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19 January, 2006

Dear Mr Swan,

## **UK Real Estate Investment Trusts (REITs)**

I am writing to represent the interests of private investors in relation to the proposals issued on 14 December last. I am able to do so as UKSA is the leading independent organisation representing the interests of private shareholders in the U.K. We welcome the proposal to allow REITs which will be vehicles that permit private investors to acquire tax-neutral investments in mixed portfolios of properties. We also agree that they should be limited to close-ended companies traded on a recognised stock exchange.

However, we have several points arising from the documents on which we wish to comment:

### **Percentage limits**

We observe in the consultative papers a number of instances where percentage limits are proposed. We are not qualified to make detailed comments on these. However, it is a matter of considerable concern that such limits on the qualification of companies should neither (a) discourage the adoption of REIT status nor (b) impose undue restrictions on their operation. We ask that each such limit be carefully reconsidered to see whether it is absolutely necessary. In particular we consider that the 95% limit in draft clause 5(7) is too high and suggest 90%.

It is essential that the operation of the free market cannot force a change of status on a REIT outside the control of the Directors and shareholders. If, for example, the Government decides, despite representations to the contrary, that the 10% limit on an individual shareholding must be retained, then any adverse consequence of a breach must fall on the shareholder who has gone above the 10% limit and not on the REIT. Equally it is important that movements in the market values of properties held shall not, on their own, be able to jeopardise the status of a REIT.

The limits must not operate to inhibit the flexibility of companies to manage their portfolios efficiently. For example it seems possible that section 5(6)(b) of the draft Clauses could exclude properties that are in the process of being refurbished. If this is a correct interpretation it could deter REITs from refurbishing their properties.

**UKSA—The independent voice of the private shareholder**

The United Kingdom Shareholders' Association Limited

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### **Conversion charge**

The 2004 and 2005 consultations both referred to a *conversion charge* but we note that the current papers use the term *entry charge* and speak of it *applying to companies joining the regime*. The significance of the change is not explained. However, since one of the objects of the proposed legislation is to put investors in the same position as if they invested in property directly, there can be no justification for an entry charge on a newly-created REIT. It would appear from the 2005 consultation that it is only in respect of potential loss of capital gains tax that a conversion charge is felt necessary. It is clearly essential that this be set at such a level that it does not discourage conversion. Assuming that the expected benefits to the economy are realised, they will of themselves generate more revenue for the Exchequer.

In the light of the re-iterated sentiment that there shall be no overall cost to the Exchequer, we trust that there is no question of the Treasury seeking compensation for losing the benefit of double taxation on existing property companies (see 2.7 of 2005 consultation). This would clearly put them at a disadvantage compared with newly-created REITs and would be a matter of the Treasury seeking to eat its cake and have it.

### **Tax-exempt funds**

Part 1 of the consultative papers makes it plain that shares in REITs will be eligible for inclusion in ISAs, PEPs and Child Trust Funds. Will the Government please clarify at an early stage whether tax deducted on distributions is to be reclaimable by such funds. Equality of treatment with property held directly in pension funds demands that pension funds and SIPPs that invest in REITs shall be able to reclaim tax deducted.

### **Regulatory regime**

In the 2004 consultation the intended regulatory regime was referred to in passing at para 2.14 but the only mention of this in the current papers is in 1. ii. of Part 4 which speaks of *a stable and well regulated basis*. We regard it as essential that a proper regulatory regime is planned and in operation before any REITs are launched. We note that the Treasury has already decided in relation to conventional investment trusts to continue to rely on the FSA's listing rules (Government response November 2005). However, we believe that property provides a fertile field for mis-selling and adequate protection for the small investor is an imperative.

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We should be very pleased to discuss or amplify any aspects of these comments. Should you have any queries would you kindly contact Roy Colbran who chairs our Company Law Reform working group at roycolbran@aol.com

Yours sincerely

David Blundell  
Chairman