



Submission on CSRC and NDRC Guidelines on the China Infrastructure REIT Pilot Program

On 30 April 2020, the CSRC and NDRC published two major documents on Chinese Infrastructure REITs:

- "*The Announcement on Pilot Program of the China Infrastructure REITs*" ("Announcement"); and,
- "*The Guidelines for the China Infrastructure REITs (Trial version)*" ("Guidelines").

The introduction of an infrastructure REITs pilot program is a milestone for China.

The Asia Pacific Real Estate Association (APREA) is very supportive of the pilot program for infrastructure REITs, and we are keen to make an ongoing constructive contribution to discussions about fine-tuning China's infrastructure REIT model.

For many years, APREA has worked closely with Chinese regulators and government agencies to share the best international thinking on modern REITs and provide advice on REIT models that meet China's long-term needs.

The announcement of the pilot program is timely given the opportunity to utilize REITs as a mechanism for boosting economic activity following the COVID-19 pandemic.

This pilot program will not only assist China to restore economic momentum, it can also help the Chinese Government achieve its objective to build a "strategic infrastructure" that will strengthen economic resilience and support broader social goals.

A distinct feature of the pilot program is the inclusion of technology-oriented assets such as logistics facilities, data centers and industrial parks, which APREA warmly welcomes.

APREA has established a special technical advisory committee in China, which includes international and domestic REIT experts who are also prominent real estate industry leaders.

Please see the appendices to this submission for more details on APREA and its China advisory committee.

This APREA committee has considered the issues outlined in the *Guidelines* under seven topics and offers 19 specific recommendations for consideration by CSRC and NDRC.

Summary of APREA Recommendations by Topic

Topic	Recommendations for Consideration	
REIT structure and management	1.	Simplify the REIT structure proposed in the <i>Guidelines</i> to align with international practice.
	2.	Expand the scope of entities eligible to manage a REIT.
REIT sponsors and underlying assets	3.	Relax requirements for qualifying as a sponsor and strengthen criteria for determining assets that can be included in REITs.
	4.	Reconsider the requirement for assets to achieve three years of stabilized cash flow before qualifying to be injected into a REIT.
	5.	Relax the requirement to lock-in sponsors for five years and to hold 20% of shares.
REIT valuation issues	6.	Change “asset valuer” to “valuer” in the <i>Guidelines</i> .
	7.	Clarify requirements on valuers hired by fund managers, financial consultants and ABS managers.
	8.	Work with industry to publish comprehensive technical practice notes for valuing REITs.
Leverage	9.	Raise permitted levels of leverage in REITs to between 45% and 50% of asset value in line with other successful Asian REIT markets and extend the activities to which debt can be applied.
Taxation	10.	Clarify the tax treatment of REITs to ensure: <ul style="list-style-type: none"> a) to encourage the establishment of REITs with high-quality assets, it is recommended that the transfer of assets into a REIT be tax exempt; b) avoid double taxation of REIT distributions – where tax is paid at the REIT level, investors should not be liable for tax on income distributed from REITs; c) capital gains arising from the sale of REIT shares by investors be taxed the same as other financial products.
REIT economics	11.	Focus on the quality of income generated by assets to be included in a REIT rather than require unnecessary diversity of income sources.
Ancillary issues	12.	Align the <i>Guidelines</i> and Announcement to ensure the types of assets eligible to be included in infrastructure REITs are consistent.
	13.	Expand the pilot program to include other asset types and geographies in China.
	14.	Relax restrictions in relation to the use of funds obtained by the sponsor from the sale of underlying assets.
	15.	Clarify and expand the circumstances for raising further equity relevant to the efficient operation and capital management of REIT funds.
	16.	Clarify the definition of “distributable profits” to ensure it relates to the distribution of net income.
	17.	Encourage participation by individual investors by relaxing the requirements on holdings by institutional investors.
	18.	Enhance requirements on regulations to incorporate international best practices.
	19.	Allow pilot REITs to participate in the Shanghai-Hong Kong and Shenzhen-Hong Kong stock market connect programs.

REIT Structure and Management

APREA Recommendation 1

Simplify the REIT structure proposed in the *Guidelines* to align with international practice.

APREA commends the Chinese Government for proposing a pilot REIT program.

APREA also recognizes the benefits of utilizing an existing legislative framework to ensure the pilot study can proceed as an immediate priority.

However, from a longer-term perspective, APREA proposes that the Government align its REIT legislation with international practice, especially tried and tested formats that work effectively in the Asia Pacific region.

The diagrams below show the structure proposed in the *Guidelines* for the Chinese infrastructure REITs pilot program compared to the REIT structure utilized in Singapore, which conforms to the standard format used in international REIT markets.

The Chinese pilot REIT model is considerably more complex than the international approach.

The complexity is due to added layers relating to an ABS (asset-backed security) manager and (potentially) PE fund manager and the inclusion of vehicles for holding assets.

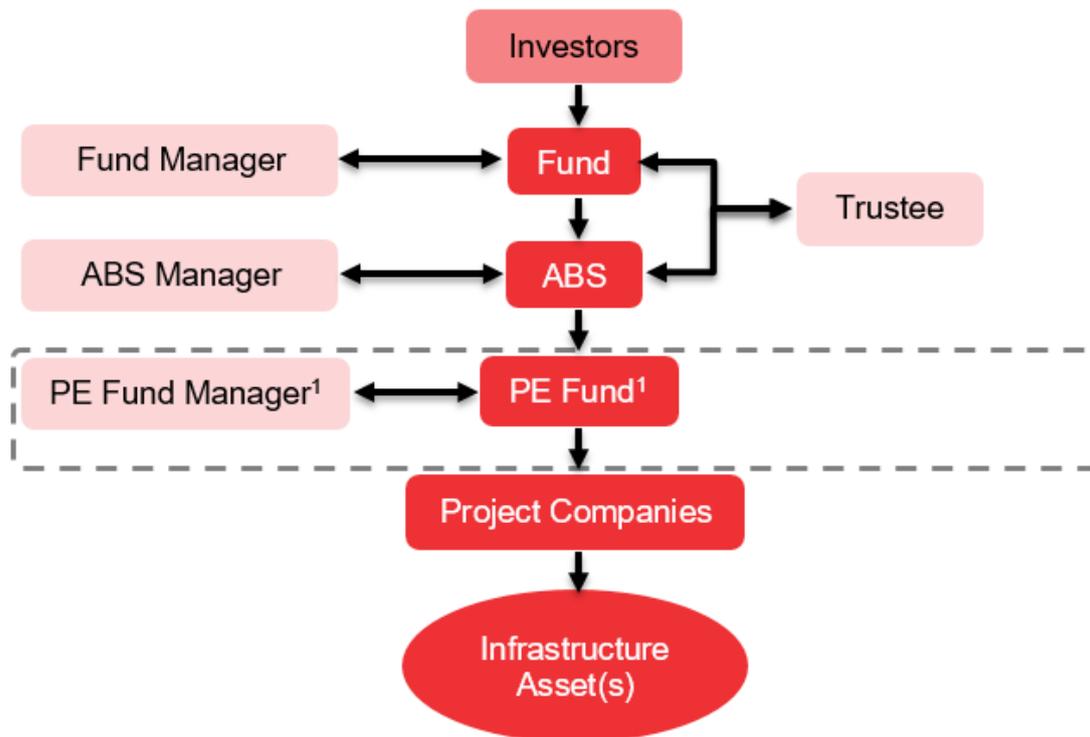
APREA proposes a simpler, more conventional approach for several reasons:

- the standard model has worked successfully in many countries around the world over many decades;
- reduced costs and higher returns to investors;
- clearer management, transparency and reporting;
- reduced potential for conflicts of interest; and,
- more efficient management of underlying assets in the REIT.

Finally, REITs are equity products that exist to serve the long-term interests of unitholders; whereas an ABS framework is designed for a different purpose – shorter-term financing.

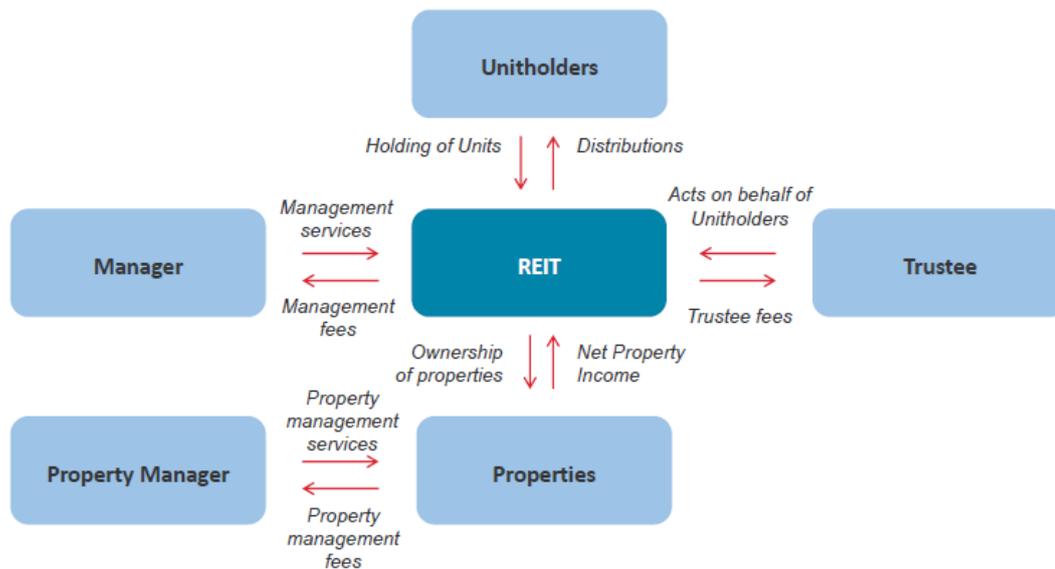
Consequently, APREA recommends a more conventional international REIT structure be adopted at the soonest opportunity.

Diagram 1: Structure for Infrastructure China REIT Pilots – prepared by Baker McKenzie



1. While the PE fund and its manager are not explicitly prescribed under the Draft Guidance, they may be required for practical reasons.

Diagram 2: Typical Singapore REIT Structure



APREA Recommendation 2

Expand the scope of entities eligible to manage a REIT.

The *Guidelines* require REITs to be managed by a mutual fund. APREA understands that mutual funds may outsource this responsibility.

APREA notes that professional REIT management is critical to the ongoing performance and success of REITs and that Chinese mutual funds are not experienced in this field.

However, there are many respected investment managers in China that could undertake this role which are not licensed as mutual funds.

In addition, APREA notes that it is common in Asia for sponsoring companies to establish specialist management entities with the skills to manage REITs. APREA believes this approach could be replicated in China.

The existence of a professional REIT management industry is a major benefit of establishing a REIT regime as it creates new jobs and builds international investment skills.

APREA suggests there is value in committing to professional development as a high priority in the pilot stage of the REIT program. A more professional REIT management sector will significantly improve efforts to foster a more sustainable and stable REIT industry in China.

Consequently, APREA recommends that the criteria for selecting REIT managers to be broadened so that existing fund managers with a proven track record can apply to be REIT managers.

APREA also proposes that sponsors be specifically permitted to establish REIT management companies that operate on an arms-length basis in line with international practice.

Furthermore, APREA recommends the *Guidelines* clarify the requirements of third-party managers in relation to quality, role, performance etc. to ensure professional standards of management.

Ultimately, a broader funds management industry will energize more listings and encourage a deeper, more liquid Chinese capital market.

REIT sponsors and underlying assets

APREA Recommendation 3

Relax requirements for qualifying as a sponsor and strengthen criteria for assets that can be included in REITs.

Many factors influence the success of REITs, including the quality of sponsors, management and assets. Consequently, it is crucial to balance these factors when setting eligibility or qualifying criteria for REITs.

At present, the *Guidelines* give too much weight to the qualifying criteria for sponsors at the expense of factors such as the quality of assets to be included in a REIT.

As currently drafted, several criteria relevant to sponsor eligibility could unnecessarily exclude respected companies from participating in the pilot REIT program.

APREA agrees with the CSRC's efforts to ensure an investor-focused REIT marketplace and that reasonable criteria are required to assess the eligibility of sponsors.

APREA offers to work with the CSRC to highlight overly restrictive criteria.

APREA also recommends that a regulator's assessment of REIT proposals should give appropriate weight to the quality, economic viability and sustainability of assets to be included in the REIT.

Such a framework would also align with international approaches to REIT regulation.

APREA Recommendation 4

Reconsider the requirement for assets to achieve three years of stabilised cash flow before qualifying to be injected into a REIT.

Item seven of the *Guidelines* says that:

"The asset should have more than three years of operation and have generated sustained, stable cash flow, with a good return on investment, and demonstrate a continuing capacity and growth potential."

APREA suggests two problems with this approach:

- many good quality projects have not been in operation for three years – this would narrow the universe of qualifying assets to be included in REITs; and,
- the income stream from projects can be stabilised before the completion of projects (via leases and contracts) – there is no reason to exclude such projects.

APREA proposes that the regulator focuses on proof that rental income from a project is stabilised via contracts and leases rather than utilizing a three-year timeframe.

It is possible to assess whether a project will deliver a good return and demonstrate growth potential from these contracts/leases. After all, valuations are based on similar evidence of future income streams.

If a timeframe is considered necessary, then APREA recommends a one-year period for evidencing the existence of contracts which signify the project's capacity to generate stable earnings, which would be consistent with international practice.

APREA Recommendation 5

Relax the requirement to lock-in sponsors for five years and to hold 20% of shares.

The *Guidelines* require REIT sponsors to hold 20% of a REIT's shares for at least five years. The objective is to ensure the sponsor retains "a stake in the game".

This is not the approach generally adopted in international markets.

A fixed time-frame may encourage volatility in stocks if sponsors exit at the end of that period.

Consequently, APREA suggests there are superior approaches to aligning the interests of sponsor and investors.

For instance, the Monetary Authority of Singapore (MAS) does not require sponsors to take a specific percentage of a REIT or to lock-in for a specific number of years. Nevertheless, S-REIT sponsors tend to hold around 30% of the stock.

One reason for these high levels of participation by sponsors is to ensure they can play a prominent role in strategic decisions about the REIT, including votes in relation to the appointment and dismissal of the REIT manager (which requires the agreement of 75% of a REIT's unitholders).

REIT valuation issues

APREA Recommendation 6

Change “asset valuer” to “valuer” in the *Guidelines*.

Based on the *China Asset Valuation Law*, “asset valuer” means those professional valuation institutes and individuals who value and appraise real estate assets, movables, intangible assets, corporate value, asset losses, or other economic rights and prepare a valuation report.

In the *Asset Valuation Law*, it calls those professionals “valuers”. Consequently, to maintain consistency, APREA suggests changing the designation of “asset valuer” to “valuer” in the *Guidelines* to align directly with the *Asset Valuation Law*.

In addition, “asset valuer” has a special meaning for assets owned by government entities.

There are strict probity rules associated with the valuation of assets in China which are better addressed through the use of term “valuer” rather than “asset valuer”.

APREA Recommendation 7

Clarify requirements on valuers hired by fund managers, financial consultants and ABS managers.

Provision 10 of the *Guidelines* require the fund manager to hire an independent asset appraiser to value an infrastructure asset to be injected into a REIT.

In addition, Provision 9 requires the financial consultant who is hired by the fund manager to undertake due diligence on the infrastructure project proposed for securitisation.

Furthermore, the ABS manager would also undertake valuations periodically. In short, multiple valuations will be required at various stages over the life of the REIT, which could be performed by a single valuer or several valuers.

APREA recommends the Guidelines declare clear rules in relation to the appointment and rotation of valuers by different stakeholders.

APREA Recommendation 8

Work with industry to publish comprehensive technical practice notes for valuing REITs.

Credible and trusted valuation practices are critical to the success of REIT markets.

The *Guidelines* and complementary CSRC documents specifically mention the importance of adopting international valuation practices.

APREA strongly supports this recommendation and offers to work with authorities to prepare comprehensive standards and practices for the valuation of REIT assets that will aid market transparency and promote credible reporting.

In particular, several issues require attention:

- who is qualified to undertake valuations?
- what valuation protocols and methodologies should be applied?
- what level of information should be disclosed?
- how can international concepts, such as FFO (funds from operation/net operating income) that are specific to REITs be adapted to the Chinese marketplace?

Overall, the requirements of the valuation sections of the *Guidelines* are comprehensive.

However, APREA suggests adding further details in Provision 11 that deal with information disclosures in the valuation report., such as:

- discount rate;
- return on income;
- forecast income growth rate;
- vacancy rate (where applicable);
- level of rental income compared with similar assets (where applicable);
- forecast income growth;
- annual operating revenue;
- cost of asset operation and maintenance;
- tax; and,
- annual net income.

The disclosure of these details will inject rigour into the valuation process. APREA commends the Singapore and Hong Kong real asset valuation rules as a model to be applied to Chinese infrastructure REITs.

We also propose that an independent analysis of relevant market trends and dynamics (including supply and demand fundamental) be incorporated into the valuation report.

As in Singapore and Hong Kong, market research reports provide a significant reference for investors to better understand the underlying market dynamics which drive asset performance.

There are also valuable international approaches relevant to issues such as due diligence and market investigation that APREA could help adapt to the Chinese marketplace in partnership with regulators.

From a practical perspective, there is value in developing rigorous due diligence processes for infrastructure construction projects given the size of these assets and the importance of assessing their inclusion in a REIT.

Provision 34 requires valuations to be undertaken every quarter. APREA recommends such valuations be conducted by an independent third party, as such parties can helpfully advise on the fair value of underlying assets.

In addition, APREA recommends that the *Guidelines* require a due diligence report by a qualified practitioner on legal issues, including:

- ownership of assets;
- the rights of asset management;
- ensuring the good character, reputation and conformance with all legal requirements of each stakeholder party; and,
- full disclosure and verification of all relevant documentation.

Leverage

APREA Recommendation 9

Raise permitted levels of leverage in REITs to between 45% and 50% of asset value in line with other successful Asian REIT markets and extend the activities to which debt can be applied.

The *Guidelines* restrict leverage to 20% of a REIT's asset value. This rate is far lower than the leverage levels permitted in international markets.

The chart below shows the current debt ceiling for Asia Pacific REITs. All markets allow a far higher level of leverage than is proposed in the *Guidelines*.

Country/Region	REIT leverage limitation
Japan	No specific limitation
Australia	No specific limitation
Singapore	No more than 50%
Hong Kong SAR	No more than 45% of the net asset value
Malaysia	No more than 50%
Thailand	Up to 60% with an investment credit rating
Taiwan	No more than 50%
India	Up to 49%

A survey of major Asia Pacific REIT markets also shows that actual debt levels are lower than those mandated in legislation. For instance:

- Japan – 44%
- Australia – 34%
- Singapore – 35%
- Hong Kong SAR – 26%

It is also worth noting that the world's largest REIT market, the United States, as well as the United Kingdom, France, Canada and Spain, do not mandate a debt ceiling.

In all these cases, market forces and market transparency persuade REIT managers to maintain leverage at reasonable levels.

APREA also notes that Belgium, Germany, the Netherlands and South Africa restrict leverage to a range of 60% to 66.25%.

APREA also notes that countries that instituted low debt ceilings during the early days of REIT regimes, such as Singapore, soon increased leverage allowances to more practical levels.

Finally, APREA recommends that the *Guidelines* specifically allow for borrowed capital to be used for purchasing other assets, as well as mergers and acquisitions, within agreed rules.

REIT taxation

APREA Recommendation 10

Clarify the tax treatment of REITs to ensure:

- a) to encourage the establishment of REITs with high-quality assets, it is recommended that the transfer of assets into a REIT be tax exempt;
- b) avoid double taxation of REIT distributions – where tax is paid at the REIT level, investors should not be liable for tax on income distributed from REITs;
- b) capital gains arising from the sale of REIT shares by investors be taxed the same as other financial products.

Tax is integral to the success of REITs in mature international markets.

The *Guidelines* are silent on the issue of REIT taxation and no supplementary advice has been published by the Ministry of Finance.

A tax regime for REITs that aligns with international practice in successful markets will help achieve these critical objectives.

Based on the current tax policies in China, we have three recommendations that address:

- the tax impact of transferring assets into a REIT
- the taxation of REIT income
- the taxation of capital gains

1. *The tax impact of transferring assets into a REIT*

It is critical to the success of REITs that they contain high-quality assets.

Therefore, it is important that sponsors be motivated to transfer such assets into a public REIT vehicle.

APREA contends that tax laws should assist rather than impede this process by removing all taxes that relate to the transfer of assets into the REIT.

Chinese law already provides infrastructure projects with incentives that reduce taxable liability. APREA proposes the same incentives be applied to infrastructure REITs.

This would mean that the transfer of assets into a REIT (which is effectively a corporate reconstruction) is free of land capital gain tax, capital gains tax, stamp duties etc.

APREA contends that this approach should apply to all taxes associated with the transfer of assets into a REIT.

This approach would align China with international practice and the world’s most successful REIT markets.

APREA has reviewed the history of REIT taxation and also surveyed the world's 12 largest REIT markets, comprising 95% of the global REIT market capitalisation.

Nine out of 12 central governments don't charge corporate tax when transferring assets into a REIT, as Table 1 shows:

Table 1: What is the capital gains tax applied to the transfer of assets into a REIT?

Country/region	Tax on the value of transferred assets
United States	Nil – deferred under UPREIT structure
Japan	Nil
Australia	Nil
United Kingdom	Nil
Singapore	Nil
France	19%
Canada	Nil
Hong Kong SAR	Nil
Spain	Nil
Netherlands	Yes – at the corporate tax rate
South Africa	Nil
Belgium	15%

Source: EPRA Global REITs Survey 2019

2. *The taxation of REIT income*

From the 12 largest REIT markets mentioned above, we found that:

- none of the 12 mature REIT markets is subject to double taxation;
- 11 out of the 12 REIT markets levy tax on income at the investor level, as Table 2 shows.

Table 2: Who pays tax on distributed income and capital gains?

Country/region	Who pays tax on distributed income?	Who pays tax on capital gains?
United States	Investor	Investor
Japan	Investor	Investor
Australia	Investor	Investor (with 50% discount available for some investors)
United Kingdom	Investor	Investor
Singapore	Investor	Investor
France	Investor	Investor (with 50% discount available for some investors)

Canada	Investor	Investor
Hong Kong SAR	REIT – for domestic assets: one level of tax (although SPVs can pay tax under the two-tier tax system from 2018/2019. No tax on offshore real estate.	No CGT
Spain	Investor	Investor
Netherlands	Investor	Investor
South Africa	Investor – some pension funds exempt	Investor (discounts available)
Belgium	Investor	Investor

Source: EPRA Global REITs Survey 2019

In line with current Chinese tax policies, tax is levied at the REIT level.

APREA recommends that if this policy is maintained, then to ensure a reasonable investment return, there should be no tax paid at the investor level.

3. *The tax treatment of capital gains on investors*

APREA recommends that capital gains arising from the sale of REIT shares by investors be taxed the same as other financial products.

At this same time, APREA notes that the tax treatment of infrastructure projects is already constrained by several tax issues. These matters need to be resolved so that they do not apply to infrastructure REITs.

Other observations on the taxation of REITs

There is evidence that countries that fail to develop effective taxation arrangements for REITs hamper the effective introduction of a vibrant REIT market.

There are currently 13 countries that have enacted REIT legislation but failed to stimulate a REIT market, primarily due to poor tax frameworks. These countries are Chile, Qatar, Portugal, the Philippines, Hungary, Vietnam, Luxembourg, Oman, Lithuania, Mauritius, Costa Rica, Tanzania and Uganda.

The Philippines provides a standout example. Despite a successful stock market, quality assets, efficient developers and a good financial system, there have been no REIT IPOs since legislation was passed in 2009. This is due to tax rules that do not support a REIT market.

APREA also notes that a truly liquid REIT marketplace in the USA was delayed for almost a quarter of a century due to the poor tax policy framework.

More recently, India's promising REIT and InvIT (infrastructure investment trust) marketplace was delayed for four years until the tax arrangements for REITs/InvITs and their

subsidiaries were remedied. In 2019, the tax rules were fixed and several successful real estate and infrastructure IPOs were launched.

In conclusion, inefficient tax policies can undermine the economic viability of REITs and therefore discourage sponsors from bringing assets to the REIT marketplace.

APREA's goal is to ensure REITs can help build China's cities, inject capital, create jobs and increase the retirement wealth of millions of Chinese citizens.

As previously noted, a tax regime for REITs that aligns with international practice in successful markets will help achieve these critical objectives.

Finally, APREA strongly agrees with the *Announcement*, which says:

"REITs are a financial investment product with the medium return, medium risk, provide high liquidity, stable returns and high security, which increases choice in the investment world, and broadens options for investors."

APREA believes REITs are an ideal vehicle for helping achieve the Chinese Government's prosperity goals and help share the benefits of real estate and infrastructure investment across the mainstream Chinese community.

Given the potential social and economic dividends that a successful Chinese REIT market can deliver, APREA recommends the government adopt an international approach to the taxation of REITs, including targeted tax incentives.

APREA is keen to liaise with authorities to address these issues.

Economics of REITs

APREA Recommendation 11

Focus on the quality of income generated by assets to be included in a REIT rather than require diversity of income sources.

The *Guidelines* note that:

"The sources of cash flow from an infrastructure project should be highly diverse, and it should be mainly generated by market-oriented operations, and not rely on income support from a third-party".

However, APREA observes that many infrastructure projects are managed via a government platform, which reduces the diversity of income sources.

For example, for infrastructure projects stipulated in the *Guidelines*, such as "environmental protection projects including municipal sewage waste disposal projects, solid waste disposal projects and other hazardous waste disposal projects", it is common for the government to act as the sole provider of income even though several agencies may be associated with the project.

In addition, the government acts as a sole purchaser for many urban infrastructure projects, thereby reducing the diversity of income sources required by the *Guidelines*.

Given this common situation in China, APREA recommends a relaxation of the requirement to secure diverse income streams.

Instead, APREA recommends that the quality of the income from the assets act as the primary criterion for REIT inclusion.

Such an approach would conform exactly with the announcement by the CSRC and NDRC, "Announcement of China infrastructure REITs pilot program", which states:

"infrastructure projects that are determining to be injected into REITs should have the income mainly come from the project users, and the projects should not have any major problems and contract disputes".

Ancillary issues

APREA Recommendation 12

Align the *Guidelines* and *Announcement* to ensure the types of assets eligible to be included in infrastructure REITs are consistent.

The range of asset types stated in Provision 2 of the *Guidelines* are:

"infrastructure projects include logistics, toll-roads, airports, seaports etc, the municipal projects on water, electronics, gas, heat etc, the other type of infrastructure assets like industrial parks etc; and it doesn't include residential and commercial real estate."

APREA suggests aligning these categories to those cited in the *Announcement* which states:

"infrastructure projects include logistics, transportation facilities such as toll-roads etc; the municipal projects on water, electronics, gas, heat etc; hazardous waste disposal projects like sewage waste disposal projects, solid waste disposal projects etc; new infrastructure projects like internet communications etc; as well as national strategic industrial parks such as high-tech industrial parks, featured industrial parks etc, and it doesn't include residential and commercial real estate."

APREA Recommendation 13

Expand the pilot program to include other asset types and geographies in China.

APREA welcomes the strategic focus of the infrastructure REIT pilot program.

Nevertheless, APREA believes there is a case for increasing the economic performance of REITs by allowing a moderate portion of the fund to include assets and geographies not specifically identified in the *Guidelines*.

A range of 10% to 20% of the total fund value is suggested as a moderate portion.

The inclusion of high quality, high-performing assets would boost the overall return of the pilot REIT funds and lift overall confidence in REITs as an investment vehicle.

APREA Recommendation 14

Relax restrictions in relation to the use of funds obtained by the sponsor from the sale of underlying assets.

The *Announcement* states that:

"To enhance the management of financing, when the sponsors (the original owners) obtain the funds through transferring infrastructure assets into REITs, the activities of those funds should accord with the government's policy for the industry. We encourage the original owners to use the funds on new infrastructure projects, public utilities and services, and support the projects that strengthen areas of weakness, and form a healthy circle of investment."

In short, the government requires funds raised from the sale of assets to be dedicated to a limited range of municipal activities.

APREA suggests a relaxation of these rules. As the original owners of the REITed assets, local governments may be permitted to utilize the revenue raised after selling assets for such purposes as poverty alleviation, bail-outs etc., that might more directly serve local needs and create jobs.

APREA Recommendation 15

Clarify and expand the circumstances for raising further equity relevant to the efficient operation and capital management of REIT funds.

The *Guidelines* provide few details on the range of activities to which the pool of REIT capital can be directed.

Legislation in other jurisdictions is more specific on permitted activities, for instance, M&A, purchase and sale of whole assets or portions of assets etc.

APREA offers to work with authorities to prepare a more specific list of activities and recommends the latest Singapore legislation as a valuable starting point.

APREA Recommendation 16

Clarify the definition of "distributable profits" to ensure it relates to the distribution of net income.

Item two of the *Guidelines* states that 90% of annual "profits" must be distributed to unitholders for a fund to qualify as a REIT.

APREA suggests there is great value in clarifying the concept of "distributable profits".

We suggest that to align with international practice, 90% of the **net income** should be distributed. That is, "net income" is the relevant concept rather than "profit".

There are standardized international definitions of net REIT income which take account of operating issues, fees, capital allowances, provisions etc. However, the concept remains clear: REIT investors (beneficiaries) receive their share of the net income they would get as if they owned the assets directly.

APREA Recommendation 17

Encourage participation by individual investors by relaxing the requirements on holdings by institutional investors.

Provision 18 of the *Guidelines* states that:

"The shares to be sold to institutional investors should not be less than 80% of the total equity offered to the public, after deducting the shares sold to the strategic [cornerstone] investors".

The provision also requires that strategic investors must subscribe to no less than 20% of total equity.

This means the portion of shares left available to individual investors will be less than 16% of the total value of a REIT.

APREA agrees that the success of the China REIT pilot program will depend on strong support from cornerstone and institutional investors.

However, there is also great value in allowing ordinary citizens and families to invest in REITs directly, as well as via their pension funds.

Consequently, APREA recommends that, in time, the regulator increases the share of REIT units available to individual investors.

APREA Recommendation 18

Enhance requirements on regulations to incorporate international best practices.

The success of international REIT markets is a function of practices evolved over many years that can be adapted to Chinese circumstances.

These practices cover every aspect of a REITs operation, governance, capital management, budget approval, fees and compensation, reporting and disclosure, voting practices, dispute solution, conflicts of interest, M&A protocols (to name a few).

APREA offers to collaborate with regulatory authorities to help prepare best practice guidance documents that complement the formal *Guidelines*.

The goal is to ensure an efficient, transparent and investor-oriented REIT market in China.

APREA Recommendation 19

Allow pilot REITs to participate in the Shanghai-Hong Kong and Shenzhen-Hong Kong stock market connect programs.

APREA suggests that there is an ideal opportunity to include the infrastructure REITs pilot program in the "Shanghai-Hong Kong Stock Exchange" and "Shenzhen-Hong Kong Stock Exchange" connect mechanisms.

This would increase liquidity by allowing Hong Kong-based investors to participate in the pilot program.

It would also help accelerate the financial connection between the mainland market and the Hong Kong SAR.

As a result, the pilot infrastructure REIT program could also help finance the Greater Bay Initiative.

Appendix 1: About APREA

APREA is a non-profit society that represents the property investment industry across the Asia Pacific. Our members include prominent pension, insurance and sovereign wealth funds, investment managers, family office platforms, developers, professional firms, and thought leaders.

APREA's focus is a cross-border investment and engages closely with governments to help open-up and expand property investment markets by working with governments to improve business ground rules.

At present, APREA hosts chapters in China, Japan, India, Australia, Malaysia, Singapore, Hong Kong, and the Philippines.

APREA's policy solutions address:

- REITs & securitization frameworks;
- infrastructure and nation-building programs;
- housing affordability;
- sustainability & ESG;
- investor-focussed practices for fund managers; and,
- informed, skilled, and transparent markets.

Appendix 2: APREA China Advocacy Committee - member list

Name	Job Title and Company
Hei-Ming Cheng (Chairman)	Founder & Chairman, KaiLong Group
Professor Meng Xiaosu (Special Advisor)	Chairman, Huili Fund; Leader, REITs Research of State Council Development Department
Alvin Loo	Head of China, ARA Asset Management
Rico Chan	Senior Partner, Baker McKenzie
Cliff Chen	Managing Director, China, Blackstone Group
Hu Feng	Senior Director, Head of Valuation & Advisory Service, North China, Cushman & Wakefield
David Chen	Chairman and CEO, F.O.G Capital & Asset Management; Independent Director, Yuexiu REIT
Harry Du	Senior Partner, King & Wood Mallesons
Tracey Zhang	Financial Services Leader, Tax, KPMG China

Allan Zhang Wenliang
Country Principal
APREA China Chapter
30 May 2020 – FINAL ENGLISH VERSION

Please note

This is an English translation of APREA's submission to regulatory authorities. The Chinese version takes precedence as APREA's official viewpoint.