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FEATURE HAVING THE REIT APPROACH

REIT developments in Saudi Arabia and the UAE

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HAVING THE REIT APPROACH

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There have recently been significant developments in the regional Real Estate Investment Trust (REIT) market, including the first industrial and commercial REIT in Dubai and the first REIT with guaranteed returns in Saudi Arabia. **Nabil Issa, James Stull, Sayf Shuqair and Hamzeh Al Rasheed** of King & Spalding LLP look at the impact of changes on market trends.

WHAT'S HAPPENED?

“A UAE conglomerate has announced the launch of its private Real Estate Investment Trust or REIT known as Manre which will be a Property Fund and a Real Estate Investment Trust for qualified investors in Dubai,” Nabil Issa explains.

“This has been set up in line with DFSA legislation and aims to raise about 330 million AED as part of its strategy to acquire additional rent-yielding commercial assets. It is significant as it is the first industrial and commercial REIT in Dubai.”

“REITs have also been making news in Saudi Arabia where MEFIC Capital has launched the first

REIT with guaranteed returns. Their REIT is valued at 1.23 billion Saudi Riyals and the company plans to list 879.5 million Riyals of the fund's units on the Saudi Stock Exchange (Tadawul).”

“This will mean this REIT will have the largest public offering in Saudi Arabia,” Issa adds.

“The Fund will give investors access to the Saudi and UAE real estate markets through eight properties and will be open to Saudi citizens or companies with an exclusive Saudi presence. Its management fees will also be the lowest in the market at 0.35% and there is a guaranteed minimum 2% annual return if it doesn't meet the 5% investment threshold.”

“There are now 16 listed REITs in Saudi Arabia and



the UAE worth approximately US\$2 billion and more are to be listed in the future. In both jurisdictions investors are attracted by a retail product which delivers consistent yields, while providing an upside if the asset increases in value at the time of exiting the properties. In addition, while land is generally not liquid, listed REITs are tradable," James Stull notes.

SAUDI ARABIA

"Saudi Arabia does not currently allow for trusts although it has implemented a REIT regime and allows for real estate exchange traded funds, which are listed real estate funds which operate in a similar way to real estate investment trusts in other jurisdictions."

"REITs in Saudi Arabia are governed by the Real Estate Investment Funds Regulations, the REIFR and the Real Estate Investment Traded Funds Instructions, or REIT Instructions issued by the Capital Market Authority. Under the REIFR and REIT Instructions, a REIT is structured in a way which represents a contractual relationship between an investor and a Capital Market Authority licensed fund manager in respect of an investment in a listed real estate investment fund."

"The main contractual document governing the relationship between an investor and a licensed fund manager is the Terms and Conditions, which is similar to an Information Memorandum or a prospectus," Sayf Shuqair adds.

"The diversification of REITs in the market varies considerably with some owning a single asset and others owning up to ten assets, like the Riyadh REIT which has recently completed its capital increase to acquire additional assets including the Burj Rafal Kempinski Hotel in Riyadh. There are a number of large, diversified REITs in the market which have acquired assets in various sectors including the commercial, retail, hospitality and residential sectors, while some other REITs with more specialised assets have concentrated on a single sector (although most of the single asset REITs are looking to acquire additional assets)," Shuqair notes.

"As an income generating investment product, a REIT in Saudi Arabia is required to invest no less than 75% of its total asset value in income generating real estate and distribute no less than 90% of its net profits



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to investors. In addition, the minimum amount to be raised from the public is 500 million Riyals with at least 30% of a REIT's units being owned by the public who must consist of at least 200 unitholders," Stull adds.

"The Saudi Capital Market Authority has recently introduced amendments to the REIT Instructions. These amendments introduce additional requirements and codify various practices. The amendments include the minimum amount which needs to be raised from the public being increased from 100 million to 500 million Riyals. While revenues obtained from a single tenant have been capped at 25% of the REIT's total asset value in order to mitigate revenue concentration risk. Investors who invest in the REIT by way of an in-kind contribution upon establishment are also restricted from trading their units in the REIT for one year from the date of listing. In addition, related parties are able to trade their units in the REIT

and are exempt from a restriction imposed on related party trading under the REIFR. There is now also a clear mechanism for carrying out a capital increase and so it may be expected more REITs will expand following the capital increase of Riyadh REIT and the approval of the Taleem REIT capital increase. Finally a new mechanism for merging REITs has been introduced in addition to a new mechanism for converting private real estate funds into REITs," Issa says.

"REITs are obtaining increasing exposure to foreign real estate, like Bonyan REIT which acquired property in Dubai and it is expected more will follow, possibly with exposure in the US or Europe."

"In addition, given the Authority's increasing focus on asset disclosure, it is reasonable to expect future REITs will start to target higher quality assets with investment grade tenant and strong lease terms," Stull explains.

"Given the Authority is tightening up the REIT regime, it is expected smaller REITs will start merging and existing private funds will start converting into

RELATED LEGISLATION

Part 1 of Saudi Arabia Capital Market Authority Decision No. 6/130/1438

These Instructions aim to regulate the offering of REITs. They should be read together with the Capital Market Law and its Implementing Regulations.

(Source: Lexis Middle East Law)



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REITs as a way of exiting their underlying assets. In addition, it is expected the level of competition between the various REITs will increase in terms of quality of assets, property management and corporate governance. It is also expected a mortgage REIT regime may be developed and implemented in the near future," Stull adds.

UAE

"In the UAE, REITs can set up onshore or in the DIFC or Abu Dhabi Global Market (ADGM). A REIT registered onshore would be regulated by the Securities and Commodities Authority. The Securities and Commodities Authority is the Federal securities regulator and has oversight over the investment funds industry, such as REITs, in onshore UAE. It is also the licensing body for the Dubai Financial Market and Abu Dhabi Stock Exchange. The Authority has only recently started developing the regulatory framework for investment funds. In June 2016, it reformed its legal infrastructure with Securities and Commodities Authority Decision No. 9/RM/2016 Concerning the Regulations of Mutual Funds and supplemented this with Securities and Commodities Authority Decision No. 1/RT/2017 on Real Estate Investment Fund Controls, or REIT Regulations," Hamzeh Al Rasheed says.

"A REIT is not required to, and may not take the form of a corporate vehicle under the Funds Regulations or the REIT Regulations. However, when it is licensed by the Authority, a REIT does enjoy a separate corporate personality. Neither the Funds Regulations nor the REIT Regulations impose any internal corporate governance requirements on a REIT established onshore. However, certain corporate governance and statutory requirements are imposed on the REIT's founders and fund manager. Despite this, REIT sponsors onshore are facing practical difficulties in licensing a public REIT with the Authority. This is primarily due to a relative ambiguity in the current regulatory infrastructure and lack of cooperation between the Authority and other relevant authorities like the Dubai Financial Market, Abu Dhabi



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Stock Exchange and local land departments," Stull explains.

"For example, while the Authority requires closed-ended investment funds, like REITs to be listed on either the Dubai Financial Market or Abu Dhabi Stock Exchange, it does not provide sufficient guidance on the listing requirements, or confirm

if the listing requirements applicable to companies also apply to REITs. It has been reported, that the Authority is considering enhancing its current regulations and is working with the Dubai Financial Market and Abu Dhabi Stock Exchange's respective real estate authorities to pave the way for the development of the onshore REIT market. In fact several REITs are expected to launch onshore once an enhanced regulatory platform comes into force", Al Rasheed adds.

WHAT'S NEXT?

"As real property prices stabilise in the UAE and Saudi Arabia, it is expected sponsors will launch new private and listed REITs," Issa states.

"In addition, as the number of REITs increase in Saudi Arabia and the UAE, it is expected the regulators will take further steps to harmonise regulations and improve the transparency and consistency required to launch additional REITs."

"It is expected REITs will follow international standards in terms of diversification and quality, which should provide comfort to investors. As the REITs grow in size, we are also likely to see them increasingly looking to overseas markets both in the GCC and internationally to diversify and find suitable and attractive assets," Issa concludes.

RELATED STORY

Bahrain: Domiciled Real Estate Investment Trusts Directives Released
LNB News 28/11/2017 87
Bahrain's Central Bank has released directives on the Bahrain Domiciled Real Estate Investment Trusts. The aim is to enhance their Real Estate Investment Trusts framework. They will allow retail investors to invest in Bahrain Domiciled Real Estate Investment Trusts.