European Commission

European
Construction Sector
Observatory

Policy measure fact sheet
Ireland
Real Estate Investment Trust Regime
Thematic Objective 1
March 2016

Implementing body:	Department of Finance
Key features & Objectives:	Introduction of Real Estate Investment Trust (REIT) Regime
Implementation date:	27th March 2013 (enacted into law in the Finance Act 2013)
Targeted beneficiaries:	Investors in Irish Real Estate (both Irish and non-Irish investors) and REIT shareholders
Targeted sub-sectors:	Real estate (property) sector, Construction sector
Budget (EUR):	n/a

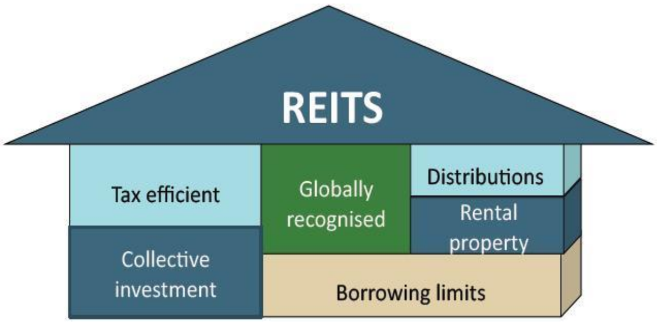
In a nutshell

Prior to the collapse of the banking sector in 2008, the Irish property and construction sector had been growing rapidly during the Celtic Tiger period (mid-1990s to mid-2000s). By 2008, the two related sectors accounted for approximately 20% of Irish economic activity.[1] Following the financial crisis, construction sector output fell relative to the economy and by 2013 it accounted for less than 7% of economic output. Commercial and residential property values also fell sharply.[2]

The Government has introduced a number of measures since 2009 to help the property and construction sector to grow output to 12% of economic activity. In 2009, the Government established the National Asset Management Agency (NAMA)[3] – Ireland's 'bad bank' – to acquire property development loans from Irish banks to improve the availability of credit. Reforms to Capital Gains Tax[4] and stamp duty[5], and a move from transaction-based property taxes to annual property taxes are some examples of more recent measures implemented since 2012.[6] The rationale for the 12% objective is to recover output to a level that is in line with the European average of about 10% of GDP.

The main objective[7] of NAMA since its foundation is to recoup over €30 billion of taxpayers' money spent on loan acquisitions. Achievement of this objective depends on private sector investment to drive transactions and reactivate the property market. One of the Government´s key measures to encourage new sources of investment in the property and construction sector is the introduction of Real Estate Investment Trusts (REITs)[8] as a new corporate property investment vehicle. The Finance Act 2013[9] introduced a substantial new body of legislation into Irish law, providing a tax framework for **REITs.**[10]

Figure 1: REITs – what are they?[11]



The new legislation was introduced to address a number of structural issues of concern in Ireland's investment property market:

1. **REITs remove the double layer of taxation** that applies **to property investment via corporate vehicles** – i.e. taxation of company and shareholder profits. Subject to strict criteria, REITs are exempt from tax on qualifying income and gains within the REIT;
2. **REITs diversify risk** by providing a framework for collective investment in property assets. Investors can buy shares in a REIT that manages a diversified property portfolio and spread the risk to their investment;
3. **REITs are an internationally recognised investment model**[12] and are more attractive to investors than unique Irish products. The aim is **to attract new sources of investment capital** to the Irish property market with the potential to finance the completion or development of commercially viable property assets that may otherwise struggle to attract financing from traditional sources.

First introduced in the US in 1960, REITs make investments into large-scale, income-producing property available to the ordinary investor, without the need to invest in physical bricks and mortar. By purchasing equity shares in a REIT, an ordinary investor can access the commercial property market in the same way that share purchases would enable them to access any other industry or market.[13]

REITs are now a globally recognised investment structure and are employed by a majority of the world's most developed nations. EPRA estimated in 2014 that 37 countries worldwide have REIT or 'REIT-like' legislation in place.[14] By incentivising profitable investments in real estate, the Government hopes to also encourage investment in construction projects to develop new and existing commercial and residential buildings. For example, REITs are an important vehicle for unwinding NAMA's warehouse of 'assets', moving ownership back into private hands and funding the completion of development and construction projects that were halted following the financial crisis.

General description

A REIT is a publicly listed company whose main activity is the ownership and management of property-related assets.[15] These properties include, but are not limited to, offices, shopping centres and warehouses, as well as commercial sites for development opportunities. As publicly traded companies, shares in REITs can be bought and sold in the same way as other shares.

REITs are designed to generate investment returns through:

1. Exposure to the value of the property assets that the REIT owns and the accompanying capital growth; and
2. Rental income.

To qualify for the REIT tax regime in Ireland, a REIT must:[16]

- Be resident in Ireland and not resident elsewhere;
- Be incorporated under the Irish Companies Acts;
- Be a listed quoted company which is traded on a main Stock Exchange in an EU Member State;
- Not be a close company[17] (subject to certain 'good shareholder' exceptions);
- Derive at least 75% of its profits from its operations as a property rental business. Such business must consist of at least three properties, no one of which must be more than 40% of the total;
- Maintain a ratio of at least 1.25:1 of income to financing costs;
- Hold at least 75% of its assets, by market value, in its property rental business;
- Maintain a loan to value ratio of not more than 50%; and
- Distribute at least 85% of its income by way of dividends to its shareholders (income does not include capital gains).

REITs provide investors with:

- Improved Liquidity: REITs are listed on a stock exchange, making it easier for the ordinary investor to move in and out of their property investments.
- High dividend payout ratio: The dividend payout obligation on REITs means that a much larger share of total returns come from dividends when compared with other equity investments, such as seed and venture capital, private equity, stocks and bonds, exchange-traded funds, amongst others.
- Diversification: Investment in REITs can provide asset class diversification to an investment portfolio, through exposure to property, without having to invest in physical bricks and mortar.
- Access to high quality projects: REITs can provide investors with access to high quality properties which would generally tend to be out of reach to the ordinary investor.
- Inflation hedge: REITs can provide a natural hedge against inflation. Commercial real estate rents and values have tended to increase when in line with inflation over the long-term.

Achieved or expected results

In a little over one year from their launch, Irish REITs[18] had already raised over €900m from investors. One of the reasons the Dept of Finance introduced REITS was to try and bring international investors to Ireland. This has proven to be the case thus far, with the majority of Green and Hibernia REIT investment coming from overseas investors.[19]

The **Green REIT**[20] was the first to list in Ireland in July 2013 after the introduction of REIT legislation by the Government. Figures for June 2015 show that it has a property portfolio valued at €968 million, spanning 24 properties with a total rental income of €55.7 million. Green REIT invests in commercial properties in prime locations, mainly around Dublin (95%), which requires capital and asset management expertise.

Green REIT is also implementing a development programme made possible by the high levels of investment and rental income that it generates. This type of REIT development programme has the potential to significantly boost investment in the construction sector. The investment made by REIT shareholders is used by the REIT to acquire a property portfolio. In order to profit from the rental income that these properties generate, development work is required to make acquired properties fit for rental. Such work may involve the updating or redevelopment of existing properties or the development of new buildings on acquired land or in place of existing buildings. REITs are commissioning and financing construction projects that may otherwise be difficult to finance, for example, because of constrained bank financing.

Green REIT will fund the costs of its development programme through its €150 million, four-year revolving credit facility (RCF) with Barclays Bank Ireland (set up in December 2014), with the exception of Central Park's Block H, for which the REIT is using a ring-fenced funding facility.

The second REIT to launch was the **Hibernia REIT**, which listed on the Irish & London stock exchanges in Dec 2013 after raising €385m from Investors. By November 2015, it has already amassed a mixed use portfolio of 21 properties worth a total of €739 million, primarily consisting of office buildings in the Dublin area.

The **Irish Residential Properties (Ires) REIT** (formerly Capreit) is the third Irish REIT. It launched in April 2014 and is the only REIT in the residential property space. This REIT is focused on consolidating the fragmented Irish rental market by targeting high quality property assets in Dublin and other major centres. The company has a very strong track record back in Canada for this type of investment and so therefore is expected to do well. By end of Q2 2015, Ires REIT had invested over €426 million across 12 locations in the Dublin area. The Group has a portfolio of 1,566 residential suites and has reported a pre-tax profit of €14.8 million for the first six months of 2015.[21]

Perspectives and lessons learned

From a **government perspective**, the Department for Finance explains that it introduced the REIT framework to help to revitalise the property and construction sectors. By providing a new source of capital to the property market, the intention is that REITs will, in turn, reduce dependence on bank financing and because REITs are closed ended, encourage taking a longer term view, leading eventually to stability of tenure for tenants, greater supply of commercial and residential properties and better quality buildings. The Department of Finance points out that the REIT regime is in its relative infancy in Ireland. The fact that the three current REITs have grown significantly in terms of investment and property acquisition [and more recently development projects] in a relatively short period of time is very positive. The Department of Finance expects the property [and construction] sector to continue to develop over time and in so doing to increase the supply of professionally managed, good quality, secure and affordable rented accommodation.[22]

From a **property owner, investor/shareholder and developer perspective**, REITs are offering investors highly attractive investment opportunities and returns, while also contributing to the growth of the construction sector. The success of the Green REIT, for example, has enabled it to be an early mover in the development of new space in Dublin. Green REIT wants to benefit from lower construction costs and be able to deliver completed projects when demand for space outstrips supply and while rental values remain strong. While a property may not be let when a development or refurbishment commences, the marketing of the building commences well before the scheduled completion date. If rental occupancy is deemed to be a risk, the Green REIT can mitigate that risk by starting the letting process earlier.[23]

According to the CEO of Green REIT plc, the launch of its development programme in 2015 signals the start of an exciting new era. Green REIT forecasts continued growth as it is well positioned to take advantage of supply constraints and has the financial capacity to deliver new buildings on those sites earmarked for development and to acquire further properties in line with the company's investment policy.[24]

The CEO of Hibernia REIT is also optimistic for the future and points to the Group's pleasing performance in the first half of 2015, with significant progress having been made with their development portfolio. Their new €400 million flexible credit facility is enabling them to quickly take advantage of investment opportunities and to fund their development project pipeline.[25]

From a **construction industry perspective**, there are some early indications that REIT development activities are having a positive impact on the Irish construction sector, by commissioning and financing construction activity.

One of Ireland's leading civil engineering and building companies, BAM Contractors, has recently reported significant growth in their construction activity and resurgence in areas such as commercial office building activity.[26] This growth has led the company to invest €3 million in six new cranes for deployment at four different sites, two of which are projects commissioned by Green REIT. Another leading Irish construction firm,

Another leading firm, JJ Rhatigan & Company, has also reported growth in its construction activity since 2013, particularly in the Dublin area and in the residential sector,[27] which it attributes to projects commissioned and financed by Hibernia REIT plc and NAMA. It also notes "continued and substantial tender activity", which indicates that business prospects for construction firms are on the rise. J.J. Rhatigan has been involved in a number of Hibernia REIT development projects, such as the fit-out and completion of partially completed apartment blocks[28] in the Dublin area, and says that further growth in this sector is likely because it is currently substantially undersupplied. [29]

Despite the relative infancy of REITs in Ireland, it does appear that they are helping to reactivate the property and construction sectors. This trend is expected to grow in the coming years, in line with REIT investment growth.

Comparison with other analytical sources

This Policy Fact Sheet concurs with the Country Fact Sheet 2016 on Ireland:[30]

- Key economic drivers of the construction sector – business confidence and access to finance for construction enterprises;
- National and regional policy and regulatory framework;
- Current status and national strategy to meet Construction 2020 objectives – TO 1;
- Outlook.

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Endnotes

1 Property Industry Ireland Briefing to Oireachtas Environment Committee http://www.propertyindustry.ie/Sectors/PII/PII.nsf/vPages/News_and_events~pii-addresses-oireachtas-joint-committee-on-environment,-culture-and-the-gaeltacht-23-09-2014?OpenDocument

2 Ibid

3 www.nama.ie

4 'Capital Gains Tax' is a tax levied on profit from the sale of property or an investment.

5 'Stamp Duty' is a tax placed on legal documents usually in the transfer of assets or property.

6 http://www.oireachtas.ie/parliament/media/committees/environmenttransportcultureandthegaeltacht/Property-Industry-Ireland-opening-statement-%2819.9.2014%29.pdf

7 https://www.nama.ie/about-us/

8 http://taxpolicy.gov.ie/wp-content/uploads/2013/02/John-Moran-REITs-Presentation.pdf

9 http://www.irishstatutebook.ie/eli/2013/act/8/enacted/en/html

10 http://www.irishstatutebook.ie/eli/2013/act/8/enacted/en/pdf

http://taxpolicy.gov.ie/wp-content/uploads/2013/06/E3_DeirdreDonaghy.pdf

11 http://taxpolicy.gov.ie/wp-content/uploads/2013/02/John-Moran-REITs-Presentation.pdf

12 First founded by the US Congress in the 1960s, REITs are internationally recognised by the Global Industry Classification Standard (GICS) by S&P Dow Jones Indices and MSCI Inc. REITs and REIT-like structures are implemented in at least 34 countries worldwide. In fact, EPRA estimates that 37 countries worldwide have adopted this type of instrument.

https://www.reit.com/investing/investor-resources/gics-classification-real-estate

https://www.msci.com/resources/pressreleases/GICS_implementation_date_2016.pdf

REITS are also recognized by EPRA – European Public Real Estate Association:

http://www.epra.com/regulation-and-reporting/taxation/reit-survey/

13 https://www.zurichlife.ie/static/documents/DOC_9948/Understanding_Irish_Real_Estate_Investment_Trusts.PDF?docTag=

14 http://www.epra.com/regulation-and-reporting/taxation/reit-survey/

15 Irish Stock Exchange, May 2014

https://www.zurichlife.ie/static/documents/DOC_9948/Understanding_Irish_Real_Estate_Investment_Trusts.PDF?docTag=

16 http://www.irishreits.ie/uploads/4/4/7/8/4478917/102562_reits_a4_newsletter_april13.pdf

17 http://www.revenue.ie/en/tax/ct/close-companies.html

18 Green REIT, Hibernia REIT and Irish Residential Properties REIT

19 http://www.wealthwise.ie/blog.php?p=21

20 http://www.greenreitplc.com/

21 http://www.irishtimes.com/business/commercial-property/ires-reit-reports-pre-tax-profits-of-14-8m-in-first-half-1.2312332

22 https://www.kildarestreet.com/wrans/?id=2015-02-04a.8

23 Green REIT plc Annual Report 2015 http://www.greenreitplc.com/investor-relations/reports/

24 http://costarfinance.com/2015/02/24/green-reit-earmarks-e114m-for-ambitious-development-programme-after-reporting-forecast-busting-nav-growth/

25 http://www.irishtimes.com/business/commercial-property/pretax-profits-jump-at-property-group-hibernia-reit-1.2426870

26 http://www.bamcontractors.ie/news.htm/view/id/283

27 http://www.irishbuildingmagazine.ie/2015/07/26/jj-rhatigan-company-building-on-a-reputation-of-excellence/

28 http://www.irishexaminer.com/business/property-deals-offer-proof-sector-is-rebounding-284057.html

29 http://www.jjrhatigan.com/ie-news/wyckham-point-in-dundrum-completed-ahead-of-schedule/

30 European Construction Sector Observatory, Country Fact Sheet Ireland, March 2016, http://ec.europa.eu/growth/sectors/construction/observatory/index_en.htm