessary. In this sense, a REIT is more or less protected against taking unwarranted development risks. Hence trustees will be consulted.

Question 6: Do you have any comments on the proposed scope of the Relevant investment and the proposed Maximum Cap?

Comments: We agree that allowing REITs a broader range of investment options could potentially enhance returns to unitholders, especially in times of limited suitable property investment opportunities.

In Australia, REITs are required to invest in real estate that generates real estate income but no specific requirements are stipulated for the ratio of real estate owned to the overall portfolio.

In the United States, for example, 75% of an REIT's assets must be composed of real estate (including mortgages), government securities or cash items. In other words, the United States has a relatively more liberal approach than the proposal under the Consultation Paper as cash items is not treated as outside the "scope".

As cash items are traditionally viewed as "risk-free" (as long as they are deposited in

jurisdictions with investment grade or above credit rating), we believe that they could be excluded from the above 25% Maximum Cap under the proposal.

In particular, we consider that large REITs would benefit most from investment in property development in such proposed changes. This is because they would have more investment options than smaller REITs. Larger REITs are also more likely to leverage on their existing resources and expertise to invest in property development for future business growth. The gross asset values of most of Hong Kong-listed REITs are small and the cap on property-development spending would limit their options available, especially in developed markets where opportunities for longer-term revenue growth are available.

Question 7: What other safeguards do you consider appropriate to be put in place corresponding to the proposal to allow for the Relevant Investments?

Comments: We believe that the current proposal has adequate safeguards.

In conclusion, our Chapter agreed the amendment would advance the development of Hong Kong's REIT market, as the current regulations on Hong Kong's REITs are generally stricter than those in the rest of Asia. In addition, we have some further points, as follows:

1. CRECCHK, being a well-represented industry chamber of commerce in the real estate industry, would like to see the REIT market in Hong Kong to develop further and be able to attract more companies in the Asia Pacific Region to choose REIT listing in Hong Kong. Hong Kong REIT market needs to grow in scale and trading volume to attract global long-term fund and reinforce its leading position of capital formation centre. We reckon that long term capital, versus short term speculative fund, will favor stability and long term development of the securities and real estate markets of Hong Kong. Thus, we welcome any new initiatives from SFCives in increasing flexibilities for REIT so that REIT Manager can better manage and grow the portfolio while investor's interest is safeguarded.
2. We would also like to see more cross-border REITs, especially those from Mainland China to be listed in Hong Kong as it is one of the cities having the most competitive tax system reliable legal regime and dynamic capital market in the region.
3. For the Investment Options, REIT should not be allowed to invest in relatively high-risk products such as financial derivatives. Also it would be much better if there would be clearer definitions what SFC allows REIT managers to invest and not to for investment options.

Should you require more information, please do not hesitate to contact the undersigned