



SECURITIES AND  
FUTURES COMMISSION  
證券及期貨事務監察委員會

**Consultation Conclusions on  
The Draft Code on Real Estate Investment Trusts  
《房地產投資信託基金守則》  
草擬本的諮詢總結**

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## Executive Summary

1. The Securities and Futures Commission (“SFC”) issued a Consultation Paper on the draft Code on Real Estate Investment Trusts (“REITs”) on 7 March 2003 for an initial period of 4 weeks. The consultation period was extended by two weeks in response to requests from market participants and industry practitioners that they be given more time to analyse the draft Code. The consultation ended on 23 April 2003.
2. A total of 52 submissions were received, representing comments from a diverse group of professionals, including investment bankers, fund managers, lawyers, property managers/developers, surveyors and accountants. The submissions are currently posted on SFC’s website [www.hksfc.org.hk](http://www.hksfc.org.hk). A list of respondents is set out in Annex 1.
3. Respondents to the public consultation support the SFC’s initiative to introduce a set of guidelines to facilitate the offering of REITs to retail investors in Hong Kong. Comments have generally focused on issues regarding fund structure, the mode of management, investment restrictions, borrowing limit, valuation and dividend policy. The SFC has carefully considered the comments and suggestions in respect of these issues, and conducted follow-up meetings with market practitioners to better understand their concerns and to explore alternatives that would facilitate market development without compromising investor protection.
4. The SFC has concluded that many of the regulatory restrictions in the draft Code can be revised to allow more flexibility in the development of the REIT market, provided that REIT managers provide full disclosure, appropriate structural safeguards are in place, and a complementary investor education program is launched by the SFC. The SFC agrees to adopt the following major revisions to the draft Code:
  - (a) allow REITs to hold real estate through wholly-owned special purpose vehicles;
  - (b) allow the management company to choose between having internal or external management for the REIT;
  - (c) increase the borrowing limit of a REIT to 35% of the value of gross assets;
  - (d) allow investments in hotels and recreation parks;
  - (e) remove the limit on cash holdings;
  - (f) reduce the dividend payout ratio to 90% of net income after tax;
  - (g) reduce the valuation frequency of a REIT to an annual basis; and
  - (h) provide measures to ensure good corporate governance and give holders the right to vote on important matters.
5. However, at this early stage, the SFC will retain the requirement that SFC-authorized REITs should only invest in real estate in Hong Kong. This focused approach should help facilitate better understanding of this new product by retail investors. Depending on the development of the REIT market, the SFC takes the view that this geographical restriction need not be in place indefinitely. Therefore, the SFC undertakes to set up a task force after the

implementation of the Code on REITs (“Code”) to examine the minimum benchmarks that REITs should set for themselves should they invest in overseas properties. The public will also be consulted specifically on this issue.

6. The SFC has decided that all REITs should be listed on the Stock Exchange of Hong Kong (“the Exchange”) having taken into account that the majority of respondents have indicated a preference for REITs to be listed. Listing REITs will also provide investors an exit mechanism without creating an excessive burden on the management of the real estate, given that property is generally considered an illiquid asset. Bearing in mind the differences between the investment features of a REIT and a listed property company, the SFC intends to promote good corporate governance principles for listed REITs by implementing rules that are appropriate for these types of investment vehicles. Towards this end, the SFC has included the Code requirements concerning the real time disclosure by independent financial advisers to unit holders on matters that require their approval.
7. The text of the Code is set out in Annex 2.
8. The SFC will closely monitor the development of REITs including the issues encountered in the implementation of the Code. The SFC will review the Code as and when required. The SFC also intends to seek approval by the Legislative Council to increase the application and authorisation fees for REITs.
9. The SFC extends its appreciation to all respondents who have provided their views on the proposals in the Consultation Paper on the draft Code.

## **Regulatory Philosophy**

10. The SFC believes that it is important, at the outset, to clearly explain the purpose of introducing REITs to the retail market. This will help the market and the investing public understand the SFC's policy decisions that underlie the regulations contained in the Code and the regulatory approach that the SFC adopts.

## ***Primary Objective***

11. The primary objective in authorising REITs to be offered to the investing public is to give retail investors in Hong Kong an additional product choice. In order to distinguish itself from investments in listed property companies, a REIT should be able to provide attractive investment features that are not readily available to investors of listed property companies. The SFC believes that a REIT should be transparently held and run with structural safeguards for its assets, have a clear and focused investment objective (holding of real estate for recurring income over a long term), distribute to investors a stated percentage of its net income after tax (though the dividend income itself cannot be guaranteed), and have good corporate governance.
12. In order to achieve these regulatory aims, the SFC has prepared a new and separate set of regulations and guidelines in the form of the new Code, specifically to regulate REITs in Hong Kong. The SFC is well aware that any new investment product being introduced for the first time to the Hong Kong market requires a period of gestation and familiarisation by all parties including the regulator. Therefore, the SFC intends to maintain as much flexibility as possible by keeping the Code under review to build a regulatory framework for REITs that encourages best practice and overall fairness for all parties concerned.

## ***REIT – Hybrid Product***

13. It should be made clear that a REIT is a *hybrid* product that combines the characteristics of a listed company and the activities of a collective investment scheme. The structure of a REIT is modelled after that of an investment fund. Thus, the regulatory rules governing a REIT would have to cater to *both* the listed company and fund activity aspects of a REIT.

## ***Regulatory Principles***

14. Based on the premise above, the SFC believes that the Code should incorporate the following principles to ensure adequate investor protection:
  - proper management experience and expertise;
  - ongoing supervision and regular monitoring by the management company of the activities of its delegates (if any);

- clear description of the scheme's investment policy and objective(s);
  - segregation of management and the safekeeping of assets;
  - appropriate valuation methodology and frequency;
  - adequate financial reporting;
  - transparent and efficient exit mechanism;
  - timely disclosure of material information pertaining to the scheme;
  - all transactions are conducted on an arm's length basis and in the best interest of unit holders;
  - proper voting rights for unit holders on key issues relating to the interests of a REIT; and
  - fair and equitable treatment of all unit holders.
15. The fundamental requirement is that a REIT should engage in dedicated investments in real estate that generate recurrent rental income, with an aim to distribute a significant portion of its net income after tax to unit holders in the form of regular dividends.

### ***Distinction between REITs and Listed Property Companies***

16. Based on these principles, there should be a clear distinction between investing in listed property companies and in REITs. A listed property company relies on the ability of its management team to effectively mobilize its resources to enhance the capital return to its investors. The company's management also has the discretion to venture into activities unrelated to property investments. On the other hand, a REIT relies *solely* on the ability of the management company to generate a stable source of recurrent income from the properties under management for distribution to investors. To this end, the management company should strive to maintain a portfolio of quality rental properties and at the same time adopt a rental strategy for its properties in order to deliver a steady stream of dividend income to investors.
17. The bottom line is that the management company of the REIT cannot deviate from its core activity of investing in real estate. By comparison, when an investor buys shares in a listed property company, he effectively chooses to put his trust in the company's management to pursue business and growth prospects, which may or may not be focused on real estate. When an investor buys units in a REIT, he effectively chooses to buy a right to interests in or benefits from the real estate that the REIT owns and manages.

### ***Types of Investment Risk***

18. However, investments in REITs, like investments in listed property companies, are subject to the same risks that underlie property investments, e.g., property market cycles, interest rate cycles, economic prospects and political outlook. Moreover, while a REIT is required under the Code to distribute not less than 90% of its annual net income after tax, the amount of that income may fluctuate. Operating losses or a negative revaluation of a REIT will adversely affect the income of the REIT. In addition, units in a REIT may trade at a value above or

below its issue price, or the net asset value of the REIT. Given that REITs are a new product to the market, investors should therefore carefully consider the types of investment products that best suit their investment goals, understand the risks involved in each type of product and if in doubt, always consult professional advisers before making their investment decisions.

## **Summary of Comments Received**

19. Most respondents requested changes to the regulatory provisions governing REIT operations and investments to ensure that fund managers are given sufficient flexibility to develop REITs as a product. The main areas to be reviewed are geographical exposure, gearing ratio, types of real estate, and cash level.
20. Some of the submissions also provided useful analysis, based on overseas experience, on how a REIT would most likely operate in Hong Kong, and thus recommended that the manager of a REIT should be allowed to choose between having internal or external management for the REIT, subject to the expertise of the manager.
21. Respondents also suggested that, since REITs that are authorised under the Code are likely to be listed on the Exchange, REITs should be allowed to be competitively structured vis-à-vis listed companies, and should be subject to a regulatory and disclosure regime broadly similar to that for listed property companies.

## **Consultation Responses to Specific Issues**

### ***Fund Structure***

22. *Public Comments:* Respondents generally supported the SFC's recommendation for a trust structure. However, they suggested that REITs be allowed to take on a corporate form for tax reasons. Most respondents also argued that REITs should not be required to directly hold real estate, as doing so would render REITs liable to property tax. If REITs were allowed to invest through special purpose vehicles ("SPVs"), as do listed companies, then REITs would pay profits tax via the SPVs. Respondents noted that the deductions allowed for profits tax are more generous than those for property tax. The use of SPVs could also facilitate property transactions, ring fence liabilities and alleviate concerns over stamp duty. Some respondents also proposed preferential treatment, such as reduction or total exemption of stamp duty.
23. *SFC's Response:* The SFC considers that the trust structure is the preferred form, as it ensures that the trustee will provide a layer of oversight. Given that a REIT will invest in real estate in Hong Kong, the trust should be established in Hong Kong. The SFC understands the tax implications of a trust structure and has, therefore, amended the Code to allow a REIT to hold real estate through special purpose vehicles, which may be domiciled overseas. Such a structure will

enhance the operational flexibility of a REIT, allowing it to be competitively structured vis-à-vis listed companies, and to adopt an efficient tax strategy.

24. As the Code now allows REITs to hold properties through SPVs, there is a need to ensure a high degree of transparency concerning REIT activities. As such, the SFC requires that there shall be no more than two layers of SPVs and all such SPVs should be 100% owned by a REIT. An SPV holding property must do so directly, but it may co-own a property with a third party, provided that the SPV holds majority interest and control. Moreover, while the Code allows a REIT the flexibility of co-owning a piece of real estate property, the Code requires that the general principles for protecting the assets and interests of unit holders need to be upheld and reflected at various levels of operations within the REIT. Therefore, the management company has the responsibility to ensure that any transactions or activities conducted by the SPVs comply with all relevant Code requirements. Furthermore, the trustee of a REIT is responsible for the appointment of the board of directors of all SPVs.

### ***Management of REITs***

25. *Public Comments:* Comments by respondents focused mainly on two aspects, namely how a REIT should be managed and the licensing of the management company.

- (a) Management of a REIT: The majority of respondents suggested that the management company should be allowed the option of internally managing a REIT, or delegating certain functions to third parties. Respondents took the view that the Code should not mandate delegation or the type of management activities to be contracted out. Furthermore, respondents considered that the qualifications of the key personnel of the management company, rather than the track record of the company itself, is more important to the proper management of a REIT. Suggestions were also made stating that experience with public fund management is not important in the context of REIT management.

However, opinions varied regarding the qualification requirements of the key personnel responsible for property management. Some respondents considered that the property manager should not be subject to the stringent qualification requirements proposed in the draft Code, while others recommended that the key personnel of the property manager should have a longer history of relevant experience, instead of the proposed five years, given the duration of a typical property cycle.

- (b) Licensing of the management company: Respondents requested clarification on the type of licence that the management company should seek from the SFC.

- (c) Others comments:
  - (i) The management company should be allowed to invest in the REIT that it manages.
  - (ii) The management company, rather than the trustee, should be responsible for arranging insurance coverage for the real estate of the scheme, as the extent of insurance coverage is a commercial decision to be undertaken by the management company, having regard to the nature and risks of the underlying real estate. However, views were mixed as to whether the SFC should stipulate the extent of such coverage.
  - (iii) The management company should be allowed to manage more than one REIT.
  - (iv) Clarification on acceptable overseas jurisdictions for management companies.

26. *SFC's Response:*

- (a) Management of a REIT: The SFC recognises the benefits of giving the management company flexibility in choosing its mode of management. The SFC has undertaken follow-up studies with market practitioners concerning alternative management set-ups, and notes with interest that new companies may be formed comprising both investment professionals and seasoned property managers. Such an arrangement enables internal management of a REIT by providing a “one-stop service” for a REIT, and would also facilitate the development of home-grown REIT managers. In light of these findings, the Code has been revised to allow for different management models:
  - (i) a fund management company which, having regard to the expertise of its key personnel, delegates or contracts out to qualified third parties one or more of its functions (which may include property management functions), and having established mechanisms in place to supervise the activities of its delegates or contractors on a continuous basis and is ultimately responsible for the management of the REIT;
  - (ii) a fund management company which hires qualified property management professionals and is therefore able to internally manage the REIT; or
  - (iii) a new company, formed for the purpose of managing a REIT, and having within its management and operations structure key personnel from the disciplines of investment management and property management, thus enabling the company to provide a “one-stop” service for the management of the REIT.

Since REITs will be listed and there will be no redemption facility, the administrative aspects of a REIT are very different from open-ended public funds holding liquid assets like equity securities or bonds. Open-



ended funds require fund managers to ensure that on-going subscriptions and redemptions of units and calculation of asset value are performed on a regular and frequent basis. The SFC is therefore prepared to consider, as an alternative to the 5-year public fund management experience requirement, the suitability of a REIT manager on the basis of whether it employs key personnel who possess at least five years' track record managing collective investment schemes including private funds. The management company is also expected to have sufficient resources and experience to oversee issues arising out of the listing of REITs.

On the other hand, since property management is a fundamental aspect of managing a REIT, the SFC believes that it is important to set out the qualification requirements of the key personnel responsible for property management, whether they are part of the management company or outside delegates. With the tenure of rental agreements in Hong Kong generally ranging between three to four years, the SFC will maintain the requirement that such key personnel should have at least five years of property management experience and are professionally qualified to perform such a function.

- (b) In view of the functions to be performed by a management company, the SFC will only accept a management company licensed for Type 9 regulated activity (asset management) to become a management company of a REIT. Whether the management company will also be required to be licensed for other types of regulated activity depends on its mode of operation. For instance, if the company also carries out the distribution and selling of collective investment schemes, a licence for Type 1 regulated activity will likely be required as well.

In order to obtain an SFC licence, the management company must demonstrate to the SFC that it has adequate resources and technical expertise to perform its duties in relation to the management of REITs (including key personnel who the management company is satisfied are fit and proper) and that it complies with the requirements set out in the Code. In circumstances where the management company delegates functions to third parties, it should demonstrate to the SFC that it has sufficient resources and measures in place to properly select, supervise and monitor the activities of its delegates on an on-going basis.

There are currently a large number of management companies licensed for Type 9 regulated activity. Any one of these companies can act as a REIT manager by:

- (i) employing in-house property managers (individuals) with requisite experience and whose roles are properly supervised; or
- (ii) delegating or contracting out the property management functions to external property management companies.

If however, the intention is to establish a new company or apply for a new registration with the SFC for asset management, the application process for registration would take a certain period of time (normally 15 weeks).

*(For further information on licensing, applicants are recommended to refer to the Licensing Information Booklet, Fit and Proper Guidelines and Guidelines on Competence published by the SFC. The SFC also provides on its website answers to some Frequently Asked Questions on licensing related matters. Interested parties are reminded that if they choose the route of establishing a new company, the processing of an application for a new licence takes time. They are reminded to contact the SFC at their earliest convenience, should they choose to use this route.)*

- (c) The SFC agrees that if the management company has ownership or an interest in the REIT it manages, it will have strong incentive to ensure the REIT performs well and this in turn, will benefit unit holders as the management company's interests are aligned with the unit holders of the REIT. Therefore, the SFC has no objection to such an arrangement. However, a management company may not obtain units in the REIT as payment for fees owed to it.

The SFC is also prepared to allow a management company to manage more than one REIT, if the company could demonstrate that it has established procedures to ensure that unit holders of all REITs under its management are fairly and equitably treated and of course, subject to the availability of resources of the management company. However, where transactions are conducted between or among REITs managed by the same management company, such transactions would be deemed connected party transactions and should therefore comply with the provisions on connected party transactions, and be disclosed to unit holders to ensure proper transparency.

On the issue of insurance, the Code has been revised to require the management company to arrange for insurance in relation to the real estate including ownership and lease thereof. However, in view of the fact that the determination of the appropriate level of insurance varies among real estate and requires professional knowledge, the SFC does not consider it appropriate to prescribe any minimum requirements. Meanwhile, the extent of insurance coverage arranged for a REIT should be disclosed to unit holders.

Finally, the SFC has incorporated a list of acceptable inspection regimes whose licensed management companies are considered acceptable for the management of REITs in Hong Kong. Broadly speaking, the regulator in each of these recognised overseas jurisdictions should carry out inspections of the management company, including its REIT activities, within its jurisdiction in a manner generally consistent with that of the SFC, and this regulator should have signed a memorandum of understanding ("MoU") with the SFC regarding the timely exchange of information regarding the management company.

It should be noted that while the Securities and Exchange Commission of the US and Commission des Operations de Bourse of France have entered into MoUs with the SFC, they are not included in the list of acceptable inspection regimes for the purpose of REITs as both of these overseas regulators do not perform inspections on REIT managers in their respective jurisdictions.

### ***Qualification Requirements of Trustees and Their Obligations***

27. *Public Comments:* Comments by respondents generally focused on two aspects, namely the qualification requirements of the trustee and the scope of responsibilities imposed on the trustee.

- (a) **Qualification requirements:** Respondents generally considered the proposed requirement that the trustee should have at least three years of relevant experience in holding real estate under a scheme that operates in a similar manner as a REIT, as being too onerous. They pointed out that there is an absence of such trustees in Hong Kong, given that REITs are a very new product.

Two alternatives were proposed by respondents:

- (i) a trustee should be deemed acceptable by the SFC if it could demonstrate that other members within its corporate group have experience in acting as trustees of schemes that operate in a manner similar to that of a REIT under the Code; and the relevant key personnel of such members could be hired or seconded to the trustee in Hong Kong to ensure that it is equipped with the necessary knowledge and experience; or
- (ii) a trustee should be acceptable by the SFC if it hires a team of qualified and experienced professionals to manage the REIT business.

Some respondents also questioned the exclusion of trust companies registered under Part VIII of the Trustee Ordinance from the list of eligible trustees.

- (b) **Responsibilities of the trustee:** Respondents commented that the scope of responsibilities imposed on the trustee is too broad. They pointed out that some of the responsibilities, such as *ensuring* that properties are properly valued and all connected transactions are identified and properly reported, are inappropriate, given that the trustee may lack expertise in property valuations and has limited knowledge of the identities of connected parties.

28. *SFC's Response:*

- (a) Regarding qualification requirements, the SFC agrees with the respondents' pragmatic approach and has accordingly adopted the alternatives proposed by the respondents. At the same time, the SFC does not consider trust companies registered under the Trustee Ordinance to be suitable candidates to act as trustees for REITs, as these trust companies are subject to a lower capital requirement.
- (b) On the obligations of a trustee, the SFC appreciates the respondents' concern that the trustees may not have sufficient expertise in property valuation. The intention here is to require the trustee to provide a layer of oversight with respect to the operations of a REIT. The trustee has a fiduciary duty with respect to the assets held in a REIT under its trusteeship, and has the responsibility to appoint the board of directors to the SPVs held by the REIT. The relevant provisions in the Code have been revised accordingly to clarify a trustee's fiduciary responsibilities, and to provide that in performing its oversight functions, the trustee may rely on professional advisers.

***Investment Restrictions***

29. *Public Comments:* Most respondents favoured an open architecture approach to investment, in which the management company of a REIT has absolute discretion over:

- (a) geographical exposure of a REIT;
- (b) the type of real estate acquired by a REIT;
- (c) the gearing level of a REIT;
- (d) the cash level of a REIT; and
- (e) the length of time that a REIT holds the real estate.

30. The public comments generally favoured having no geographical restrictions on investments, arguing that full disclosure and adequate risk warnings would be sufficient, and the SFC should not assume that Hong Kong retail investors would not understand the risks. Some respondents were mindful of the potential risks of investing in overseas properties and suggested that the Code should either prescribe a limit on overseas real estate investments or stipulate the overseas jurisdictions in which a REIT may invest.

31. Respondents were also aware of the potential risk of assuming an unduly high level of borrowings but considered that the proposed borrowing limit of 35% of net asset value as being too low. Some suggested that the gearing ratio should be increased to at least 35% of the gross asset value of a REIT, while others considered that the gearing ratio should be determined by the management company. There were also suggestions that the SFC should adopt a pure disclosure-based system in which a REIT is only required to clearly disclose to its unit holders the REIT's geographical exposure and borrowings, as well as the inherent risks.

32. On dividend policy, respondents supported the approach of mandating a certain level of dividend payout ratio but suggested that such ratio should either be determined by the management company or mandated at 50% to 90% of the net after-tax income of a REIT. Some respondents also sought clarification on the definition of “net after tax income”.
33. Respondents also requested that REITs should not be required to hold a property for at least two years, as proposed in the Code. They pointed out that this requirement would limit the flexibility of the REITs in responding to changes in the real estate market. Some even suggested that REITs should be allowed to engage in property development activities.
34. *SFC’s Responses:* The SFC accepts suggestions that hotel, recreation parks and serviced apartments should be included as permissible investments. The SFC has also removed the restriction on cash holdings, raised the borrowing limit to 35% of a REIT’s gross asset value, and reduced the minimum dividend payout ratio to 90% of *net income after tax*. These revisions should significantly improve the financial flexibility of a REIT, as advocated by the respondents. However, it should be noted that the trustee shall determine whether revaluation surplus credited to income or gains on disposal of properties shall form part of net income for distribution to holders.
35. The question of whether REITs should restrict their property investments only to property in Hong Kong is the most difficult issue. Arguably, the removal of the investment restriction to only Hong Kong properties will align Hong Kong with international practice and strengthen Hong Kong’s position as an international finance centre. It will also provide more choices for investors and added flexibility for investment managers. Market participants overseas may also be attracted to establish REITs in Hong Kong and thus adding breadth and depth to the REIT market in Hong Kong. None of the other jurisdictions where REITs are offered imposes any geographical limitations on their REITs, although it must be pointed out that, with few exceptions, the REITs offered in these jurisdictions have invested exclusively in their respective local markets.
36. On the other hand, the potential risks of investing in overseas properties could be substantial. Some respondents to the public consultation also highlighted these risks. The risks involved may include the lack of qualified managers or property valuers, transparency and legal protection such as security of title, enforceability of contract and property rights, quality of corporate governance, availability of information and foreign currency convertibility. Disclosure of such risks and risk warnings may not be sufficient in the case of property investments in jurisdictions with less well developed legal frameworks and protection.
37. The SFC has also considered the alternative of providing a limit on overseas investments; a measure which some respondents suggested could reduce some of the downside risks. The SFC believes that this measure does not address the concerns discussed above, and introduces other practical problems:

- (a) given that asset values fluctuate, the industry would have problems ensuring on-going compliance, while the SFC would have difficulty in monitoring compliance; and
  - (b) since property investments involve huge capital commitments, the setting of a low limit may not be practicable, unless a REIT is of a very substantial size.
38. The SFC believes that since its intention in authorising REITs is to give retail investors additional product choice and a viable alternative to investing in real estate or listed property companies, the SFC should keep this product simple and relate it to the *local* real estate market with which retail investors are familiar, and where the system and legal rights are clear and enforceable. If an investor wishes to invest in real estate overseas, he has plenty of other avenues to do so. The SFC strongly believes that it is of paramount importance to preserve the integrity of the initial REITs in Hong Kong in order to build and develop public confidence in the REIT product and the REIT market.
39. However, this restriction need not be a permanent feature as the SFC will closely monitor how the REIT market develops and will keep the Code under review to assess whether REITs will be able to invest in overseas properties. Towards this end, the SFC will form a task force after the implementation of the Code to examine the appropriate manner, timing and the minimum benchmarks that REITs should set for themselves if and when they invest in overseas properties. The public will also be consulted specifically on this issue.
40. Furthermore, the SFC does not believe it is appropriate to permit REITs to engage in property development activities, on the basis that such activities not only undermine the fundamental principle of rental income generation, but also require skills that are different from those of REIT management, which focus on the generation of recurrent rental income.
41. The provision on holding period is maintained, as it serves to promote the stability of a REIT's source of income. A mechanism (by special resolution of unit holders) to enable the disposal of REIT property prior to the expiry of the holding period can be built-in to enable added flexibility.

### ***Valuation***

42. *Public Comments:* Respondents stress the important of the independence of the valuer and the integrity of valuation reports. Within these parameters, they generally support the proposed qualification requirements of the property valuer and the concept of regular valuation on real estate. However, they suggested the following:
- (a) the paid-up capital requirement of the property valuer should be lowered to HK\$1 million in order to be aligned with the requirement under the Companies Ordinance.

- (b) the proposed valuation frequency would not provide added investor protection, but would instead unnecessarily increase the cost to unit holders.
- (c) the mandatory retirement of the property valuer after every two years is too restrictive, with some suggesting a three-year period while others recommending that the decision should be left to the trustee of a REIT.

43. *SFC's Response:*

- (a) The SFC has maintained the requirement that the valuer be independent of the scheme, the management company, the trustee and the significant holders. Valuers who have acted in certain capacities in relation to real estate being the subject matter of a proposed transaction (eg. the valuer had valued the property for the counter party within the last year, or has been engaged by the scheme to act as principal or agent in relation to the acquisition) are also not permitted to provide valuation to the scheme.
- (b) The SFC has adopted the proposal to lower the paid-up capital requirement in the Code. As property valuers are required to be professionally qualified, possess sufficient expertise and experience, and have adequate professional indemnity insurance, the SFC believes that these standards help to balance the lowering of the capital requirement originally proposed.
- (c) As regards valuation frequency, the Code will require an annual valuation so as to align with Listing Rules requirements.
- (d) The SFC believes that mandatory rotation of the property valuer is important. However, it agrees that a period of two years may be a little too short and could create an undue burden and costs for the REIT. The SFC will now accept a rotation of the property valuer after every three years, as proposed by respondents.

***Corporate Governance***

- 44. *Public Comments:* Comments were supportive of the SFC's attempt to foster a high standard of corporate governance by requiring unit holders' approval of all connected party transactions, unless the value of such transactions is below the proposed threshold of HK\$10 million. However, given the nature of the underlying investments, some respondents suggested that the threshold amount be raised.
- 45. Regarding the definition of "connected persons to the scheme", respondents recommended that unit holders who have a substantial interest in the scheme should also be categorized as such. However, respondent views were mixed as to the threshold for deeming a unit holder to be a substantial holder.
- 46. In view of the fact that REITs authorised under the Code will be listed on the Exchange, industry comments have suggested that REITs be subject to a corporate governance and disclosure regime that is on a par with that governing listed companies.

47. *SFC's Response:* Where transactions involve connected persons, the SFC considers that the existing limit should be set at 5% of the net asset value of a REIT. Meanwhile, the SFC agrees with the view that "significant holders" should be regarded as "connected persons" and that the size of their holdings should be disclosed. Therefore, the Code now includes any unit holder with an interest of 10% or more in a REIT shall be "a significant holder". This is in line with the 10% threshold for a "substantial shareholder" of a listed company.
48. The Code will now adopt a framework that shares broadly similar corporate governance principles as the Listing Rules for connected party transactions. To summarise, the Code requires all connected party transactions (unless below a prescribed threshold) to be subject to voting by unit holders, with those holding a material interest in the transactions to abstain from voting. Advice from an independent expert is also required. Finally, public announcements will have to be made.

### ***Termination of REITs***

49. *Public Comments:* In general, it was suggested that the management company should have the flexibility to decide on the mode, timing and price level at which the real estate of a REIT is disposed of, provided that the transaction is performed in the best interests of the unit holders. The proposed time limit of 21 days for the preparation and despatch of audited financial statements was also considered too short.
50. *SFC's Response:* To provide clarity and ensure certainty, the SFC believes that the Code should stipulate the timeframe for the liquidation of real estate investments in the event that a REIT is terminated. However, the SFC also recognizes the potential difficulty and adverse effect of selling a large portfolio of real estate within a short period of time. Therefore, it now recommends that the termination process should be completed within one year. In the event that the disposal of REIT property within a year is not possible without causing hardship, the trustee has the discretion to grant a further and final extension, not exceeding another twelve months.
51. The management company should be responsible for determining the open bid prices of the real estate and selling the real estate either through public auction or open bid. At the same time, the trustee has the fiduciary duty to oversee the conduct of the termination process. Semi-annual payments should be made to unit holders in respect of proceeds from property disposal, followed by a final payment upon completion of the termination exercise. The final set of accounts should be delivered to unit holders' within three months after the termination is completed.



### ***Exit Mechanism / Listing***

52. *Public Comments:* Respondents favoured the listing of REITs but sought clarification on the roles to be played by the SFC and the Hong Kong Exchanges and Clearing Limited (“HKEx”). However, there were conflicting views regarding unlisted REITs, fixed-term REITs and redemption limits.
53. *SFC’s Response:* Since the majority of the respondents support the listing of REITs and pointed out the various pitfalls of unlisted REITs, the SFC now mandates that all REITs authorised by the SFC shall be listed on the Exchange. While these REITs may issue new units in accordance with the requirements set out in the Code, they are not allowed to redeem units but unit holders may divest their units by selling them on the Exchange. The discussion between the SFC and the HKEx to streamline and shorten the time process for the listing of SFC-authorized funds (including REITs) is now at an advanced stage. The SFC has reached a general understanding with the HKEx that the SFC will be the authority responsible for vetting the constitutional and offering documents and other product description documents, and ensuring their compliance with the Code. The HKEx will be responsible for listing-related matters of REITs including vetting the listing documents, supervising the conduct of the listing process, and monitoring continuous compliance with the Listing Rules. Further details will be released in due course.
54. REITs are now required to appoint a listing agent to oversee the proper management of listing. This agent may be the REIT manager or its delegate and is subject to prior approval by the SFC including such conditions as the SFC may impose.

### ***Disclosures***

55. *Public Comments:* Respondents requested that unit holders be provided with material information about a REIT on a timely basis. In particular, there were requests that:
- (i) the identities of the significant unit holders should be disclosed in the offering documents of a REIT; and
  - (ii) more detailed information on the real estate of a REIT should be disclosed, such as discounted cashflow analysis and yield forecast.
56. *SFC’s Response:* A REIT should provide its unit holders with sufficient and accurate information on a timely basis to ensure a high degree of transparency. The SFC, while mindful of the importance of achieving a balance between the right of the unit holders to be informed and the effect of releasing commercially sensitive data, believes that the disclosure standards of a REIT shall be no less than those of a listed company, given that a REIT is a listed product.

57. Therefore, a disclosure framework to require timely dissemination of information by REITs has been incorporated into the Code. Such disclosure requirements include:
- (i) announcements to be issued with respect to material information pertaining to a REIT or connected party transactions and, where appropriate, circulars and notices also to be issued;
  - (ii) the unit holdings of the significant unit holders to be disclosed in the announcements and circulars, where applicable; and
  - (iii) “significant holders” to be required to disclose in the offering documents any of their business interests which may be in competition with those of the REITs that they hold units in.
58. The SFC recognises the importance of information pertaining to the yield of a REIT. The Code has been amended to allow yield forecast, subject to certain principles and requirements. Meanwhile, the Code only sets out the minimum level of disclosure with respect to the real estate of the scheme. The management company and the property valuer must exercise their professional judgment to ensure that all pertinent information about the real estate of a REIT is accurately and sufficiently disclosed to unit holders.

### ***Other Issues***

59. *Public Comments:* The proposed requirement that new units should be priced at the net asset value of a REIT, based on the valuation report prepared for the REIT, is considered inappropriate as the market price of a REIT is driven by market dynamics, while the valuation of real estate is only conducted periodically and the timing of such valuation may not coincide with that of the offering of units.
60. *SFC’s Response:* The SFC appreciates the practical difficulty in implementing the proposal in the draft Code. The Code is now revised to allow REITs to offer units at prices based on prevailing market conditions.
61. *Public Comments:* The draft Code mentioned the ‘Committee on REITs’. The respondents therefore sought clarification on the nature and role of this committee.
62. *SFC’s Response:* Since REITs involve complex issues regarding property investments and clearly demand a high standard of corporate governance, a Committee on REITs is to be set up in due course. It is intended that the Committee will be advisory in nature and members will be drawn from various sectors of the market, e.g. accounting, investment management, investment banking, law, property management, property valuation and people representing wider public interests. Advice will be sought from the Committee as and when required.

## **Implementation of the Code**

63. The Code will become effective upon publication in the government Gazette.
64. The Code is non-statutory. Funds seeking authorisation as REITs will need to comply with all relevant provisions of the Code. The SFC will adopt a pragmatic approach and will interpret the Code in a manner that ensures overall fairness for all parties concerned and particularly with a view to safeguarding the interests of investors. Where appropriate, the SFC will impose such conditions as it deems proper, under the powers conferred on it by section 104 of the Securities and Futures Ordinance, with respect to its authorisation and regulation of a REIT.
65. Management companies that are newly set up for the purpose of managing REITs are encouraged to discuss their licence applications with the SFC at their earliest convenience.
66. Announcements and disclosures may be made through electronic means.
67. As mentioned earlier, upon implementation of the Code, the SFC will set up a task force to examine the minimum benchmarks that REITs should set for themselves if and when they invest in overseas properties. The public will also be consulted specifically on this issue.
68. Based on Australia's listed property trusts experience (Australia has about 50 listed property trusts capitalising over US\$30 billion), the SFC observes that once the number of listed property trusts reaches a significant level, active takeovers and mergers would take place. While the SFC does not expect that there will be active takeover and merger activities immediately following the launch of REITs, we believe that the Hong Kong market will eventually begin to see mergers and amalgamations of REITs. Therefore, in the longer term, a regulatory regime will have to be worked out to govern this type of activity, and the SFC will consult the market on further guidance as to acceptable practices and standards.
69. The SFC will also review the fee structure for collective investment schemes applying for authorisation as REITs, as they are effectively listed vehicles requiring authorisation and ongoing regulatory oversight based on rules that are very different from those applicable to other collective investment schemes. As such, there appears to be appropriate grounds for placing REITs under a different fee structure to that of other collective investment schemes authorised by the SFC.

### List of Respondents (in alphabetical order)

#### Category A – Commentator has no objection to publication of name and content of submission

1. ABN AMRO Asset Management (Asia) Ltd
2. Alan Choy
3. Alliance Capital Management Australia Ltd
4. Baker & McKenzie
5. Bank Consortium Trust
6. Capital For Business Ltd
7. CB Richard Ellis Ltd
8. Centaline Surveyors Ltd
9. Chun chun dong
10. Clifford Chance
11. Clifford Chance (on behalf of Bermuda Trust (Far East) Ltd, Dexia Trust Services Hong Kong Ltd and HSBC Trustee (Hong Kong) Ltd)
12. Constance Hsu
13. DBS Bank
14. Deacons<sup>1</sup>
15. Deutsche Bank
16. DTZ Debenham Tie Leung Ltd
17. Ernst & Young
18. First American Title Insurance Company
19. Franklin Templeton Investments (Asia) Ltd
20. Guangdong (Int'l) Capital Ltd
21. Hong Kong Institute of Facility Management
22. Hong Kong Policy Research Institute Ltd
23. Hongkong Land
24. HSBC
25. HSBC Asset Management Ltd
26. INVESCO Asia Ltd
27. Jardine Lloyd Thompson Asia
28. Jones Lang LaSalle together with HSBC Trustee (Hong Kong) Ltd, Rodamco Asia, Standard Chartered Bank, Professor K W Chau of The University of Hong Kong and Research Team of the Hong Kong Polytechnic University
29. JPMorgan
30. KPMG
31. Linklaters
32. Lombard Capital Ltd
33. Macquarie Real Estate Asia Ltd and Mallesons Stephen Jaques
34. Merrill Lynch (Asia Pacific) Ltd
35. National Association of Real Estate Investment Trusts
36. Patrick Chung & Associates Ltd
37. Pioneer Global Group Ltd
38. PricewaterhouseCoopers

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<sup>1</sup> Group submission representing 33 industry participants.

39. Rodamco Asia
40. Simmons & Simmons
41. Stephen Chung, Howard Zhang, Jason Lee, Jason Blank, John Chen and Thomas Nam
42. Swire Properties Ltd
43. The HK Association of Online Brokers
44. The Hong Kong Institute of Surveyors
45. The Law of Society of Hong Kong
46. The Real Estate Developers Association of Hong Kong
47. ULI Asia
48. Wan-yi Shiu
49. Zeppelin Group

**Category B – Commentator requested submission to be published on a "no-name" basis**

Three submissions

*Note: A submission was received from The Hong Kong Society of Accountants after the closing date (23 April 2003) of the consultation period.*



SECURITIES AND  
FUTURES COMMISSION  
證券及期貨事務監察委員會

**Code on  
Real Estate Investment Trusts**

**《房地產投資信託基金守則》**

Hong Kong  
August 2003

# Code on Real Estate Investment Trusts (“REITs”)

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## **Authorisation of REITs and its General Principles**

### **Explanatory Notes**

The Securities and Futures Commission ("Commission") is empowered under section 104(1) of the Securities and Futures Ordinance (Cap. 571) ("SFO") to authorise collective investment schemes, subject to such conditions as it considers appropriate.

This Code on Real Estate Investment Trusts ("Code") establishes guidelines for the authorisation of a collective investment scheme which is a real estate investment trust ("REIT").

The Commission is empowered under section 105(1) of the SFO to authorise the issue of an advertisement or invitation to the public in Hong Kong to invest in a collective investment scheme, subject to such conditions as the Commission considers appropriate.

The Commission may at any time review its authorisation of a REIT, or of an advertisement or invitation relating thereto, and may modify, add to or withdraw any of the conditions of such authorisation, or revoke the authorisation, as it considers appropriate.

The issue of a false or misleading advertisement or an invitation to the public in Hong Kong to invest in an unauthorised collective investment scheme may amount to an offence under section 103(1) of the SFO.

This Code does not have the force of law and shall not be interpreted in a way that will override the provision of any law.

## **General Principles**

The Commission has modelled the Code on principles developed by the International Organization of Securities Commissions and other principles that the Commission believes to be fundamental for the proper regulation of REITs. The management company, the trustee and their agents or delegates are expected to comply with the spirit of these principles in managing or administering any matters relating to the operation of a REIT.

### **GP1. Clarity of legal form and ownership structure**

The assets of a REIT shall be held in a trust and segregated from the assets of its trustee, its management company, its related entities, other collective investment schemes and any other entity.

### **GP2. Effective oversight by trustee**

The trustee shall be functionally independent of the management company of a REIT and shall act in the best interests of holders in maintaining the legal integrity of the assets of the REIT. The trustee shall ensure that it discharges its duties with diligence and prudence.

### **GP3. Eligible management company**

The management company of a REIT shall satisfy the Commission that it possesses the human, technical and financial resources to effectively and responsibly discharge its functions in relation to the REIT, including carrying out its stated investment policy. In this aspect, the management company shall observe high standards of integrity, market conduct, fair dealing and corporate governance. Further, the management company shall not exceed the powers conferred upon it by the constitutive documents of the REIT.

### **GP4. Delegation of management functions**

A REIT management company shall perform all the key functions in relation to the management of the REIT. No management function shall be delegated unless the management company can properly monitor and ensure proper performance by the delegate. Notwithstanding that certain subsidiary functions can be delegated to a third party, the management company remains fully liable to the REIT's holders and trustee for the proper performance thereof. The management company shall ensure that a delegate remains competent to undertake the function in question. The legal relationship between the management company and a delegate shall be unambiguous.

### **GP5. Compliance with relevant requirements**

The management company of the REIT shall satisfy the Commission that sufficient systems, controls and procedures are in place to ensure that all applicable regulatory and other legal requirements are complied with. The management company and the trustee of a REIT shall bear ultimate responsibility in ensuring compliance with this Code and they shall deal with the Commission in an open and co-operative manner.

#### **GP6. Good governance and avoidance of conflicts of interest**

The management company shall act in the best interests of the REIT's holders, to whom it owes a fiduciary duty. Transactions entered into by the management company for the REIT shall be at arm's length and on normal commercial terms. The management company shall ensure that procedures are in place to ensure that its staff do not enter into transactions for the REIT which may compromise the interests of the REIT's holders. Unless otherwise specified in this Code, transactions involving connected parties to the scheme shall be subject to holders' approval, and those holders having a material interest in the transactions which is different from the interests of all other unit-holders, shall abstain from voting.

The management company shall adhere to and uphold good corporate governance principles and best industry standards for all activities and transactions conducted in relation to the REIT and any matters arising out of its listing or trading on any stock exchange. The trustee, management company, property valuer and any other delegates of the scheme shall observe the best governance standards.

#### **GP7. Valuation of the scheme**

The management company shall ensure that the assets of a REIT are regularly valued in good faith according to market practice and in accordance with procedures that are approved by the Commission, and prepared in accordance with accepted accounting principles.

#### **GP8. Investment and borrowing limitations**

There shall be investment restrictions and borrowing limitations that take into account the investment objectives, risk profile and liquidity required for a REIT. Such restrictions and limitations shall be disclosed clearly in the offering document of the REIT.

#### **GP9. Management fees and investor rights**

Management fees shall be disclosed clearly in the offering document. A REIT shall ensure that holders are able to participate in significant decisions concerning the REIT and are treated fairly and equitably. Any material change in the REIT's activities shall not unfairly prejudice the rights of the holders.

#### **GP10. Marketing and disclosure**

Potential investors and current holders in a REIT shall be provided with full, accurate and timely information regarding the REIT in order to enable them to fully understand the investment and risk profile of the REIT and to help them make informed investment decisions. All transactions, appointments or activities that could create a conflict of interest or be perceived to create such a conflict should be disclosed to investors and holders. Advertising shall not contain information which is false or misleading nor be presented in a deceptive manner.

### **Effect of Breach of the Code:-**

Failure by any person to comply with any applicable provision of the Code

- (a) shall not by itself render the person liable to any judicial or other proceedings, but in any proceedings under the SFO before any court, the Code shall be admissible in evidence, and if any provision set out in the Code appears to the court to be relevant to any question arising in the proceedings, it shall be taken into account in determining the question; and
- (b) may cause the Commission to consider whether such failure adversely reflects on the person's fitness and properness and the suitability of the REIT to remain authorised.

## **Chapter 1: Administrative Arrangements**

- 1.1 The Commission has delegated its powers under section 104 of the Securities and Futures Ordinance with respect to REITs to its Executive Director (Intermediaries and Investment Products) and any of its delegates appointed pursuant to the Securities and Futures Ordinance.
- 1.2 According to section 8 of the Securities and Futures Ordinance, the Commission is empowered to set up committees whether for advisory or other purposes. The Commission will establish a Committee on REITs for the purpose of consultation and advice on matters that may relate to the Code. The remit of the Committee on REITs and its membership shall be laid down in its Terms of Reference.

### **Data Privacy**

- 1.3 The information requested under the Code may result in the applicant providing the Commission with personal data as defined in the Personal Data (Privacy) Ordinance. The data supplied will only be used by the Commission to perform its functions, in the course of which it may match, compare, transfer or exchange personal data with data held or obtained by the Commission, government bodies, other regulatory authorities, corporations, organizations or individuals in Hong Kong or overseas for the purpose of verifying those data. Subject to the limits in sections 378 of the Securities and Futures Ordinance, the Commission may disclose personal data to other regulatory bodies. Persons who have supplied data to the Commission under the Code may be entitled under the Personal Data (Privacy) Ordinance to request access to or to request the correction of any data supplied to the Commission, in the manner and subject to the limitations prescribed. All enquiries shall be directed to the Data Privacy Officer at the SFC.

## **Chapter 2: Interpretation**

- 2.1 “associate” bears the meaning as defined in the Securities and Futures Ordinance for “associate” of a person.
- 2.2 “associated company”. A company shall be deemed to be an associated company of another company if one of them owns or controls 20% or more of the voting rights of the other or if both are associated companies of another company.
- 2.3 “Code” means Code on Real Estate Investment Trusts issued by the Securities and Futures Commission.
- 2.4 “collective investment scheme” bears the meaning as stated in Schedule 1 of the Securities and Futures Ordinance.
- 2.5 “Commission” or “SFC” refers to the Securities and Futures Commission as stated in section 3 of the Securities and Futures Ordinance.
- 2.6 “Committee” means the Committee on REITs.
- 2.7 “connected persons” shall bear the meaning as defined in 8.1 of this Code.
- 2.8 “constitutive documents” means the principal documents governing the formation of the scheme, and includes the trust deed and all material agreements.
- 2.9 “controlling entity” bears the meaning as defined in the Securities and Futures Ordinance for “controlling entity”, other than (a)(ii) in its definition.
- 2.10 “dividend reinvestment plan” means an automatic reinvestment of holders’ dividends in more units of a scheme.
- 2.11 “Exchange” means The Stock Exchange of Hong Kong Limited.
- 2.12 “holder” in relation to a unit in a scheme means the person who is entered in the register as the holder of that unit.
- 2.13 “Institute” means The Hong Kong Institute of Surveyors.
- 2.14 “management company” means the entity appointed for a scheme pursuant to Chapter 5 of this Code and includes its delegates where applicable.
- 2.15 “offering document” means the document, or documents issued together, containing information on a scheme to invite the public to buy units in the scheme.
- 2.16 “ordinary resolution” by holders of a scheme means a resolution passed by a simple majority of the votes of those present and entitled to vote in person or

by proxy at a duly convened meeting and the votes shall be taken by way of a poll.

- 2.17 “property valuer” or “valuer” refers to the property valuer appointed to a scheme pursuant to Chapter 6 of this Code.
- 2.18 “real estate” or “property” refers to land or buildings, whether the interest is a freehold or leasehold interest, and includes carparks and assets incidental to the ownership of real estate (e.g. fittings, fixtures, etc).
- 2.19 “REIT” shall be a scheme authorised by the Commission under this Code.
- 2.20 “scheme” means a REIT authorised under this Code.
- 2.21 “significant holder” bears the meaning as defined under 8.1 of this Code.
- 2.22 “special purpose vehicles” or “SPVs” means the special purpose vehicles that are 100% held by a scheme in accordance with this Code.
- 2.23 “special resolution” by holders of a scheme may only be passed by 75% or more of the votes of those present and entitled to vote in person or by proxy at a duly convened meeting and the votes shall be taken by way of a poll.
- 2.24 “substantial financial institution” means a licensed banking institution authorised under the Banking Ordinance or a financial institution with a minimum paid-up capital of HK\$150,000,000 or its equivalent in foreign currency.
- 2.25 “trustee” means the entity appointed pursuant to Chapter 4 of this Code.

## **Chapter 3: Basic Requirements for the Authorisation of a REIT**

### **What is a REIT**

- 3.1 A REIT is a collective investment scheme constituted as a trust that invests primarily in real estate with the aim to provide returns to holders derived from the rental income of the real estate. Funds obtained by a REIT from the sale of units in the REIT are used in accordance with the constitutive documents to maintain, manage and acquire real estate within its portfolio.

### **Requisite Conditions for REIT Authorisation**

- 3.2 A REIT seeking authorisation from the Commission shall have the following characteristics: -
- (a) dedicated investments in real estate that generates recurrent rental income;
  - (b) active trading of real estate is restricted;
  - (c) the greater proportion of income shall be derived from rentals of real estate;
  - (d) a significant portion of income is distributed to holders in the form of regular dividends;
  - (e) a maximum borrowing limit is defined; and
  - (f) connected party transactions are subject to holders' approval.
- 3.3 Pursuant to sections 104(2) and 105(2) of the Securities and Futures Ordinance, there shall be an individual approved by the Commission for the purposes of being served by the Commission with notices and decisions for, respectively, the REIT and the issue of any related advertisement, invitation or document. An applicant for authorisation is, therefore, required to nominate an individual for approval by the Commission as an approved person.
- 3.4 An approved person shall:
- (a) have his/her ordinary residence in Hong Kong;
  - (b) inform the Commission of his/her current contact details, including, in so far as applicable, the address, telephone and facsimile numbers, and electronic mail address;
  - (c) be capable of being contacted by the Commission by post, telephone, facsimile and electronic mail during business hours;
  - (d) inform the Commission of any change in his/her contact details within 14 days after the change takes place; and
  - (e) comply with any other requirements as the Commission considers appropriate.



- 3.5 An individual approved by the Commission as an approved person for a REIT shall generally be approved also for the issue of any advertisement, invitation or document made in respect of that REIT.
- 3.6 It is a condition for a REIT to be authorised by the Commission that it will be listed on the Exchange within a period acceptable to the Commission.

## Chapter 4: Trustee

### Appointment of Trustee

- 4.1 Every scheme for which authorisation is requested shall be structured as a trust and appoint a trustee acceptable to the Commission.

*Note: This chapter lists the general obligations of the trustees. Trustees also have to fulfill the duties imposed on them by the general law of trusts.*

### General Obligations of Trustee

- 4.2 The trustee shall:-

- (a) (i) exercise all due diligence and vigilance in carrying out its functions and duties and in protecting the rights and interests of the holders;

*Note: The trustee may seek the opinion or advice of an independent professional adviser concerning matters in the administration of the scheme if it deems appropriate.*

- (ii) ensure that all the assets of the scheme are properly segregated and held for the benefit of the holders in accordance with the provisions of the constitutive documents; and
- (iii) be liable for the acts and omissions of its nominees and agents in relation to assets forming part of the property of the scheme.
- (b) take all reasonable care to ensure that the sale, issue, repurchase and cancellation of units effected by a scheme are carried out in accordance with the provisions of the constitutive documents;
- (c) appoint from time to time a property valuer who meets the qualification requirements set out in Chapter 6 to value the real estate of the scheme and to produce valuation reports with respect to the real estate of the scheme in accordance with Chapter 6;
- (d) cause a valuation of any of the real estate of the scheme to be carried out if it, or the management company, reasonably believes that such valuation is appropriate;
- (e) carry out the instructions of the management company in respect of investments unless they are in conflict with the provisions of the offering or constitutive documents or this Code or under general law;
- (f) take all reasonable care to ensure that the investment and borrowing limitations set out in the constitutive documents and the conditions under which the scheme was authorised are complied with;

- (g) take all reasonable care to ensure that no real estate is acquired or disposed of by or on behalf of the trustee until the trustee has obtained a recent valuation report of a property valuer appointed and instructed in writing by the trustee;

*Note: The effective date as at which the real estate is valued shall not be more than three months before the date on which the relevant circular is issued (if the transaction requires holders' approval) or the date of the sale and purchase agreement (if the transaction does not require holders' approval).*

- (h) take all reasonable care to ensure that all transactions carried out by or on behalf of a scheme are conducted at arm's length and that connected party transactions are carried out in accordance with Chapter 8;

*Note: Where the trustee is in doubt as to whether a transaction is a connected party transaction, it shall require such transaction to be subject to the provisions of Chapter 8.*

- (i) issue a report to the holders, to be included in the annual report, on whether in the trustee's opinion, the management company has in all material respects managed the scheme in accordance with the provisions of the constitutive documents; if the management company has not done so, the report shall specify respects in which it has not done so and the steps which the trustee has taken in respect thereof;

- (j) take all reasonable care to ensure that unit certificates are not issued until subscription monies have been paid;

- (k) take all reasonable care to ensure that a scheme has proper legal title to the real estate owned by the scheme, as well as to the contracts (such as rental agreements) entered into on behalf of the scheme with respect to its assets and that each such contract is legal, valid and binding and enforceable by or on behalf of the scheme in accordance with its terms;

*Note: The real estate shall have a good marketable title.*

- (l) take all reasonable care to ensure that the management company arranges adequate property insurance and public insurance coverage in relation to the real estate of a scheme;

- (m) take all reasonable care to ensure that the net asset value per unit of a scheme is calculated as and when an annual valuation report is issued by the valuer for the relevant period, and that such net asset value shall be published in the annual report;

- (n) require that the management company reports to the trustee as soon as reasonably practicable any breaches of the provisions in this Code and

the trustee shall inform the Commission of such breaches, where appropriate, upon notification by the management company; and

- (o) be responsible for the appointment of the board of directors of all special purpose vehicles held by a scheme.

### **Criteria for Acceptability of a Trustee**

4.3 A trustee shall be:-

- (a) a bank licensed under Section 16 of the Banking Ordinance; or
- (b) a trust company which is a subsidiary of such a bank; or
- (c) a banking institution or trust company incorporated outside Hong Kong which is acceptable to the Commission.

4.4 A trustee shall be independently audited and shall have minimum issued and paid-up capital and non-distributable capital reserves of HK\$10 million or its equivalent in foreign currency.

4.5 Notwithstanding 4.4 above, the trustee's paid-up capital and non-distributable capital reserves may be less than HK\$10 million if the trustee is a wholly-owned subsidiary of a substantial financial institution (the "holding company") acceptable to the Commission; and

- (a) the holding company issues a standing commitment to subscribe sufficient additional capital in the trustee up to the required amount, if so required by the Commission; or
- (b) the holding company undertakes that it will not let its wholly-owned subsidiary default and will not, without prior approval of the Commission, voluntarily dispose of, or permit the disposal or issue of any share capital of the trustee such that the trustee ceases to be a wholly-owned subsidiary of the holding company.

4.6 The trustee shall:

- (a) possess key personnel with the knowledge, organizational resources and experience relevant to the holding of real estate under a scheme that operates in a manner similar to that of a scheme authorised under this Code; or
- (b) belong to a corporate group that:
  - (i) is of good repute;
  - (ii) has acted as trustees for REITs or schemes of similar nature in overseas jurisdictions; and

- (iii) is able to provide the trustee with adequate support in all material aspects to enable the trustee to discharge its functions in relation to the scheme.

#### **Retirement of Trustee**

- 4.7 The trustee shall not retire except upon the appointment of a new trustee whose appointment has been subject to the prior approval of the Commission. The retirement of the trustee shall take effect at the same time as the new trustee takes up office.

#### **Independence of Trustee**

- 4.8 The trustee and the management company shall be independent of each other.
- 4.9 Notwithstanding 4.8 above, if the trustee and the management company are both corporations having the same ultimate holding company, whether incorporated in Hong Kong or outside Hong Kong, the trustee and the management company are deemed to be independent of each other if:-
  - (a) they are both subsidiaries of a substantial financial institution;
  - (b) neither the trustee nor the management company is a subsidiary of the other;
  - (c) no person is a director of both the trustee and the management company;
  - (d) both the trustee and the management company sign an undertaking that they will act independently of each other in their dealings with the scheme; and
  - (e) the ultimate holding company of the trustee and the management company submits a declaration and an undertaking to the Commission that the trustee and the management company are, and that the ultimate holding company shall ensure that they continue to be, independent of each other, except as regards their relationship with each other as member companies in the same group.

## **Chapter 5: Management Company, Auditor and Listing Agent**

### **Appointment of a Management Company**

- 5.1 Every scheme for which authorisation is requested shall appoint a management company acceptable to the Commission.

### **General Obligations of a Management Company**

- 5.2 A management company shall:-

- (a) manage the scheme in accordance with the scheme's constitutive documents in the sole interest of the holders. It shall also fulfill the duties imposed on it under general law;
- (b) ensure that the financial and economic aspects of the assets of the scheme are professionally managed in the sole interest of the holders; including, without limitation:
  - (i) formulating the investment strategy and policy of the scheme and managing risks connected with the scheme efficiently;
  - (ii) determining the borrowing limit of the scheme;
  - (iii) investing in real estate that meets the investment objective of the scheme;
  - (iv) managing the cashflows of the scheme;
  - (v) managing the financial arrangements of the scheme;
  - (vi) formulating dividend payment schedules of the scheme;
  - (vii) arranging adequate property insurance and public insurance coverage in relation to the real estate of the scheme;
  - (viii) planning the tenant mix and identifying potential tenants;
  - (ix) formulating and implementing leasing strategies;
  - (x) enforcing tenancy conditions;
  - (xi) ensuring compliance with government regulations in respect of the real estate under management;
  - (xii) performing tenancy administration work, such as managing tenant occupancy and ancillary amenities, and negotiating with tenants on grant, surrender and renewal of lease, rent review, termination and re-letting of premises;
  - (xiii) conducting rental assessment, formulating tenancy terms, preparing tenancy agreements, rent collection and accounting, recovery of arrears and possession;
  - (xiv) securing and administering routine management services, including security control, fire precautions, communication systems and emergency management;
  - (xv) formulating and implementing policies and programmes in respect of building management, maintenance and improvement; and
  - (xvi) initiating refurbishment and monitoring such activity.

- (c) ensure that the scheme has proper legal title to the real estate owned by the scheme, as well as to the contracts (such as rental agreements) entered on behalf of the scheme with respect to its assets, and that all such contracts are legal, valid and binding, and enforceable by or on behalf of the scheme in accordance with its terms;
- (d) maintain or cause to be maintained proper books and records of the scheme (and where applicable of all SPVs) in Hong Kong and prepare the scheme's financial statements which are in agreement with the scheme's books and records and in accordance with the relevant provisions of this Code, the constitutive and offering documents or circulars in relation to the scheme and which give a true and fair view of the state of affairs of the scheme at the end of the financial period and of the financial transactions of the scheme for the financial period then ended;
- (e) prepare and publish reports, and at least two reports shall be published in respect of each financial year, such reports to be sent to all holders and filed with the Commission within the time frame specified in Chapter 10;
- (f) ensure that all documents in relation to the scheme, (including those in relation to its listing but excluding such documents containing commercially sensitive information) are made available for inspection by the public in Hong Kong, free of charge at all times during normal office hours at the place of business of the management company and that of the approved person; and ensure that copies of such documents are available upon request by any person upon the payment of a reasonable fee;
- (g) ensure that holders are given sufficient prior notice, and where applicable, right to vote, with respect to any material change to the scheme, such as an increase in the level of management fees, changes in investment objectives or proposal to de-authorise the scheme; and
- (h) ensure compliance with any applicable laws, rules, codes or guidelines issued by governmental departments, regulatory bodies, exchanges or any other organizations regarding the activities of the scheme or its administration.

### **Criteria for Acceptability of Management Company**

- 5.3 A management company shall be licensed under Part V of the Securities and Futures Ordinance and approved by the Commission to manage the scheme.

*Note: Where a management company is licensed by the securities regulator of an overseas regime acceptable to the Commission to conduct business similar to that carried out by the scheme, the Commission may consider such management company acceptable where several conditions are met. The management company shall be subject to the regulatory oversight of the overseas regulator. There shall be a*

*memorandum of understanding between the overseas regulator and the Commission whereby the Commission can rely on the mutual assistance of the overseas regulator in regulatory matters in relation to the management company. Such overseas management company shall demonstrate to the satisfaction of the Commission that it generally meets the requirements imposed on a management company under this Code and it is experienced with respect to the property market of Hong Kong. It shall also undertake to the Commission that it will, upon request, provide the Commission with all books and records relating to the scheme. A list of overseas regimes acceptable to the Commission is set out in Appendix A.*

- 5.4 The management company shall possess sufficient human, organizational and technical resources for the proper performance of its duties, including two responsible officers each of whom shall have at least five years' track record in managing collective investment schemes, and at least one of the responsible officers shall be available at all times to supervise the management company's business of regulated activity, including asset management. It shall also maintain satisfactory internal controls and written compliance procedures which address all applicable regulatory requirements.

*Notes: (1) For the purpose of determining the experience of the responsible officers, the Commission may consider their experience in managing private funds.*

*(2) The management company may choose to itself perform all the functions required of it under this Code or delegate or contract out to one or more outside entities one or more of these functions (see 5.7). Where it chooses to itself perform the function of management of the real estate of the scheme, the management company shall have key personnel who are specifically responsible for the property management functions and who shall be professionally qualified to manage real estate. Each such person shall have at least five years of experience in managing real estate. The management company shall properly supervise such personnel and ensure that they are fit and proper.*

- 5.5 The management company shall:

- (a) demonstrate that it has sufficient financial resources at its disposal to enable it to conduct its business effectively and meet its liabilities; in particular, it shall comply with any financial requirement applicable to the company under the Securities and Futures (Financial Resources) Rules; and
- (b) not lend to a material extent.



5.6 Indebtedness owed by the management company to its parent company will be considered as part of capital for the purpose of 5.5 in the following circumstances:-

- (a) the indebtedness shall not be settled without the prior written consent of the Commission; and
- (b) the indebtedness shall be subordinated to all other liabilities of the management company, both in terms of its entitlement to income and its rights in a liquidation.

5.7 The management company may delegate one or more functions in relation to the scheme, and it shall:

- (a) ensure that its delegates have sufficient experience and financial resources at their disposal to enable them to conduct their business and meet their liabilities; and
- (b) demonstrate that it has proper due diligence procedures and management or administrative structures in place for the selection and on-going monitoring of the delegate(s).

*Notes: (1) The management company shall ensure that its delegates are fit and proper. This includes ensuring that the delegates are companies with a good and established reputation in performing such duties, and have sufficient resources, relevant experience, and professional qualifications (those set out in Note (2) to 5.4) to carry out their duties in relation to the functions being delegated. Such delegates shall also be financially sound, have a positive net asset position, and have acquired sufficient insurance (including professional insurance, where applicable) to cover the usual risks.*

*(2) The agreement between the management company and each of the delegates shall clearly document the demarcation of functions between themselves.*

*(3) The management company shall be entitled to inspect, and the delegates shall make available for inspection, any books and records kept by the delegates in relation to the functions delegated to them.*

5.8 The management company shall at all times maintain on-going supervision and regular monitoring of the competence of its delegates to ensure that the management company's accountability to investors is neither diminished nor compromised. Although one or more functions of the management company may be delegated to third parties, the responsibilities and obligations of the management company may not be delegated and shall remain the responsibilities and obligations of the management company.

- 5.9 All transactions carried out by or on behalf of the scheme shall be at arm's length. In particular, any transactions between the scheme and the management company or any other connected persons to the scheme acting as principal may only be made and disclosed in the scheme's annual report, both in accordance with Chapter 8.
- 5.10 The management company shall satisfy the Commission as to the overall integrity of the management company. The management company shall ensure that it has reasonable assurance of the adequacy of internal controls and the existence of written procedures, which shall be regularly monitored by the management company's senior management for updatedness and compliance. Conflicts of interests shall be properly addressed to safeguard investors' interests.
- 5.11 The management company of the scheme shall ensure that there are sufficient resources and expertise to address the requirements of the Exchange and to comply with its listing rules. The management company shall ensure that the initial public offering process is conducted in a fair, proper and orderly manner. An agent shall be appointed to be responsible for preparing the scheme as a new applicant for listing, for lodging the formal application for listing and all supporting documents with the Exchange and for dealing with the Exchange on all matters arising in connection with the application. In particular, such agent shall have sufficient experience to discharge the following functions:
- (a) communications with the Exchange – the agent will deal with the Exchange on all matters arising from the listing application and ensure that all the applicable procedural and documentary requirements are complied with; and
  - (b) overall management of the offer of interests in the scheme through the Exchange and the listing process – the agent will ensure that the offer and listing process are managed and conducted in a fair, timely and orderly manner.
- 5.12 Subject to the approval of the Commission, the management company may itself perform the functions and duties described in 5.11, or appoint an agent for such purpose.

*Notes: (1) The management company shall ensure that it, and any agent appointed by it, performs its functions and duties in accordance with the standards required under the Commission's codes and guidelines including the Corporate Finance Adviser Code of Conduct, licensing conditions and such other conditions as the Commission shall impose.*

*(2) It is the duty of the management company to ensure that any agent appointed for the purpose of managing an initial public offering for a scheme and the listing of the scheme is fit and proper, and possesses the relevant experience and resources to undertake the*

*same. Notwithstanding the appointment of an agent, the management company shall remain responsible for all matters relating to the conduct of an initial public offering and the listing of the scheme.*

*(3) The agent appointed in connection with the listing of a scheme shall be a person licensed by the Commission to engage in one or more regulated activities including the provision of corporate finance services, and shall be acceptable to the Commission. The agent shall at all times conduct its activities in accordance with the standards and requirements under the Commission's codes and guidelines including the Corporate Finance Adviser Code of Conduct, licensing conditions and such other conditions as the Commission may impose.*

*(4) Marketing materials in relation to a scheme may only be published, distributed or issued to the public after they are authorised by the SFC. For avoidance of doubt, the SFC would normally not authorise any marketing materials for a scheme before the scheme is authorised by the Commission or listing approval is granted by the Exchange.*

5.13 The management company shall disclose to holders of the scheme of the name of any significant holder with which it has a relationship, and the nature of such relationship.

#### **Retirement of a Management Company**

5.14 The management company shall be removed by the trustee by notice in writing in any of the following events:-

- (a) the management company goes into liquidation, becomes bankrupt or has a receiver appointed over its assets or any part thereof; or
- (b) for good and sufficient reason(s), the trustee states in writing that a change in management company is desirable in the interest of the holders; or
- (c) holders representing at least 75% in value of the units outstanding (excluding those held or deemed to be held by the management company, as well as by any holders who may have an interest in retaining the management company), deliver to the trustee a written request to dismiss the management company.

*Notes: Units held by holders who are (i) directors, senior executives or officers of the management company; or (ii) associates of the persons in (i); or (iii) controlling entity, holding company, subsidiary or associated company of the management company or any holders who may have an interest in retaining the*

*management company, are units deemed to be held by the management company or holders, as the case may be.*

- 5.15 In addition, the management company shall retire:-
- (a) in all other cases provided for in the constitutive documents where such retirement will not adversely affect the interests of the holders in any material respect; or
  - (b) when the Commission withdraws its approval of the management company.
- 5.16 The trustee shall inform the Commission forthwith of any proposal or decision to remove the management company.
- 5.17 Upon the retirement or dismissal of the management company, the trustee shall appoint a new management company as soon as possible whose appointment has been subject to the prior approval of the Commission.

**Appointment of the Auditor**

- 5.18 The management company shall, at the outset and upon any vacancy, appoint an auditor for the scheme and any special purpose vehicles acquired or to be acquired by the scheme.
- 5.19 The auditor shall normally have an international name and reputation, and shall be qualified under the Professional Accountants Ordinance for appointment as an auditor of a company and independent of the management company, the trustee and any other party concerned.
- 5.20 The management company shall cause the scheme's financial statements to be audited by the auditor. Such statements shall contain the information in Appendix C.

## **Chapter 6: Property Valuer**

### **Appointment of a Property Valuer**

- 6.1 Every scheme for which authorisation is requested shall appoint an independent property valuer in accordance with 6.4.

*Note: The agreement for such appointment shall clearly list the obligations and length of tenure of the property valuer as set out in this Chapter.*

### **General Obligations of a Property Valuer**

- 6.2 A property valuer shall value all the real estate held under the scheme, on the basis of a full valuation with physical inspection in respect of the site of the real estate and an inspection of the building(s) and facilities erected thereon once a year, and in any event for the purposes of issuance of new units. A property valuer shall also produce a valuation report on real estate to be acquired or sold by the scheme or where new units are offered by the scheme or in any other circumstances prescribed by the Code. The contents of the valuation report shall comply with 6.8.
- 6.3 The valuation methodology shall follow the “Hong Kong Guidance Notes on the Valuation of Property Assets” published by the Hong Kong Institute of Surveyors.

### **Criteria for Acceptability of Property Valuer**

- 6.4 A property valuer shall be a company that:
- (a) provides property valuation services on a regular basis;
  - (b) carries on the business of valuing real estate in Hong Kong;
  - (c) has key personnel who are fellow or associate members of the Hong Kong Institute of Surveyors and who are qualified to perform property valuations;
  - (d) has sufficient financial resources at its disposal to enable it to conduct its business effectively and meet its liabilities; in particular, it shall have a minimum issued and paid-up capital and capital reserves of HK\$1 million or its equivalent in foreign currency, and its assets shall exceed its liabilities by HK\$1 million or more as shown in the company’s last audited balance sheet;
  - (e) has robust internal controls and checks and balances to ensure the integrity of valuation reports and that these reports are properly and professionally prepared in accordance with international best practice; and
  - (f) has adequate professional insurance to cover its usual risks.
- 6.5 The property valuer shall be independent of the scheme, the trustee, the management company and each of the significant holders of the scheme. The property valuer is not considered independent if:-

- (a) it is the subsidiary or holding company of:
  - (i) the management company of the scheme;
  - (ii) the trustee of the scheme;
  - (iii) any of the significant holders of the scheme; or
  - (iv) the holding company, subsidiary or associated company of the scheme's management company, the scheme's trustee, or any of the significant holders of the scheme; or
- (b) any of its partners, directors or officers is an officer, servant, director or an associate of:
  - (i) the management company of the scheme;
  - (ii) the trustee of the scheme;
  - (iii) any of the significant holders of the scheme;
  - (iv) the holding company, subsidiary or associated company of the scheme's management company, trustee or any of its significant holders; or
- (c) any of its directors or officers holds or controls 10% or more of the beneficial interest in, or the right to vote in the governing bodies of, any of the entities in (b)(i), (b)(ii), b(iii) or (b)(iv); or
- (d) in the case where the scheme intends to acquire or dispose of a property (the "subject property"), the valuer or its associate:
  - (i) is engaged whether as principal or agent by the scheme's counterparty that intends or has agreed to sell to or purchase from the scheme the subject property, in relation to the introduction or referral of the scheme to the subject property or vice versa; or
  - (ii) is engaged whether as principal or agent by the scheme in relation to the acquisition of the subject property; or
  - (iii) acts as a broker for the property transaction for a fee; or
  - (iv) had, at any time during the one year immediately before the date of the agreement for such intended purchase or disposal, been retained to provide valuation of the subject property to the scheme's counterparty(or its associated companies).

6.6 The valuer shall ensure that its opinion and valuation is independent of and unaffected by its business or commercial relationship with other persons.

#### *Qualifications of Directors*

6.7 The directors of the property valuer shall be persons of good repute who possess the necessary experience for the performance of their duties.

## Valuation Report

6.8 The property valuer shall produce a valuation report which shall include as a minimum:

- (a) all material details in relation to the basis of valuation and the assumptions used;
- (b) describe and explain the valuation methodologies adopted;
- (c) the following particulars in respect of each property, such as:
  - (i) an address sufficient to identify the property, which shall generally include postal address, lot number and such further designation as is registered with the appropriate government authorities in Hong Kong;
  - (ii) the nature of the interest the scheme holds in the property (e.g. if it is a freehold or leasehold, and the remainder of the term if it is a leasehold);
  - (iii) the existing use (e.g. shops, offices, factories, residential, etc.);
  - (iv) a brief description of the property, such as the age of the building, the site area, gross floor area, net lettable floor area, and the current zoning use;
  - (v) the options or rights of pre-emption and other incumbrances concerning or affecting the property;
  - (vi) the occupancy rate;
  - (vii) lease cycle duration;
  - (viii) lease expiry profile;
  - (ix) a summary of the terms of any sub-leases or tenancies, including repair obligation, granted to the tenants of the property;
  - (x) the capital value in existing state at the date the valuation was performed;
  - (xi) the existing monthly rental before profits tax if the property is wholly or partly let together with the amount and a description of any outgoings or disbursements from the rent, and, if materially different, the estimated current monthly market rental obtainable, on the basis that the property was available to let on the effective date as at which the property was valued;
  - (xii) the estimated current net yield;
  - (xiii) a summary of any rent review provisions, where material;
  - (xiv) the amount of vacant space, where material; and
  - (xv) any other matters which may affect the property or its value;
- (d) particulars (as set out in (c)) of any real estate for which the scheme has an option to purchase; and
- (e) a letter stating the independent status of the valuer and that the valuation report is prepared on a fair and unbiased basis.

6.9 Whenever a valuation report is prepared for the scheme, the date of the valuation report shall be:

- (a) the date the scheme is valued, if such report is prepared for the purpose of calculating the net asset value of the scheme; or
- (b) a date which is not more than three months before the date on which:
  - (i) an offering document is issued; or
  - (ii) a circular is issued, if the circular relates to a transaction that requires holders' approval; or
  - (iii) a sale and purchase agreement (or other agreement to transfer legal title) is signed, if the transaction does not require holders' approval.

*Note: Where the date of the valuation report precedes the end of the last period reported on by the auditor, it will be necessary for the offering document or circular to include a statement reconciling the valuation figure with the figure included in the balance sheet as at the end of the period in the event the two figures are different.*

### **Retirement of a Property Valuer**

- 6.10 The property valuer shall retire after it has conducted valuations of the real estate of the scheme for three consecutive years. Furthermore, the same valuer may only be re-appointed after another three years.
- 6.11 The property valuer shall be subject to removal by notice in writing from the trustee in any of the following events:
  - (a) the property valuer goes into liquidation, becomes bankrupt or has a receiver appointed over its assets; or
  - (b) for good and sufficient reason, the trustee states in writing that a change in the property valuer is desirable in the interests of the holders; or
  - (c) an ordinary resolution is passed by the holders to dismiss the property valuer.

*Notes: The following persons shall abstain from voting:*

- (i) the property valuer;
- (ii) directors, senior executives or officers of the property valuer;
- (iii) associates of the persons in (ii); and
- (iv) controlling entity, holding company, subsidiary or associated company of the property valuer.

- 6.12 In addition, the valuer shall retire in all other cases provided for in the constitutive documents.
- 6.13 Upon the retirement or dismissal of the valuer, the trustee shall appoint a new property valuer that meets the qualification requirements of this Chapter.



## **Chapter 7: Investment Limitations and Dividend Policy**

### **Core Requirements**

7.1 The scheme shall only invest in real estate in Hong Kong.

*Notes: (1) The real estate shall generally be income-generating.*

*(2) The scheme may acquire uncompleted units in a building which is unoccupied and non-income producing or in the course of substantial development, redevelopment or refurbishment, but the aggregate contract value of such real estate shall not exceed 10% of the total net asset value of the scheme at the time of acquisition.*

*(3) The offering document shall clearly disclose if the scheme intends to acquire further properties during the first 12 months from listing.*

7.2 The scheme is prohibited from investing in vacant land or engaging or participating in property development activities. For this purpose, property development activities do not include refurbishment, retrofitting and renovations.

7.3 A scheme shall not lend, assume, guarantee, endorse or otherwise become directly or contingently liable for or in connection with any obligation or indebtedness of any person nor shall it use any assets of the scheme to secure the indebtedness of any person nor shall it use any assets of the scheme to secure any obligations, liabilities or indebtedness without the prior written consent of the trustee.

7.4 A scheme shall not acquire any asset which involves the assumption of any liability that is unlimited.

### **Use of Special Purpose Vehicles**

7.5 The scheme may hold real estate through special purpose vehicles only if:

- (a) the special purpose vehicles are 100% legally and beneficially wholly-owned by the scheme;
- (b) the special purpose vehicles are incorporated in jurisdictions which have established laws and corporate governance standards which are commensurate with those observed by companies incorporated in Hong Kong;
- (c) there is either:
  - (i) one layer of special purpose vehicles which are established for the sole purpose of directly holding real estate for the scheme and/or arranging financing for the scheme; or

- (ii) two layers of special purpose vehicles, comprising a top-layer special purpose vehicle which is formed solely for the purpose of holding 100% interests in one or more special purpose vehicles described in (i);
- (d) the scheme has no more than two layers of special purpose vehicles;
- (e) neither the memorandum or articles of association or equivalent constitutional documents of the special purpose vehicles nor the organization, transactions or activities of such vehicles shall under any circumstance contravene any requirements of this Code;
- (f) the board of directors of each of the special purpose vehicle shall be appointed by the trustee of the scheme; and
- (g) both the scheme and the special purpose vehicles shall appoint the same auditor and adopt the same accounting principles and policies.

*Note: Where the scheme invests in hotels, recreation parks or serviced apartments, such investments shall be held by special purpose vehicles.*

7.6 If the scheme acquires real estate through the acquisition of a special purpose vehicle, the following shall be complied with for the purpose of the purchase:

- (a) a report made by accountants (who shall be named in the offering document or circular) shall be prepared on:
  - (i) the profit and loss of the special purpose vehicle in respect of each of the three financial years (or such other shorter period as appropriate) immediately preceding the transaction; and
  - (ii) the assets and liabilities of the special purpose vehicle as at the last date (which cannot be more than 6 months old from the date of the report) to which the accounts of the special purpose vehicle were made up;

*Note: The accountant shall be qualified under the Professional Accountants Ordinance for appointment as auditor of a company and shall not be an officer or servant, or a partner of or in the employment of an officer or servant, of the special purpose vehicle or of the vehicle's subsidiary or holding company or of a subsidiary of the vehicle's holding company; and the expression "officer" shall include a proposed director but not an auditor.*

- (b) the report required under (a) shall:
  - (i) indicate how the profits and losses of the special purpose vehicle would, in respect of the shares to be acquired, have concerned the scheme, if the scheme had at all material times held the shares to be acquired; and
  - (ii) where the special purpose vehicle has subsidiaries, deal with the profits or losses and the assets and liabilities of the special purpose vehicle and its subsidiaries, either as a whole, or separately; and

- (c) a valuation report in respect of the special purpose vehicle's interest in real estate shall be prepared, and such report shall comply with the requirements set out in Chapter 6.

7.7 The scheme shall hold good marketable legal and beneficial title in all its real estate, whether directly or via a 100% owned special purpose vehicle. However, the scheme may hold such title whether as joint tenants or tenants-in-common with one or more third parties provided that the scheme shall hold majority interest and control and the scheme has freedom to dispose of its interest (subject to complying with applicable requirement of this Code).

### **Holding Period**

7.8 The scheme shall hold each property within the scheme for a period of at least two years, unless the scheme has clearly communicated to its holders the rationale for disposal prior to this minimum holding period and its holders have given their consent to such sale by way of a special resolution at a general meeting.

*Note: In the case where a property is held through a special purpose vehicle, this provision applies as well to the disposal of such special purpose vehicle.*

### **Limitations on Borrowing**

7.9 A scheme may borrow (either directly or through its SPVs) for financing investment or operating purposes but aggregate borrowings shall not at any time exceed 35% of the total gross asset value of the scheme. The scheme may pledge its assets to secure such borrowings. The scheme shall disclose in its offering document its borrowing policy, including its maximum borrowing limit, and the basis for calculating such limit.

*Notes:(1) In the event that the limit is exceeded, holders and the Commission shall be informed of the magnitude of the breach, the cause of the breach, and the proposed method of rectification. While the scheme may not be required to dispose of assets to pay off part of the borrowings where such disposal is prejudicial to the interest of the holders, no further borrowing is permitted. The management company shall use its best endeavours to reduce the excess borrowings. Furthermore, holders and the Commission shall be informed on a regular basis as to the progress of the rectification.*

*(2) All borrowings shall be conducted at arm's length and the terms shall be commensurate with those of transactions of similar size and nature.*

*(3) The borrowings of all special purpose vehicles held by the scheme shall be aggregated for the purpose of calculating borrowing limits.*

7.10 The scheme shall disclose at least the following data on its borrowings and liabilities in its semi-annual report, annual report and such circulars pertaining to either a breach in borrowing limits or a real estate transaction:

- (a) total borrowings as a percentage of gross assets; and
- (b) gross liabilities as a percentage of gross assets.

*Note: Such data shall reflect the aggregate borrowings and liabilities of all the special purpose vehicles held by the scheme.*

#### **Name of Scheme**

7.11 If the name of the scheme indicates a particular type of real estate, the scheme shall invest at least 70% of its non-cash assets in such type of real estate.

#### **Dividend Policy**

7.12 The scheme shall distribute to unitholders as dividends each year an amount not less than 90% of its audited annual net income after tax.

*Notes: (1) The trustee shall determine if any (i) revaluation surplus credited to income, or (ii) gains on disposal of real estate, shall form part of net income for distribution to holders.*

*(2) Where the scheme holds real estate via special purpose vehicles, each special purpose vehicle shall distribute to the scheme all of its income as permitted by the laws and regulations of the relevant jurisdictions.*

## Chapter 8: Transactions with Connected Persons

### Connected Persons

8.1 Connected persons to the scheme include:

- (a) the management company of the scheme;
- (b) the property valuer of the scheme;
- (c) the trustee of the scheme;
- (d) a significant holder.

*Notes: (1) A holder is a significant holder if it holds 10% or more of the outstanding units of the scheme.*

*(2) The following holdings will be deemed holdings of a holder:*

- (i) holdings of the associate of the holder who is an individual; or*
- (ii) holdings of the director, senior executive, officer, controlling entity, holding company, subsidiary or associated company of the holder if the holder is an entity.*

- (e) a director, senior executive or an officer of any of the entities in 8.1 (a), (b), (c) or (d) above;
- (f) an associate of the persons in 8.1(d) or 8.1(e);
- (g) a controlling entity, holding company, subsidiary or associated company of any of the entities in 8.1 (a) to (d).

8.2 The following shall be disclosed in the scheme's offering document, semi-annual reports, annual reports and circulars in relation to connected party transactions:

- (a) beneficial interests, and any changes thereof, of the connected persons in the scheme; and
- (b) any potential conflicts of interests involving the connected persons and the measures implemented to address such conflicts.

8.3 Where any of the connected persons as described in 8.1 has an interest in a business ("related business") which competes or is likely to compete, either directly or indirectly, with the scheme's activities, the offering document shall prominently disclose the following:

- (a) a description of the related business of the connected person and its management, to enable investors to assess the nature, scope and size of such business, with an explanation as to how such business may compete with the scheme;

- (b) where applicable, a statement from the relevant connected person that it is capable of performing, and shall perform, its duty in relation to the scheme independently of its related business and in the best interests of the scheme and its holders; and
- (c) a statement as to whether the scheme may acquire any of the related business or assets of the connected person in the future, together with the time frame during which such acquisition will take place or no such acquisition is intended. If there is any change in such information after the scheme is authorised, the management company shall announce it by way of a press announcement as soon as the management company or the trustee becomes aware of such change.

*Note: Where the management company manages any schemes other than the scheme, the management company shall prominently disclose in the offering document and in the next published semi-annual or annual report, the same matters as set out in (a), (b) and (c) as if each of the other schemes were a related business of the management company.*

8.4 Where any of the connected persons as described in 8.1 has for the purpose of the establishment of the scheme, agreed to sell real estate to the scheme, the offering document shall prominently disclose the following:

- (a) a valuation report of the real estate that the connected person has agreed to sell; and
- (b) the price to be paid by the scheme for the subject real estate and other terms of the transaction.

### **Connected Party Transactions**

#### *Categories of Transactions*

8.5 For the purpose of this Code, a connected party transaction is any transaction between the scheme and any of the persons described in 8.1 or any transaction falling within 8.6.

8.6 If the management company manages more than one scheme and a transaction involves two or more of the schemes managed by the management company, transactions between these schemes shall be deemed connected party transactions for each of the schemes involved in the transactions.

8.7 All transactions carried out by or on behalf of the scheme shall be:

- (a) carried out at arm's length;

*Note: The management company shall ensure that all transactions are carried out in an open and transparent manner. Where*

*circumstances permit, transactions shall be carried out by way of open tender or competitive bidding by auction.*

- (b) valued, in relation to a property transaction, by an independent valuer that meets the requirements of Chapter 6;
- (c) consistent with the investment objectives and strategy of the scheme;
- (d) in the best interests of holders; and
- (e) properly disclosed to holders.

8.8 If cash forming part of the scheme's assets is deposited with the trustee, the management company, the property valuer of the scheme or with any other connected persons (being an institution licensed to accept deposits), interest shall be paid on the deposit at a rate not lower than the prevailing commercial rate for a deposit of that size and term. The same principle applies to the scheme's borrowings from the trustee, the management company, the property valuer of the scheme or any other connected persons (being an institution licensed to lend money).

8.9 Holders' prior approval is not required for connected party transactions where:

- (a) the total consideration or value of the transaction is less than 5% of the latest net asset value of the scheme, as disclosed in the latest published audited accounts of the scheme, and adjusted for any subsequent transactions since the publication of such accounts; and

*Note: Where more than one transaction is conducted with the same connected person and the value of this single transaction does not exceed the 5% limit, the limit applies to the cumulative value of all the transactions between such person and the scheme during the twelve months preceding the intended transaction.*

- (b) the scheme has not entered into any other transactions with the same connected person (including its associate, controlling entity, holding company, subsidiary or associated company) during the twelve months preceding the current transaction .

In such case, the management company shall issue an announcement to holders in accordance with 8.14 and Chapter 10.

8.10 Connected party transactions in the nature of services provided relating to the real estate of the scheme in the ordinary and usual course of estate management, such as renovation and maintenance work, shall be contracted on normal commercial terms and subject to the prior approval of the trustee.

*Notes: (1) Where the service to be contracted with the connected party is of a stand alone or one-off nature, and the contracted value*

*exceeds 15% of the aggregate value that the scheme committed to spend or has spent on services relating to the real estate of the scheme during the preceding twelve months, prior approval by holders by way of an ordinary resolution passed in a general meeting is required, unless the service to be contracted is procured under a public tender. The requirements in 8.14 and Chapter 10 with respect to announcement, circular and notice shall be complied with to inform holders of such particulars as the nature and value of the service, the name of the connected person, the date of the general meeting, and the result of the holders' voting.*

- (2) *Services provided by the management company, the trustee and the property valuer to the scheme as contemplated under the constitutive documents shall not be deemed connected party transactions but particulars of such services (except where any services transaction has a value of not more than HK\$1 million), such as terms and remuneration, shall be disclosed in the next published semi annual report or annual report.*

- 8.11 Holders' prior approval is required for connected party transactions that do not fall within any of the categories in 8.9 or 8.10. Such approval shall be by way of an ordinary resolution passed in a general meeting. An announcement shall be made and a circular and notice shall be issued to holders in accordance with Chapter 10. The general meeting shall be conducted in accordance with 9.9.

*Note: An ordinary resolution is required for the approval of a connected party transaction in accordance with 9.9(g). Any holder who has a material interest in the transaction tabled for approval and that interest is different from that of all other holders, shall abstain from voting at the general meeting.*

- 8.12 Neither the management company, its delegates, the property valuer of the scheme nor any other connected persons to the scheme may retain cash or other rebates from a property agent in consideration of referring transactions in scheme property to the property agent. All such amounts received shall be paid to the trustee for the benefit of the scheme.
- 8.13 Except for the management company in discharging their functions under Chapter 5, the scheme shall not engage connected persons as property agents for rendering services to the scheme, including advisory or agency services in property transactions.

*Disclosure and reporting requirements for connected party transactions*

- 8.14 Announcements shall be made for all connected party transactions. Following the announcements of these connected party transactions, details of the transactions shall be disclosed by way of a circular where a vote by holders is required. Where holders' approval is required, a notice shall be issued to holders providing details of the result of the holders' voting at the general



meeting. Subsequently a brief summary of the transactions shall be included in the scheme's next published semi-annual or annual report.

*Note: No announcement shall be required for any connected party transaction falling within 8.9 or 8.10 if the value of such transaction does not exceed HK\$1 million.*

- 8.15 Where connected party transactions falling within 8.9 or 8.10 are carried out by the scheme, a summary disclosure of the total value of such transactions, their nature and the identities of the connected parties shall be made in the annual report of the scheme. Where there is no such transaction conducted during the financial year covered by the annual report, an appropriate negative statement to that effect shall be made in the annual report.
- 8.16 For connected party transactions that do not require holders' approval but are considered by the management company to be material, holders shall be initially informed by way of announcement of the brief details of the transactions, and subsequently through disclosure of the particulars of the transactions in the scheme's next published semi-annual report or annual report.

## Chapter 9: Operational Requirements

### Scheme Documentation

#### *Matters to be Disclosed in Offering Document*

- 9.1 Authorised schemes shall issue an up-to-date offering document when they offer units to the public, containing information necessary for investors to be able to make an informed judgement of the investment proposed to them, and in particular containing the information set out in Appendix B.

#### *English and Chinese Documentation*

- 9.2 All the circulars, notices, announcements, offering documents, and valuation report in relation to the scheme shall be provided in the English and Chinese languages.

#### *Inclusion of Performance Data*

- 9.3 The offering document may disclose the rental yield actually achieved by the real estate at the time the valuation report was made.
- 9.4 A forecast of the scheme's dividend yield is permitted only if it is made on reasonable grounds and on condition that:
- (a) the relevant forecasts are compiled in accordance with the requirements set out in Appendix F, and
  - (b) when results are published relating to the period covered by the forecast dividend yield, the published financial statements shall disclose the relevant figure and account for the discrepancy between the forecast and the actual yield.

*Notes: (1) The dividend yield forecast shall only cover a period of up to two years. The second year covered by the forecast shall not exceed the end of the next fiscal year.*

*(2) The assumptions pertaining to any forecasts and dividend yield calculation shall be clearly stated.*

*(3) There shall be appropriate risk disclosures, including risks that the prospective financial information and the projected yield may not be achieved.*

#### *Contents of Constitutive Documents*

- 9.5 The constitutive documents of a scheme shall contain the information set out in Appendix D. Nothing in the constitutive documents shall provide that the trustee or management company may be exempted from any liability to

holders imposed under any relevant law or breaches of trust through fraud or negligence or willful default, nor may they be indemnified against such liability by holders or at the scheme's expense.

#### *Changes to Scheme Documentation*

- 9.6 The constitutive documents may be altered by the management company and trustee, without consulting holders, provided that the trustee certifies in writing that in its opinion the proposed alteration:-
- (a) is necessary to comply with fiscal or other statutory or official requirements; or
  - (b) does not materially prejudice holders' interests, does not to any material extent release the trustee, management company or any other person from any liability to holders and does not increase the costs and charges payable from the scheme property; or
  - (c) is necessary to correct a manifest error.

In all other cases no alteration may be made except by a special resolution of holders.

#### **Register of Holders**

- 9.7 The trustee or the person so appointed by the trustee shall maintain a register in Hong Kong of holders. The Commission shall be informed of the address(es) where the register is kept. The register shall be open for inspection by holders during business hours. Where the trustee is empowered under the constitutive documents to direct disclosure of any particulars of the holdings of a holder and its associates in the scheme, the trustee shall keep proper records of any particulars obtained under such direction.

#### **Offers of Units**

- 9.8 If an initial offer of units is made, no investment of subscription money can be made until the conclusion of the first issue of units at the initial price.

#### **Meetings**

- 9.9 A scheme shall arrange to conduct general meetings of holders as follows:-
- (a) Holders shall be able to appoint proxies;
  - (b) Votes shall be proportionate to the number of units held or to the value of units held where there are accumulation units;
  - (c) The quorum for meetings at which a special resolution is to be considered shall be the holders of 25% of the units in issue and 10% if only an ordinary resolution is to be considered;

- (d) If within half an hour from the time appointed for the meeting a quorum is not present, the meeting shall be adjourned for not less than 15 days. The quorum at an adjourned meeting will be the number of those holders present at the adjourned meeting in person or by proxy;
- (e) If the possibility exists of a conflict of interest between different classes of holders there shall be provision for class meetings;
- (f) Holders shall be prohibited from voting their own units at, or counted in the quorum for, a meeting at which they have a material interest in the business to be contracted and that interest is different from the interests of all other holders;
- (g) An ordinary resolution may be passed by a simple majority of the votes of those present and entitled to vote in person or by proxy at a duly convened meeting;
- (h) A special resolution may only be passed by 75% or more of the votes of those present and entitled to vote in person or by proxy at a duly convened meeting and the votes shall be taken by way of poll.

*Note: A special resolution shall be required in the event of circumstances specified in this Code, or in such other cases as provided for in the constitutive documents of the scheme.*

- (i) Two or more holders holding not less than 10% of the outstanding units of a scheme shall have the right to requisition a general meeting of the scheme subject to satisfying any quorum requirement laid down by the scheme's constitutive documents.

## **Fees**

- 9.10 The level/basis of calculation of all costs and charges payable from the scheme's property shall be clearly stated in the offering document, with percentages expressed on a per annum basis (see Appendix B). The aggregate level of fees for investment management and property management functions shall also be disclosed.

*Note: Percentage-based transaction fees payable to the management company or any of its connected persons may be disallowed as being inconsistent with the management company's fiduciary responsibility.*

- 9.11 Where appropriate, all fees and expenses (including underwriting fees) incurred in relation to the listing of a scheme shall be disclosed in the offering document.

- 9.12 A performance fee is payable by the scheme, the fee shall be payable:

- (a) no more frequently than annually; and

- (b) if the net asset value per unit exceeds the net asset value per unit on which the performance fee was last calculated and paid (i.e. on a “high-on-high” basis).

9.13 The following fees, costs and charges shall not be paid from the scheme's property:-

- (a) commissions payable to sales agents arising out of any dealings in units of the scheme;
- (b) expenses arising out of any advertising or promotional activities in connection with the scheme;
- (c) expenses which are not ordinarily paid from the property of schemes authorised in Hong Kong; and
- (d) expenses which have not been disclosed in the offering documents or constitutive documents as required by Appendix D.

## Chapter 10: Reporting and Documentation

- 10.1 The management shall keep holders informed of any material information pertaining to the scheme in a timely and transparent manner. The reporting requirements set out in this Code shall not prejudice or affect the application of any listing rules of an exchange on which the scheme is listed, in relation to dissemination of information to investors mandated by such rules.
- 10.2 All announcements, circulars and notices shall be submitted to the Commission for prior approval. Upon such approval, they shall be disseminated to holders as soon as reasonably practicable.

*Note: Announcements shall be published in at least one leading Hong Kong English language and one Chinese language daily newspaper. Other electronic means of publication may also be considered by the Commission.*

### Announcements

- 10.3 The management company shall inform holders as soon as reasonably practicable of any information or transaction concerning the scheme which:
- (a) is necessary to enable holders to appraise the position of the scheme; or
  - (b) is necessary to avoid a false market in the units of the scheme; or
  - (c) might be reasonably expected to materially affect market activity in the scheme or affect the price of the units of the scheme, or
  - (d) requires holders' approval.
- 10.4 The following are examples of information that would require disclosure under 10.3. These examples do not constitute a complete list:
- (a) a material change in the scheme's financial forecast;
  - (b) a valuation of the real estate of the scheme, conducted upon request by the trustee under 4.2(d);
  - (c) issuance of semi-annual or annual report;
  - (d) any connected party transactions, subject to the HK\$1 million threshold in 8.14;
  - (e) a transaction (other than a connected party transaction) the value of which exceeds 15% of the gross asset value of the scheme;
  - (f) a transaction (other than a connected party transaction) for services relating to the real estate of the scheme the value of which exceeds 15% of the aggregate value that the scheme committed to spend or has spent on services relating to real estate of the scheme during the twelve months preceding the relevant transaction;
  - (g) a proposed disposal of real estate within a period of less than two years since acquisition;
  - (h) a proposed change in the management company of the scheme;
  - (i) a proposed change in the general character or nature of the scheme, such as the investment objective and/or policy of the scheme;

- (j) a recommendation or declaration or cancellation of a dividend or distribution;
- (k) issuance of new units (other than units issued pursuant to a dividend reinvestment plan);
- (l) a copy of a document containing market sensitive information or any financial documents that the scheme lodges with an overseas stock exchange (where applicable) or other regulator which is available to the public;
- (m) giving or receiving a notice of intention to undertake a merger or takeover;
- (n) a merger or acquisition;
- (o) a breach of the borrowing limit;
- (p) material litigation;
- (q) a significant dispute or disputes with contractors or with any parties;
- (r) a valuation of the scheme's real estate that has a material impact on the scheme's financial position or performance;
- (s) a major change in accounting policy adopted by the scheme;
- (t) a proposal to change the scheme's auditor;
- (u) a proposal to change the scheme's trustee;
- (v) a proposal to alter the level or structure of fees and charges only if such alteration requires holders' approval;
- (w) a decision or recommendation to request de-authorisation or delisting of the scheme;
- (x) a proposal to terminate the scheme; or
- (y) a proposal to vary the intention stated regarding acquisition of properties within the first 12 months of listing (see Note (3) to 7.1).

10.5 The content of an announcement should contain sufficient quantitative information to enable investors to fully understand the nature and ascertain the implications of the announcement. Information disclosed in the announcement shall be factual, clear, succinct and unbiased.

### **Circulars**

10.6 A circular shall be issued in respect of

- (a) transactions that require, or in the reasonable opinion of the trustee or the management company require, holders' approval; and
- (b) material information in relation to the scheme.

10.7 The following are examples of circumstances in or in relation to which a circular shall be issued. These examples do not constitute a complete list:

- (a) Transactions that require, or that in the reasonable opinion of the trustee or the management company require, holders' approval at a general meeting, including a proposal to:
  - (i) issue new units (other than units issued pursuant to a dividend reinvestment plan) that requires holders' approval under Chapter 12;

- (ii) enter into a merger or acquisition;
  - (iii) enter into a disposal of real estate within a period of less than two years since acquisition;
  - (iv) change the management company of the scheme ;
  - (v) change the general character or nature of the scheme, such as the investment objective and/or policy of the scheme ;
  - (vi) alter the level or structure of fees and charges only if such alteration requires holders' approval;
  - (vii) enter into a connected party transaction which requires holders' approval under Chapter 8; and
  - (viii) request de-authorisation or delisting of the scheme .
- (b) Material information in relation to the scheme includes, but is not limited to:
- (i) a transaction (other than a connected party transaction) the value of which exceeds 15% of the gross asset value of the scheme;
  - (ii) a transaction (other than a connected party transaction) for services performed in relation to the real estate of the scheme the value of which exceeds 15% of the aggregate value that the scheme committed to spend or has spent on services relating to real estate of the scheme during the twelve months preceding the relevant transaction;
  - (iii) a material change in the scheme' s financial forecast;
  - (iv) an issue of new units (other than units issued pursuant to a dividend reinvestment plan) that does not require holders' approval; and
  - (v) a valuation of the real estate of the scheme, conducted upon request by the trustee under 4.2(d) .

10.8 A circular shall be sent within 21 days to holders after the issuance of an announcement. Where a general meeting is to be held, the relevant circular shall be sent to holders 21 days (for special resolution) and 14 days (for ordinary resolution) prior to the day of such meeting.

10.9 The following guidance shall be borne in mind in preparing circulars that are required by the Code:

- (a) the primary objective of the circular is to enable holders to properly and in an informed manner examine the reasonableness and fairness of the proposed transaction. The balance of advantage or disadvantage to the scheme shall therefore be readily apparent to enable a holder to reach his own conclusions on the proposal;
- (b) the circular shall provide sufficient information to holders to evaluate the proposal; and



- (c) where applicable, provide a fair and objective valuation of the relevant real estate of the scheme.

10.10 The circular shall where applicable, at a minimum, contain the full particulars of the transaction or matter disclosed in the announcement to which the circular pertain. The items listed below are not meant to be exhaustive. The Commission may require additional information to be disclosed:

- (a) the date of the transaction and the parties thereto;
- (b) a general description of the nature of the real estate concerned (if any);
- (c) the total consideration and the terms and composition thereof;
- (d) the financing arrangement and justification for such arrangement;
- (e) a description of the impact to the financial position and the capital structure of the scheme in relation to the transactions contemplated in the circular;
- (f) in the case of a new issue, the proposed use of proceeds from the new issue and any other arrangements related to the new issue;
- (g) where applicable, the name of the connected person concerned and of the relevant associate (if any) and details of how the person is connected;
- (h) where applicable, the nature and extent of the interest of the connected person in the transaction;
- (i) where the transaction involves a special purpose vehicle, the particulars of the special purpose vehicle, a general description of its activities, and an accountants' report prepared in accordance with 7.6;
- (j) the date and the location of the general meeting;
- (k) where applicable, an independent valuation in respect of the real estate concerned (if any) prepared in accordance with Chapter 6;
- (l) if the matter pertains to changes to a financial forecast, information set out in Appendix F;
- (m) a statement by the management company of any material adverse change in the financial or trading position of the scheme since the date to which its latest published audited accounts have been made up, or an appropriate negative statement;
- (n) where appropriate, the nature of any resolutions required to approve the transaction and a statement that holders who have a material interest, whether direct or indirect, in the transaction and such interest is different

from the interests of all other holders, will not vote in the general meeting;

- (o) an opinion, in the form of a separate letter, by the trustee or the management company (insofar as it is not conflicted out by virtue of its interest in the transaction) as to whether the transaction is fair and reasonable so far as the holders of the scheme are concerned and such opinion shall set out the reasons for, the key assumptions made and the factors taken into consideration in, forming that opinion;
- (p) for connected party transactions, an opinion prepared in the form of a separate letter by an independent expert acceptable to the Commission, stating as to whether the transaction is fair and reasonable so far as the holders of the scheme are concerned. Such opinion shall set out the reasons for, the key assumptions made and the factors taken into consideration, in forming that opinion;

*Note: Where the transaction is a transaction with a connected person of the scheme, the unit holdings and identities of that particular connected person, and of any holders that have a prospective interest (other than interests via their holdings as holders in the scheme) in the transactions proposed to be entered into by the scheme, shall also be disclosed in the circular.*

- (q) where a transaction is not a connected party transaction, an opinion from an independent expert may be sought by the trustee or the management company after having regard to the interests of the holders and the nature of the transactions e.g. the scheme undergoes restructuring or mergers or other transactions that have a material impact on its financial or commercial interest;
- (r) where the circular includes a statement purporting to be made by an expert, a declaration by such expert of his interest in the scheme;

*Note: The expression "expert" includes engineer, valuer, accountant and any other person whose profession gives authority to a statement made by him.*

- (s) Prominent warning statement:

***“THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION. IF IN DOUBT, PLEASE SEEK PROFESSIONAL ADVICE.”***

- (t) Responsibility statement:

“The management company and its directors collectively and individually accept full responsibility for the accuracy of the information contained in this document and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other

facts the omission of which would make any statement herein misleading.”

(u) Disclaimer statement:

“The Commission takes no responsibility for the contents of this circular, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this circular.”

**Notice**

- 10.11 Holders shall be informed of the results of any holders’ voting at a general meeting by way of a notice.

**Reporting Requirements**

*Reporting to Holders*

- 10.12 At least two reports shall be published in respect of each financial year. Annual reports and accounts shall be published and distributed to holders within four months of the end of the scheme's financial year and semi-annual reports shall be published and distributed to holders within two months of the end of the period they cover. The contents of the annual reports and semi-annual reports shall comply with the requirements set out in Appendix C.

*Reporting to the Commission*

- 10.13 Subsequent to the authorisation of the scheme, all financial reports produced by or for the scheme, its management company and trustee shall be filed with the Commission within the time frame specified in 10.12.
- 10.14 The management company shall supply to the Commission, upon request, all information relevant to the scheme's financial reports and accounts.
- 10.15 The management company shall notify the Commission as soon as practicable of any change to the data in the application form.

**Advertising**

- 10.16 Advertisements and other invitations to invest in a scheme shall be submitted for authorisation prior to their issue or publication in Hong Kong. The general principle is that no advertisement can be made that is false, biased, misleading or deceptive. Any advertisement or announcement which concerns the trustee shall be accompanied by its written consent. Authorisation may be varied or withdrawn by the Commission as it deems fit.
- 10.17 If a scheme is described as having been authorised by the Commission, it shall be stated that authorisation does not imply official approval or recommendation.

10.18 Advertisements and marketing materials shall have proper risk warning statements, including a reference to the offering document of the scheme for a detailed discussion of the risk factors of the scheme.

## Chapter 11: Termination or Merger of a REIT

- 11.1 The scheme may be wound up by the court, otherwise, termination of the scheme shall be subject to holders' approval by special resolution at a general meeting. Where the proposal to terminate the scheme is recommended by the management company, the management company and its connected persons as described in 8.1(e), (f) or (g) shall abstain from voting if they hold interests in the units of the scheme and if their interest in terminating the scheme is different from that of all other holders.
- 11.2 A scheme may be merged with another scheme(s) authorised by the Commission under this Code. Such merger shall follow any procedures set out in the constitutive documents or governing law of both schemes, and shall be subject to holders' approval by special resolution at a general meeting. Where the proposal to merge the schemes is recommended by the management company, the management company and their connected persons as described in 8.1(e), (f) or (g) shall abstain from voting if they hold interests in the units of the scheme(s) and if their interest in merging the schemes is different from that of all other holders.
- 11.3 An announcement on a termination or a merger shall be made as soon as reasonably practicable in accordance with Chapter 10.
- 11.4 A circular shall be served on holders of all the relevant schemes within 21 days of the announcement. The circular shall at least contain information including the following and that required by Chapter 10:
- (a) the rationale for the termination of the scheme or merger of schemes;
  - (b) the effective date of the termination or merger;
  - (c) the manner in which the assets held by the scheme(s) are to be dealt with;
  - (d) the procedures and timing for the distribution of the proceeds (in the case of termination) or issuance or exchange of new units (in the case of a merger) arising therefrom;
  - (e) a valuation report for each relevant scheme prepared in accordance with Chapter 6;  
*Note: The date of the valuation report shall be a date which is not more than three months before the date of which the circular.*
  - (f) the alternatives available to investors (including, if possible, a right to switch without charge into another authorised scheme);
  - (g) the estimated costs of the termination or merger and who is expected to bear these costs; and
  - (h) such other material information that the holders should be informed of.
- 11.5 A notice shall be sent to holders informing them of the result of the holders' voting at the general meeting.
- 11.6 Upon holders' approval of the termination of the scheme or merger of schemes, the scheme(s) shall cease to create, cancel or sell units. No transfer

of the units may be registered and no other change to the register of holders may be made without the sanction of the trustee(s).

11.7 The terminating scheme shall not make further investments. The obligations of the trustee, the management company and the property valuer shall continue until the scheme is dissolved.

11.8 In the case of termination, the trustee shall oversee, as soon as practicable after the scheme falls to be wound up, the realisation of the real estate of the scheme by the management company, and ensure that, after paying all outstanding liabilities and providing adequate provisions for liabilities, the proceeds of that realisation are distributed to the holders proportionately to their respective interests in the scheme at the date of the termination of the scheme.

*Notes: (1) All real estate held by the scheme shall be disposed of through public auction or any form of open tender. The disposal shall be conducted at arm's length and in the best interests of the holders. The disposal price shall be the best available price obtained through public auction or open tender.*

*(2) The trustee shall ensure that the liquidation exercise is completed within twelve months from the date the termination takes effect. Where the trustee considers it is in the best interests of the holders, the liquidation exercise may be completed for such longer period (in total not to exceed twenty four months) as the trustee deems appropriate. Holders shall be informed by way of announcement.*

*(3) All cash proceeds derived from the liquidation of the scheme shall be distributed to holders on a pro rata basis. Where the liquidation exceeds six months, an interim distribution shall be made in respect of the sale proceeds received by the end of every six-month period, except where no sales were made during such period. Upon completion of the liquidation, a one-off distribution shall be made within one month from the date of completion.*

*(4) Distributions to holders upon termination of the scheme shall be made in cash only.*

11.9 Subject to any order of the court, while a scheme is being wound up, the scheme shall continue to prepare its annual or semi-annual report, whichever is applicable.

11.10 On completion of the liquidation of the scheme or merger of schemes, the following shall be prepared:

(a) the management company's review and comments on the performance of the scheme, and an explanation as to how the real estate has been

disposed of, the transaction prices and major terms of disposal, in the case of termination, and how the real estate has been accounted for in the merged scheme, in the case of a merger;

- (b) a trustee's report that the management company has managed and liquidated the fund in accordance with the Code and the provisions of the trust deed, in the case of a scheme liquidation, or that the management company has managed and merged the scheme in accordance with the Code and the provisions of the trust deed, in the case of a merger of schemes;
- (c) financial statements of the scheme (see Appendix E for content requirements); and
- (d) an auditors' report (see Appendix E for content requirements).

11.11 Copies of the financial statements shall be distributed to holders within three months of the completion of the liquidation or merger and a copy shall be filed with the Commission.

11.12 Where the scheme undertakes any form of merger, takeover, amalgamation and restructuring other than a termination as stated in 11.1, the scheme's trustee and/or management company shall as soon as practicable consult with the Commission on the manner in which such activities could be carried out so that it is fair and equitable to all holders.

## Chapter 12: Issue of New Units

12.1 A scheme shall be so structured as to enable a holder to protect his proportion of the total units held by having the opportunity to subscribe for any new issue of units. Accordingly, unless the Code otherwise permits, all issues of units by the scheme shall be offered to the existing holders pro rata to their existing holdings, and only to the extent that the units offered are not taken up by such holders may they be allotted or issued to other persons or otherwise than pro rata to their existing holdings.

12.2 If new units are not offered to holders on a pro rata basis, holders' approval by way of ordinary resolution at a general meeting is required, unless the aggregate number of new units issued under this 12.2 during the financial year does not increase the total number of units outstanding at the end of the previous financial year by more than 20% (or such lower amount as may from time to time be specified by the Commission)

*Notes: (1) New units may be issued to independent third parties in exchange for real estate under this 12.2.*

*(2) Where units to be issued under this 12.2 are issued*

*(a) to a connected person; or*

*(b) in relation to a connected party transaction that requires holders' approval under Chapter 8;*

*then notwithstanding that these new units may fall within the 20% threshold, the issue of units in the case of (a), or the transaction in the case of (b), shall require the approval of holders by way of ordinary resolution at a general meeting. An announcement, a circular and a notice shall be issued in accordance with Chapter 10. Units issued as a result of such approval shall be included in the calculation of 20% for all other purposes under this 12.2.*

12.3 Where the scheme issues new units on a pro rata basis, and the issue increases the market capitalization of the scheme by more than 50%, holders' approval by way of ordinary resolution at a general meeting is required. An announcement, a circular and a notice shall be issued in accordance with Chapter 10.

*Note: Any units issued (other than those issued under 12.2) in the preceding 12 months shall be aggregated for the purpose of calculating the 50% limit.*

12.4 Where a holder may increase his holdings of units in the scheme by more than his pro rata entitlement upon completion of an issuance of units, the holder shall abstain from voting in relation to such unit issuance.



- 12.5 Where applicable, the management company and its connected persons shall abstain from voting in relation to any unit issuance.

### Overseas Regimes Acceptable to the Commission

Management companies in the following jurisdictions are regarded as subject to an acceptable inspection regime acceptable to the Commission and may be considered as approved management companies under 5.3 of this Code. As a general guide, the Commission looks to the following matters in determining the acceptability of an overseas management company:

- (a) the management company is licensed by an overseas regulator who carries out inspections of the management company (including its activities in relation to REITs or schemes of a similar nature) within its jurisdiction in a manner generally consistent with that of the Commission; and
- (b) the Commission and the overseas regulator concerned have satisfactory procedures for the timely exchange of information regarding the management company.

The regulators of management companies in respect of the following overseas jurisdictions are regarded as acceptable to the Commission:

<b>Jurisdiction</b>	<b>Regulator</b>
Australia	Australian Securities & Investments Commission (ASIC)
Germany	Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) (German Financial Supervisory Authority)
Ireland	Financial Services Regulatory Authority
Luxembourg	The Commission de Surveillance du Secteur Financier (CSSF)
United Kingdom	Financial Services Authority (FSA)

**Information in the Offering Document**

This list is not intended to be exhaustive. The management company is obliged to disclose any information which may be necessary for investors to make an informed judgement.

*Constitution of the Scheme*

**B1** Name, registered address and place and date of creation of the scheme.

*Investment Objectives and Restrictions*

**B2** The offering document of the scheme shall clearly include:

- (i) the investment policy and strategy of the scheme;
- (ii) the proposed use of the monies raised from the public offering of the units in the scheme and any business plan for the scheme;
- (iii) the scope and type of investments made or intended to be made by the scheme, including the type(s) of real estate (e.g. residential/commercial/industrial);
- (iv) the location and the general character and competitive conditions of all real estate now held or intended to be acquired by the scheme;
- (v) any proposed program for renovation or improvement to the real estate, including the estimated costs thereof and the method of financing to be used;
- (vi) the operating data of each of the real estate, including the occupancy rate, number of tenants and its mix in terms of occupation or business, principal provisions of the leases, average annual rental per square foot, and schedule of lease expirations for the next five years;
- (vii) the borrowing policy and the method or proposed method of operating and financing the scheme's real estate investments;
- (viii) the investment risks of the scheme;
- (ix) the dividend policy;
- (x) the insurance arranged for the scheme ;
- (xi) a statement with respect to any material policy regarding real estate activities; details of transactions or agreements entered into with connected parties;

- (xii) full particulars of the nature and extent of the interest, if any, of any director of the trustee, the management company, the property valuer or any other connected persons to the scheme, in the property owned or proposed to be acquired by the scheme; and where the interest of such a director consists in being a partner in a firm, the nature and extent of the interest of the firm, with a statement of all sums paid or agreed to be paid to him or the firm for services rendered to the scheme;
- (xiii) a valuation report prepared by a property valuer in accordance with Chapter 6 with respect to all the scheme's interest in real estate, including particulars of each property owned by the scheme or contracted for purchase by the scheme;

*Note: If the scheme has obtained more than one valuation report regarding any of its real estate within six months before the issue of the offering document, then all other such reports shall be included.*

- (xiv) particulars of any bank overdrafts or similar indebtedness of the scheme, or if there is no such indebtedness, a statement to that effect; and

**B3** If the nature of the investment policy so dictates, a warning that investment in the scheme is subject to abnormal risks, and a description of the risks involved.

#### *Operators and Principals*

**B4** The names, registered addresses and responsibilities of the parties involved in the management, operation and valuation of the scheme, including the following parties (where applicable):

- (a) the management company;
- (b) the trustee;
- (c) delegates of the management company;
- (d) the property valuer;
- (e) the auditor; and
- (f) the registrar.

#### *Significant Holders*

**B5** The names of the significant holders and the number of units held and deemed to be held by each of them; or the identity of investors each of whom has agreed to subscribe to 10% or more of the scheme, and the number of units each of them has agreed to subscribe for.

**B6** The minimum period that each of the significant holders intends to hold the units after the scheme becomes authorised.

### *Characteristics of Units*

- B7** Minimum investment and subsequent holding (if any).
- B8** A description of the different types of units, including their currency of denomination.
- B9** Form of certification.
- B10** Proforma net asset value per unit upon completion of fundraising.

### *Application Procedures*

- B11** Procedure for subscribing units.
- B12** Statement that no money shall be paid to any intermediary in Hong Kong who is not licensed or registered to carry on Type 1 regulated activity under Part V of the Securities and Futures Ordinance.

### *Distribution Policy*

- B13** The approximate dates on which dividends will be paid.

### *Fees and Charges*

- B14** (a) The levels of all fees and charges payable by an investor (see 9.10 to 9.13), including all charges levied on subscription and conversion;
- (b) The levels of all fees and charges payable by the scheme, including management fees, trustee fees, start-up expense and fees in relation to listing (including underwriting fees, where applicable); and
- (c) The notice period for fee increases.

*Note: In the case of indeterminable fees and charges, the basis of calculation or the estimated ranges shall be disclosed.*

### *Taxation*

- B15** Details of Hong Kong and principal taxes levied on the scheme's income and capital, including tax, if any, deducted on distribution to holders.

### *Reports and Accounts*

- B16** The date of the scheme's financial year.
- B17** Particulars of what reports will be sent to holders and when (including those in 10.12).

**B18** A yield forecast may be incorporated into the offering document, subject to the requirements stated in Appendix F.

*Warnings*

**B19** Statements/warnings shall be prominently displayed in the offering document as follows:-

- (a) "Important - if you are in any doubt about the contents of this offering document, you shall seek independent professional financial advice".
- (b) A statement to the effect that the rental yield on real estate held by the scheme is not equivalent to the yield on the units.

**B20** A statement to explain:

- (a) the current rental receipts and that yields may not be sustained;
- (b) the value of the property may rise as well as fall; and
- (c) the property valuations are estimates made in accordance with the "Hong Kong Guidance Notes on the Valuation of Property Assets" published by the Hong Kong Institute of Surveyors.

**B21** A statement to explain the investment characteristics and risk profile of the scheme.

*Expert Statement*

**B22** Where the offering document includes a statement purporting to be made by an expert, a statement that he has given his consent to the issue of the offering document with the statement included in the form and context in which it is included.

**B23** In B22 above, the expression "expert" includes engineer, valuer, accountant and any other person whose profession gives authority to a statement made by him. For the purposes of B22 a statement shall be deemed to be included in a offering document if it is contained therein or in any report or memorandum appearing on the face thereof or by reference incorporated therein or issued therewith.

*General Information*

**B24** A list of constitutive documents and an address in Hong Kong where they can be inspected free of charge or purchased at a reasonable price.

**B25** The date of publication of the offering document.

**B26** A statement that the management company and its directions accept responsibility for the information contained in the offering document as being accurate at the date of publication.

**B27** Details of unauthorised schemes shall not be shown in the offering document. Where names of such schemes are mentioned, these shall be clearly marked as unauthorised and not available to Hong Kong residents.

**B28** Details of listing procedures and special information relating to listing.

*Termination of Scheme*

**B29** A summary of the circumstances in which the scheme can be terminated.

*Merger of Scheme*

**B30** A summary of the circumstances in which the scheme can be merged with another scheme(s).

*Accompaniment to the Offering Document*

**B31** The offering document shall be accompanied by:

- (a) the scheme's most recent audited annual report and accounts (where applicable);
- (b) the scheme's semi-annual report if published after the annual report (where applicable); and
- (c) a valuation report prepared by a property valuer that meets the qualification requirements stated in Chapter 6. The effective date as at which the real estate was valued shall not be more than three months before the date on which the offering document is issued and the valuation report shall comply with the requirements of Chapter 6.

**B32** No application form may be supplied to any person not a holder unless accompanied by the offering document, except that an advertisement or report containing all the requirements in this Appendix may be allowed to incorporate an application form.

### Contents of Financial Reports

The annual report shall contain, at a minimum, the following:

1. Manager's discussion and analysis of financial conditions and results of operations, explanation of any potential conflicts of interest and the manner in which they are dealt with; and discussions on the strategy, plans and operations for the coming year;
2. Summary of all real estate sales and purchases as well as connected party transaction(s) entered into during the relevant period;
3. Valuation report as described in Chapter 6;
4. Trustee's report as required under 4.2;
5. A report of the names of the top five real estate agents and contractors engaged by the scheme during the financial year, based on the value of commissions paid or the value of the service contracts. Such report shall include a breakdown of the consideration attributable to each of the agents or contractors by way of figures and percentages, and a description of the services/works contracted for;
6. Holdings of each of the connected persons to the scheme;
7. Number of new units issued;
8. A set of financial statements comprising:
  - (a) Balance sheet;
  - (b) Income statement;
  - (c) Cash flow statement;
  - (d) Distribution statement;
  - (e) Statement of movements in capital account;
  - (f) Comparative figures for the statements referred to in (a) to (e) above inclusive for the corresponding previous period;
  - (g) Accounting policies and explanatory notes;
  - (h) Auditor's report; and
  - (i) Performance table.

*Note: Financial statements of a REIT are required to conform with either:*

- (i) *Accounting standards approved by the Hong Kong Society of Accountants and laid down in the Statements of Standard Accounting Practice issued from time to time by that Society; or*
- (ii) *International Accounting Standards ("IAS") as promulgated from time to time by the International Accounting Standards Committee. Schemes which adopt IAS, are required:-*



- *to disclose and explain differences of accounting practice between IAS and generally accepted accounting principles in Hong Kong, which have a significant effect on their financial statements; and*
- *to compile a statement of the financial effect of any such material differences.*

The semi-annual report shall contain, at a minimum, the following:

1. Manager's discussion and analysis of financial conditions and results of operations, and discussions on the outlook for the coming half-year;
2. List of real estate held by the scheme;
3. Summary of real estate sales and purchase, as well as connected party transactions during the interim period;
4. Holdings of each of the connected persons to the scheme;
5. Number of new units issued; and
6. Performance table.

### **Balance Sheet**

The Balance Sheet shall separately disclose, where applicable, at least the following items:

1. Total value of real estate
2. Cash and cash equivalents
3. Rentals and other receivables
4. Amounts receivable on subscription
5. Bank loans and overdrafts or other forms of borrowings
6. Distributions payable
7. Total value of all assets
8. Total value of all liabilities
9. Revaluation reserve
10. Net asset value

11. Number of units in issue
12. Net asset value per unit

### **Income Statement**

The income statement shall separately disclose, where applicable, at least the following items:

1. Gross rental income from real estate
2. Other income, broken down by category
3. Deficit/Surplus on revaluation taken to the Income Statement during the accounting period
4. Profit or loss on disposal of any investment real estate
5. Equalization on issue and cancellation of units
6. An itemized list of various expenditure charged to the scheme including:
  - (a) fees paid to the management company
  - (b) remuneration of the trustee
  - (c) fees paid to delegates of the management company
  - (d) fees paid to property valuer
  - (e) other amounts paid to any connected persons of the scheme
  - (f) interest on borrowings
  - (g) directors' fee and remuneration
  - (h) safe custody and bank charges
  - (i) auditors' remuneration
  - (j) legal and other professional fees
  - (k) commission paid to property agents
7. Taxes
8. Amounts transferred to and from the capital account
9. Net income for distribution

### **Cash Flow Statement**

The cash flow statement shall include:

1. Cashflows from operating activities;
2. Cashflows from investing activities; and
3. Cashflows from financing activities

### **Distribution Statement**

The distribution statement shall separately disclose, where applicable, at least the following items:

1. Net after tax income for the period
2. Interim distribution per unit and date of distribution
3. Final distribution per unit and date of distribution

### **Statement of Movements in Capital Account**

The statement of movements in capital account shall separately disclose, where applicable, at least the following items:

1. Value of the scheme as at the beginning of the period
2. Number of units issued and the amounts received upon such issuance (after equalization if applicable).
3. Any items resulting in an increase/decrease in value of the scheme including:
  - (a) surplus/loss on sale of real estate
  - (b) exchange gain/loss
  - (c) unrealised appreciation/diminution in value of real estate
  - (d) net income for the period less distribution
4. Amounts transferred to and from the Income Statement
5. Value of the scheme as at the end of the period

### **Notes to the Accounts**

The following matters shall be set out in the notes to the accounts:

1. Principal Accounting Policies
  - (a) in respect of real estate, the basis of valuation, the treatment of changes in their value and the treatment of any revaluation on their sale;
  - (b) the revenue recognition policy regarding rental income, dividend income and other income;
  - (c) the basis of treatment of formation costs;
  - (d) taxation; and

- (e) any other accounting policy adopted to deal with items which are judged material or critical in determining the transactions and in stating the disposition of the scheme

Any changes to the above accounting policies and their financial effects upon the accounts shall also be disclosed.

## 2. Transactions with Connected Persons

The following shall be disclosed:

- (a) a description of the nature of any transactions entered into during the period between the scheme and the management company, the property valuer of the scheme or any entity in which those parties or their connected persons have a material interest, and a statement confirming that these transactions have been entered into in the ordinary course of business and on normal commercial terms;
- (b) details of all transactions which are outside the ordinary course of business or not on normal commercial terms entered into during the period between the scheme and the management company, or any entity in which these parties or their connected persons have a material interest;
- (c) name of the management company, the director of such entities or any connected persons of such entities or director who is entitled to profits from transactions in units or from management of the scheme, and the amount of profits to which each of them becomes entitled;
- (d) where the scheme does not have any transactions with connected persons during the period, a nil statement to that effect; and
- (e) the basis of the fee charged for the management of the scheme and the name of the management company.

## 3. Borrowings

State whether the borrowings are secured or unsecured and the duration of the borrowings.

## 4. Commissions

Commission paid to top five real estate agents and value of service contracts of the top five contractors engaged by the scheme during the year.

## 5. Contingent Liabilities and Commitments

Details of any contingent liabilities and commitments of the scheme.

- 6. If the free negotiability of any asset is restricted by statutory or contractual requirements, this shall be stated.

## **Contents of the Auditors' Reports**

Two reports shall be prepared by the auditor, namely:

1. An auditor's report on compliance with the regulatory requirements, in which the auditor expresses an opinion as to whether the financial statements prepared for that period have been properly prepared in accordance with the relevant provisions of the trust deed and the Code; and
2. An auditor's report on the financial statements, in which the auditor expresses an opinion as to whether the financial statements give a true and fair view of the disposition of the scheme at the end of the period and of the transactions of the scheme for the period then ended;

If the auditor is of the opinion that proper books and records have not been kept by the scheme and/or the financial statements prepared are not in agreement with the scheme's books and records, that fact should be stated in the auditors' report in (2) above.

If the auditor has failed to obtain all the information and explanations which, to the best of his knowledge and belief, are necessary for the purposes of the audit, that fact should be stated in the auditors' report in (2) above.

### **Performance Table**

A comparative table covering the last 5 financial years or since launch, whichever is later, and including, for each financial year:-

- (a) the total net asset value at the end of the financial year;
- (b) the net asset value per unit at the end of the financial year;
- (c) the highest premium or discount of the traded price to net asset value; and
- (d) the net yield per unit at the end of the financial year.

*Note: A performance table prepared for a semi-annual report shall include (a) to (d) for the relevant interim period.*

### Contents of the Trust Deed

The trust deed of a scheme shall be submitted to the Commission for prior approval. It shall, at a minimum, contain all the information listed in this Appendix. The items listed are not meant to be exhaustive, the Commission may require additional information to be disclosed in the Trust Deed.

1. Name of Scheme
2. Participating Parties

A statement to specify the participating parties such as the management company and the trustee.
3. The scheme is subject to and governed under the laws of Hong Kong
4.
  - (a) A statement that the deed is binding on each holder as if he had been a party to it and so to be bound by its provisions and authorises and requires the trustee and the management company to do as required of them by the terms of the deed.
  - (b) A provision that a holder is not liable to make any further payment after he had paid the purchase price of his units and that no further liability can be imposed on him in respect of the units which he holds.
  - (c) A declaration that the assets of the scheme is held by the trustee on trust for the holders of the units *pari passu* according to the number of units held by each holder.
5. Trustee
  - (a) A statement to set out the obligations of the trustee as set out in Chapter 4.
  - (b) A statement that the trustee shall retire in the manner as stipulated in Chapter 4.
  - (c) A statement to empower the trustee to require holders to disclose to it upon its request, their beneficial interests in the scheme.
  - (d) A statement to requiring a holder to promptly disclose to the trustee when the holder becomes a significant holder.
6. Management Company
  - (a) A statement to list the obligations of the management company including (see Chapter 5):
    - (i) its general obligations with respect to the scheme;

- (ii) its obligations with respect to the delegation of functions;
- (iii) its obligations with respect to the scheme that is seeking a listing on an exchange; and
- (iv) appointment of auditor.

(b) A statement that the management company shall retire as set out in Chapter 5.

#### 7. Investment Limitations and Dividend Policy

The following shall be specified (see Chapter 7):

- (a) core investment requirements;
- (b) criteria for using special purpose vehicles;
- (c) minimum holding period for the scheme's real estate assets;
- (d) limitations on borrowing; and
- (e) the income distribution policy/mechanism of the scheme and approximate date when income will be distributed.

#### 8. Valuation

The following rules on valuation shall be stated:-

- (a) the method of determining the value of the assets and liabilities of the scheme and the net asset value accordingly; and
- (b) the frequency of valuing the assets and liabilities of the scheme (see Chapter 6).

#### 9. Issuance of Announcement, Circular and Notice

- (a) A statement that the management company shall keep holders informed of any material information pertaining to the scheme in a timely and transparent manner as set out in Chapter 10.
- (b) A statement that the management company shall inform its holders by way of announcement as soon as reasonably practicable of any information concerning the scheme which:
  - (i) is necessary to enable holders to appraise the position of the scheme;
  - (ii) is necessary to avoid a false market in the units of the scheme; or
  - (iii) might be reasonably expected materially to affect market activity in and the price of the units of the scheme (see 10.3 and 10.4); and
  - (iv) requires holders' approval.
- (c) A statement that sets out the situations under which the management company shall send circulars to holders (see Chapter 10).
- (d) A statement that sets out the situations under which the management company shall send notices to holders (see Chapter 10).

- (e) A statement that lists out the procedures that the management company shall follow in issuing announcements, circulars and notices to holders.

#### 10. Issuance of Units

The following shall be stated:

- (a) The procedures that a scheme should follow when new units are issued (see Chapter 12).
- (b) The method of determining the issue price.

#### 11. Fees & Charges

The following shall be stated:-

- (a) the maximum percentage of the initial charge (if any) payable to the management company out of the issue price of an unit;
- (b) the maximum fee payable to the management company out of the assets of the scheme, expressed as an annual percentage;
- (c) fee payable to trustee;
- (d) fee payable to property valuer;
- (e) preliminary expenses to be amortized against the assets of the scheme; and
- (f) all other material fees and charges payable out of the property of the scheme.

#### 12. Meetings

Provisions on the manner in which meetings are conducted in accordance with 9.9; and on the circumstances under which meetings are to be held.

#### 13. Transactions with Connected Persons

The following shall be stated:-

- (a) Cash forming part of the scheme's assets may be deposited with the trustee, the management company, the property valuer of the scheme or with any other connected persons (being an institution licensed to accept deposits) so long as that institution pays interest on the deposit at a rate not lower than the prevailing commercial rate for a deposit of that size and term.
- (b) money can be borrowed from the trustee, the management company, the property valuer of the scheme or any other connected persons (being an



institution licensed to lend money) so long as that institution charges interest at no higher rate, and any fee for arranging or terminating the loan is of no greater amount than the prevailing commercial rate for a loan of the size and nature of the loan in question negotiated at arm's length.

(c) All transactions carried out by or on behalf of the scheme shall be:

(i) carried out at arm's length;

*Note: The management company shall ensure that all transactions are carried out in an open and transparent manner. Where circumstances permit, transactions shall be carried out by way of open tender or competitive bidding by auction.*

(ii) valued, in relation to a property transaction, by an independent valuer that meets the requirements of Chapter 6;

(iii) consistent with the investment objectives and strategy of the scheme; and

(iv) in the best interests of holders.

(d) any transactions between the scheme and any of its connected persons shall be carried out in accordance with the requirements set out in Chapter 8.

#### 14. Annual Accounting Period

Calendar year date on which the annual accounting period of the scheme ends.

#### 15. Base Currency

A statement of the base currency of the scheme.

#### 16. Modification of the Trust Deed

A statement of the means by which modifications to the trust deed can be effected (see Chapter 9).

#### 17. Termination of Scheme

(a) A statement of the circumstances in which the scheme can be terminated.

(b) A statement to list the procedures that are to be followed upon termination of the scheme (see Chapter 11).

#### 18. Merger of Scheme

A statement to list the procedures that are to be followed upon the merger with another scheme(s) (see Chapter 11).

**Contents of Financial Statements for Liquidation or Merger of Schemes**

The financial statements prepared for the purpose of the liquidation of a scheme or merger of schemes shall at least contain the following:

1. revenue statement;
2. statement of assets and liabilities, which shall include a separate disclosure of the net asset value of the scheme(s) as at the date of termination or merger and the relevant net asset value per unit;
3. a distribution statement; and
4. a statement of movements in capital account.

**Contents of Auditor's Reports on Financial Statements for Liquidation or Merger of Schemes**

Two reports shall be prepared by the auditor, namely:

1. An auditor's report on compliance with the regulatory requirements, in which the auditor states whether or not the management company has conducted the liquidation or the merger in accordance with the Code and the trust deed;
2. An auditor's report to state that the financial statements prepared for purpose of the liquidation / merger of the scheme(s) has been properly prepared from the books and record of the scheme(s).

If the auditor is of the opinion that proper books and records have not been kept by the scheme and/or the financial statements prepared are not in agreement with the scheme's books and records, that fact should be stated in the auditor's report in (2) above.

If the auditor has failed to obtain all the information and explanations which, to the best of his knowledge and belief, are necessary for the purposes of the audit, that fact should be stated in the auditor's report in (2) above.

### Preparation and Presentation of Forecast

No forecast of profits or dividends based on an assumed future level of profits may be made, unless it is made on reasonable grounds and supported by a formal profit forecast.

The forecast shall cover a period which is coterminous with the scheme's financial year-end. If, exceptionally the forecast period ends at a half year-end, the Commission will require an undertaking from the management company that the interim report for that half year will be audited. Forecast periods not ending on the financial year end or half year-end will not be permitted.

*Note: A forecast may be provided for the next financial year only if the management company reasonably believes that such forecast is compiled in accordance with the principles and requirements set out in this Appendix.*

The principal assumptions underlying the forecast, including commercial assumptions, upon which it is based, shall be stated. The assumptions shall be specific and precise, and readily understandable by investors. Such assumptions shall draw the investors' attention to, and where possible quantify, those uncertain factors which could materially disturb the ultimate achievement of the forecast. The assumptions shall not relate to the general accuracy of the estimates underlying the forecast. Any statement or information relating to the forecast shall be clear and unambiguous. Assumptions and limits regarding the prospective financial information shall be disclosed in a way that is no less prominent than the forecast itself.

Rental income, which forms a material element of the forecast, shall be examined and reported on by the valuer and its report shall be set out.

The accounting policies and calculations for the forecast shall be reviewed and reported on by the auditor and its report shall be set out.

The forecast and the assumptions on which it is based are the sole responsibility of the management company. The management company shall ensure that it exercises due care and consideration in the compilation of the forecast, and that sufficient information is disclosed to enable investors to interpret the forecast and to form a view as to its reasonableness. The management company shall report in addition that it has satisfied itself that the forecast has been stated after due and careful enquiry, and such report shall be set out.

There should be appropriate risk disclosures, including risks that the prospective financial information will not be achieved.