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**NATIONAL ASSOCIATION OF REAL ESTATE INVESTMENT TRUSTS®**

September 5, 2008

VIA E-MAIL

Ms. Florence E. Harmon
Acting Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: *Securities Ratings*
File No. S7-18-08
Release No. 33-8940

Dear Ms. Harmon:

This letter is submitted in response to the solicitation of comments by the Securities and Exchange Commission (Commission) with respect to its proposed rulemaking (Proposal) published in *Security Ratings,* Release No. 33-8940 (File No. S7-18-08; July 1, 2008) (Proposing Release).

The National Association of Real Estate Investment Trusts® (NAREIT) is the worldwide representative voice for real estate investment trusts (REITs) and publicly traded real estate companies with an interest in U.S. real estate and capital markets. Members are REITs and other businesses throughout the world that own, operate and finance income-producing real estate, as well as those firms and individuals who advise, study and service these businesses. NAREIT welcomes the opportunity to respond to the Proposal and is submitting its comments below.

## Executive Summary

While it is fully aware of the important reasons for the Proposal, NAREIT believes that the unintended consequences of the Proposal would create serious roadblocks to REITs' continued access to public debt capital markets. In summary, NAREIT believes that the vast majority of REITs that have a class of equity securities registered under the Securities Exchange Act of 1934 (1934 Act) would in practice be precluded from accessing public debt capital markets in an efficient manner through use by their operating partnership (OP) subsidiaries of the short-form shelf registration process under the Securities Act of 1933. This

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preclusion would result from: 1) barring issuers of investment-grade debt securities from being able to use Form S-3 unless they satisfy the new proposed eligibility standard for debt-only issuers set forth in the Proposal; and 2) a variety of legal, financial and tax constraints applicable to REITs that limit severely the ability of REIT OP subsidiaries to qualify for use of Form S-3 under other existing eligibility standards or under the new proposed eligibility standard for debt-only issuers set forth in the Proposal. The limitation on REITs' access to debt capital markets could, in turn, result in a variety of other undesirable effects on financial and real estate market activities at a time when these effects are likely to be particularly harmful, given the current reduced availability of credit.

With these considerations in mind, NAREIT respectfully requests that the Commission consider and adopt several changes to the Proposal to provide continued access to Form S-3 by REITs and their OP subsidiaries. In the following sections of this letter, we: 1) describe the typical REIT/OP structure; 2) analyze the problems created by the Proposal in its current form; 3) explain why these problems arise; and 4) suggest how the Commission could modify the existing proposal to avoid foreclosing REITs' access to debt capital markets via Form S-3.

Please be assured that NAREIT does not question the Commission's policy decision to reduce undue reliance on ratings assigned to debt securities and to improve the level of analysis underlying investment decisions with respect to debt securities in general.[1] Neither does NAREIT question the Commission's goal of limiting Form S-3 eligibility to those issuers that have wide following in the marketplace, as evidenced by their filings under the 1934 Act being broadly followed and scrutinized by investors and other market participants. The problem NAREIT wishes to highlight for the Commission's consideration is that for OPs, as public issuers of debt securities only that will rarely meet the transaction requirement of General Instruction I.B.1. to Form S-3 ($75 million public equity float), replacing the current transaction requirement of Form S-3 General Instruction I.B.2. (investment grade non-convertible debt securities) with a new requirement that the issuer have offered over $1 billion of non-convertible debt securities for cash in registered offerings over the prior three years is too restrictive in light of, as well as unnecessary to accomplish, the Commission's stated policy objectives.

NAREIT also respectfully submits that, considering all operating companies that are debt-only issuers as a group (*i.e.,* excluding special purpose vehicles created primarily for the purpose of issuing structured securities and issuers of asset-backed securities), the Proposal would have a disproportionately negative impact on REITs. It appears to NAREIT that one of the key purposes of the Proposal relative to Form S-3 eligibility is to address the recent turmoil in the debt capital markets, primarily insofar as investment grade debt issued by special purpose vehicles fueled excessive growth in some sectors of the market and led to investment losses in what were considered relatively low-risk securities. NAREIT respectfully requests that the Commission take into consideration that REITs and their OP subsidiaries are stable, well-capitalized, moderately leveraged, long-term owners and operators of investment real estate, not highly

[1] The Proposing Release states on page 4 that "the Commission is considering whether the inclusion of requirements related to securities ratings in its rules and forms has, in effect, placed an 'official seal of approval' on ratings that could adversely affect the quality of due diligence and investment analysis. The Commission believes that today's proposals could reduce undue reliance on ratings and result in improvements in the analysis that underlies investment decisions."

leveraged special purpose vehicles created to issue structured financial securities. Yet, if the Proposal is adopted in its present form, REITs and their OP subsidiaries would see their ability to access the debt capital markets most efficiently through take-down debt offerings from effective Form S-3 shelf registration statements severely constrained precisely at a time when they (and real estate markets) need that access the most. Moreover, the probable effect of denying most REIT OPs the ability to issue debt in registered offerings using Form S-3 would be to direct more of these offerings to the unregistered markets, contrary to the Commission's long term goal of increasing the attractiveness of registered offerings by reducing the time needed to access public markets and making short-form registration available to a greater number of issuers.

**I. Introduction to the Legal and Financial Structure of REITs**

In order to understand the impact of the Proposal, it is helpful to describe the typical legal and financial structure of publicly traded REITs. The prevalent corporate structure of these REITs is the so-called "umbrella partnership REIT" or "UPREIT" structure, in which a REIT (organized either as a business corporation or a business trust) is the general partner of an OP. The REIT indirectly owns its properties and conducts substantially all of its business through the OP. In almost all cases, the REIT owns a majority of the equity of the OP (OP units) and, whether or not that is the case, the REIT has full control of the OP as general partner under the terms of the partnership agreement. OP units are usually exchangeable for common shares of the REIT, subject to some conditions, making common shares of the REIT and OP units effectively economic equivalents. The OP, through the REIT's general partnership interest in the OP, is managed by the Board of Directors of the REIT for the benefit both of REIT shareholders and OP minority partners. In the great majority of cases, and in all cases with which NAREIT is concerned for purposes of this letter, the REIT's common equity securities are listed on a national securities exchange. However, the OP units are not and, for reasons summarized below, cannot be exchange-listed.

In most cases, UPREITs borrow at the OP level, rather than at the REIT level. These borrowings are comprised of both publicly issued debt securities, including debt securities of the OP exchangeable for common equity of the REIT, and private and quasi-private debt financings, such as secured and unsecured bank debt and financing provided by other institutional investors to fund acquisition and development activities. Creditors, as well as rating agencies, generally require that the OP be the primary obligor on the debt, and therefore be the issuer of the debt securities. This requirement ensures that, although the OP is only partially owned by the REIT, 100% of the cash flow from the operating assets of the whole enterprise is available to satisfy the claims of the holders of the debt securities. If the REIT were to issue the debt securities itself, the portion of the cash flow from the underlying assets that is attributable to the minority equity interests in the OP not owned by the REIT would not be available to service the debt. For the same reason, incurring debt obligations at the REIT level would interfere with preserving the pro rata liability of minority partners of the OP and undermine the effective economic equivalency of REIT shares and OP units.

In addition, OP debt securities are structurally one step closer to the actual revenue-producing real estate assets to which creditors ultimately look for repayment. Being creditors at the OP level alleviates "structural subordination" concerns from a general credit underwriting point of view. Structural subordination arises in a parent-subsidiary organizational structure regardless of whether the subsidiary is wholly or partially owned. Creditors of the parent whose claims for principal and interest should, as a business matter, rank *pari passu* with claims of creditors of a subsidiary for principal and interest do not actually rank on a parity basis with those claims because the subsidiary's creditors can exercise their remedies against the subsidiary and its assets, while the parent company's creditors cannot and thus are effectively "equity" *vis-à-vis* the subsidiary's creditors. In the UPREIT context, banks and institutional real estate lenders typically require the OP to be their borrower. If debt securities were to be issued in capital markets transactions by the REIT, rather the OP, those securities would be structurally junior to bank and similar debt.

While upstream guaranties by the OP of debt securities issued by the REIT might alleviate some of these concerns, they often present difficult enforceability/equitable subordination and other legal issues. A REIT typically does not guarantee debt issued by the OP, principally in order to afford the minority OP partners who contribute properties to the OP a tax basis proportionate to their equity interests in the OP. The fact that REITs generally do not guarantee subsidiary indebtedness is an integral part of the UPREIT structure that supports the operating and growth strategies of the REIT's real estate business as a whole. This structure is unlike many other parent/subsidiary relationships, where downstream guaranties are more common. Although downstream guaranties by the REIT of debt securities issued by the OP might be thought to reduce some of the adverse effects of the Proposal on REITs, in practice these guaranties will pose a variety of practical, legal and tax issues that would make general use of them problematic. NAREIT believes that effectively requiring downstream guaranties by the REIT as a condition to use of Form S-3 by the OP, as the Proposal would effectively do, is both unnecessary in light of the corporate relationship between the REIT and the OP and detrimental to REITs' ability to take full advantage of the UPREIT structure.

**II. REIT OPs Have Limited Eligibility for Form S-3**

Eligibility to use Form S-3 depends on an interplay of the registrant and transaction requirements in the General Instructions to Form S-3. Many REITs whose common equity securities are listed on a national securities exchange not only satisfy the registrant requirements of General Instruction I.A., but also satisfy the transaction requirements for primary offerings without limitation as to amount in General Instruction I.B.1. The largest REITs are also "well known seasoned issuers" (WKSIs) under Commission rules. However, their subsidiary OPs can only use Form S-3 pursuant to the eligibility standard for offerings of investment grade rated non-convertible debt securities that the Proposal would effectively eliminate. As discussed above, OPs in practice need to be able to issue debt securities in the public capital markets. Access to Form S-3 is therefore extremely important because it enables a REIT, through its OP, to use the shelf registration process to access the debt capital markets efficiently, both from a timing/process perspective and from a cost perspective. Preserving the eligibility of OPs to access to Form S-3 is of vital importance to REITs, which rely on frequent issuances of publicly traded debt securities to fund their operations and growth.

OPs satisfy neither the registrant requirements of General Instruction I.A. nor the transaction requirements for primary offerings of securities generally under General Instruction I.B.1. OPs do not have a class of equity securities registered under the 1934 Act that is listed for trading on a national securities exchange and therefore cannot meet the $75 million public float requirement, which is based on trading prices as reported by an exchange. The unlisted status of OP equity securities results in part from the adverse effects of becoming publicly traded partnerships (and therefore taxed as corporations) under the Internal Revenue Code. OPs cannot satisfy the transaction requirements for “limited primary offerings” under General Instruction I.B.6. because OP units are not listed for trading on any exchange. Further, even in the case of secondary sales, OPs cannot satisfy the transaction requirements of General Instruction I.B.3. to cover secondary sales (resales) of securities sold in unregistered private offerings because General Instruction I.B.3. requires that securities of the same class must be listed and registered on a national securities exchange. Finally, only the largest REIT OPs, which NAREIT believes to be very limited in number, could qualify as WKSIs by having issued more than $1 billion of non-convertible debt in registered offerings over the most recent three years.

Therefore, to be able to launch and price a public offering of debt securities on short notice using Form S-3, with the speed and efficiency necessary to take advantage of favorable market conditions, REITs and their OPs have generally relied on one of two approaches, both of which are based on the issuance of non-convertible investment grade debt securities. Neither of these approaches would be possible if the Proposal were adopted in its current form.

First, many OPs have issued investment grade non-convertible debt securities under Form S-3 General Instruction I.B.2. (*Primary Offerings of Non-convertible Investment Grade Securities*). To qualify to issue non-convertible investment grade debt securities under Form S-3, these OPs have chosen to register a class of equity securities under the 1934 Act on a voluntary basis by filing a Form 10 registration statement. This permits an OP to use Form S-3 and the shelf registration process of Rule 415 to register debt securities for issuance “off the shelf” as soon as it obtains an investment grade rating. Under the Proposal, it would no longer be possible for OPs to qualify to issue investment grade non-convertible debt securities under General Instruction I.B.2.

As an alternative, other OPs have issued debt securities in registered offerings, including shelf registrations, under General Instruction I.C.2. to Form S-3 as majority-owned subsidiaries of REITs that were transaction-eligible for use of Form S-3. However, General Instruction I.C.2. incorporates the investment grade non-convertible debt requirement currently found in General Instruction I.B.2. As a result, this eligibility to use Form S-3, like the direct eligibility described in the preceding paragraph, would no longer be available if the Proposal were adopted in its current form.

OPs also issue debt securities in unregistered offerings (generally private placements structured to take advantage of the Rule 144A resale exemption). This structure allows for speed comparable to a shelf “takedown” when marketing an offering, but carries trading restrictions associated with privately issued securities. Registered public offerings of debt securities do not face the same drawbacks, and the easy public access to the documentation for registered offerings through the EDGAR system also increases the level of transparency in the market and promotes broader research and market coverage.

We understand the underlying policy objectives reflected in the Proposal and the Commission's concurrent related rulemaking proposals, which would de-emphasize the ratings assigned to debt securities by rating agencies in general. We do not believe, however, that the $1 billion/three year threshold in the Proposal is an appropriate replacement standard for Form S-3 eligibility, particularly in the case of OPs, principally because it is not necessary to ensure that OPs as issuers of debt securities are widely followed in the marketplace, which is one of the key factors cited in the Proposal.

Those REIT OPs which are reporting companies in their own right and have significant amounts of debt securities outstanding (both with investment grade debt ratings and without) are broadly followed and scrutinized by investors, analysts and the markets. While we agree that having an investment grade debt rating is not necessary to ensure that investors and securities professionals give these issuers' financial and business reports and securities offerings appropriately thorough analysis, we do not believe that having issued $1 billion of non-convertible debt securities for cash in registered offerings during a three year period is necessary. Both because of the legal relationship between the REIT parent and its OP subsidiary and because REITs generally issue debt securities through OPs, OPs enjoy the kind of following in the marketplace that the Proposal would incorporate as a predicate for use of Form S-3.

## III. The Impact of the Commission Proposals

*The Proposal Will Significantly and Adversely Affect REITs' Access to Debt Capital*

The Proposal would for all practical purposes disqualify OPs from using Form S-3 and the shelf registration process until and unless they become WKSIs, which NAREIT believes is extremely unlikely except for a limited number of the largest OPs. We believe that this result is fundamentally inconsistent with actions taken by the Commission over the past several years that have improved the efficiency of the public capital markets and expanded the number of issuers that have access to those markets, while reducing the cost of raising debt and equity capital for public companies of different (and in many cases smaller) sizes. It also seems contrary to the assumption that the Proposal should not effect significant changes in current eligibility of issuers, as articulated by the Commission in the Proposing Release.[2]

By deleting the investment grade factor in General Instruction I.B.2. and replacing it with the $1 billion/three years test, most OPs would only be able to use Form S-3 and the shelf registration process if they satisfy a very high threshold that is essentially equivalent to the WKSI standard. We believe that few REIT OPs will satisfy this test. Based on information available to NAREIT, NAREIT believes that based on registered offerings of non-convertible debt securities by REIT OPs between 2005 and 2007, only seven REIT OPs would be eligible to use Form S-3 under the Proposal. Conversely, 27 REIT OPs have an investment grade rating currently and are thus eligible to offer debt securities using Form S-3 registration statements under General Instruction I.B.2 in its current form. Therefore, NAREIT's data show that the Proposal would result in

[2] See Proposing Release p.21: "[t]he Commission intends for the number of issuers eligible under the proposed criteria to register primary offerings of non-convertible securities on Form S-3 to not be significantly reduced, or to differ significantly from, the number of those eligible under the current form requirements."

approximately 75% of the REIT OPs that are currently eligible to use Form S-3 would become ineligible to use Form S-3 if the Commission adopts the Proposal without modification.

We strongly believe that the proposed test is, in several respects, both unduly restrictive and unnecessary to accomplish the Commission's stated goals. As noted earlier, we also believe that it is inconsistent with the Commission's actions to expand access to efficient and cost-effective capital markets and to promote use of registered offerings rather than private offerings.

*The Elimination of REITs' Access to Form S-3 Targets an Unintended Group*

The elimination of efficient and cost-effective access to public debt financing would have serious consequences for a group of issuers (REITs) that has not been associated with the market turmoil and perceived abuses that the Commission's Proposal and related proposed rulemaking seek to address. OPs are operating subsidiaries of publicly traded companies with ongoing business activities, not issuers of structured finance instruments or special purpose vehicles created for the sole purpose of issuing asset-backed securities. Elimination of REIT OPs' ability to use Form S-3 would not only have an adverse effect on their ability to efficiently and cost-effectively raise debt capital in public markets, but it would do so at a time when the effects on financial and real estate markets would be both inopportune and undesirable.

Elimination of Form S-3 eligibility for REIT OPs would likely have an immediate and significant negative effect on their access to the capital markets (both for issuance of new debt financing and for refinancing of currently outstanding debt). The resulting contraction of capital resources and liquidity may in turn have serious effects on the real estate activities of OPs and their publicly traded REIT parents. We believe that this is an unintended consequence of the Proposal, especially in light of the fact that REIT OPs that issue investment grade debt securities are in nearly every instance moderately leveraged, financially stable and well-followed in the securities markets.

We note that, in contrast to many of the well-publicized recent problems related to structured securities that are difficult to analyze in terms of risk and reward parameters and often involve complex financial instruments rather than direct obligations of operating businesses with tangible assets, REITs and their OPs are large, long-term owners and operators of tangible commercial real estate properties in various market sectors. They are also generally financially stable and well capitalized. As shown in the chart "*Composite REIT Leverage and Coverage Ratios (End of quarter, 1996:Q1 to 2007:Q4)*" attached as Annex 1 to this letter, between 1996 and 2007 leverage (measured by debt as a percentage of total [debt + equity] market capitalization) for the REIT sector has never exceeded 52%, with leverage above 50% for only three quarters, and since September 2003 (the period generally associated with excessive financial leverage) has not exceeded 45%.[3] The chart also shows that between 1996 and 2007 EBITDA coverage of interest expense has ranged between a high of 4.26 times and a low of 2.81 times, with coverage below 3.0 times for only three quarters. As operating subsidiaries of REIT parent companies that are typically listed on a national securities exchange, OPs issue debt securities in the ordinary course of business to finance their real estate development, acquisition and management activities.

[3] NAREIT notes that, as additional evidence of financial stability, most of the exchange-listed REITs (measured by market capitalization) and the OPs of these REITs have achieved investment-grade debt ratings.

Further, we note that access to efficient debt capital is supremely important to commercial real estate considering the extreme tightening of the commercial mortgage backed securities (CMBS) market and credit markets generally. According to Lehman Brothers CMBS Strategy Weekly, new U.S. CMBS issuance has fallen from $319.5 billion in 2007 to just $25.6 billion through July 31, 2008. As seen in the downturn of the early 1990s, commercial real estate's lack of access to capital can have devastating consequences to financial institutions and the overall economy.

*The Proposal is Inconsistent with Commission Goals and Prior Rulemaking*

NAREIT believes that the Proposal is, both in its effects and in its structure, inconsistent with Commission goals and prior rulemaking. We believe that the Proposal's effect of essentially eliminating the ability of REIT OPs to conduct streamlined public offerings of debt securities is inconsistent with a long series of Commission actions that have steadily expanded access to cost-effective capital markets access by public companies over the last 15 years. Starting with the change from three years to one year of status as a reporting company under the 1934 Act, the Commission has consistently made Form S-3 available to an increasing number of companies, including companies with smaller capitalization.

We also believe that the Proposal, which would severely curtail Form S-3 access for public offerings of debt securities by REIT OPs, is fundamentally inconsistent with the Commission's current policy goals. We note that the Proposing Release specifically states on page 21 that "[t]he Commission intends for the number of issuers eligible under the proposed criteria to register primary offerings of non-convertible securities on Form S-3 to not be significantly reduced, or to differ significantly from, the number of those eligible under the current form requirement." We believe that the Commission may not have been aware of the drastic impact that the Proposal will have on REIT OPs as a discrete but very important segment of public companies.

More specifically, the Proposing Release states on page 21 that "[u]sing the $1 billion threshold, we preliminarily believe that for issuances that have occurred thus far this year, the proposed change would result in approximately six issuers filing on Form S-1 instead of on a short-form registration statement." Based on information available to NAREIT, NAREIT believes the impact of the Proposal on offerings of debt securities by REIT OPs during 2008 would have been significantly more severe. In 2008 for REIT OPs alone, of the eight public offerings of debt securities by six issuers of an aggregate principal amount of $4.22 billion, six of the offerings by four of the issuers, representing $3.25 billion aggregate principal amount of debt securities, would have been ineligible for Form S-3 and thus required to have been registered on Form S-11 if the Proposal had been effective on January 1, 2008. Therefore since the beginning of 2008 the Proposal would have resulted in approximately 77% (measured by aggregate principal amount) and 75% (measured by issuers) of public offerings of debt securities on Form S-3 by REIT OPs being ineligible for Form S-3 and required to be registered on Form S-11. Given the timing, cost and related disadvantages of not being able to conduct a registered offering using Form S-3 and Rule 415, this represents a very significant, highly adverse impact on access to the debt capital markets by REITs and their OPs.

NAREIT believes that the Proposal is also structurally inconsistent with the Commission's past rulemaking and current policy goals when considered from a technical perspective. The adverse effects of the Proposal result in part from its adoption of the same standard as the test for eligibility to be a WKSI.[4] Restricting Form S-3 eligibility for debt-only issuers to those that can satisfy the WKSI test seems inconsistent with the Commission's goal of establishing a "graduated" systems in which issuers are allowed progressively easier access to the capital markets depending on the depth and breadth of their following in the market.[5] We note that adoption of such a high standard would appear to be a significant departure from current standards for Form S-3 use, which do not require issuers to satisfy a WKSI-type test, and we believe that this change is not required to achieve the goals articulated by the Commission in the Proposing Release. It is also unclear why equity issuers should be eligible to use Form S-3 based on $75 million of public float without regard to how or when those securities were issued, while debt-only issuers would be required to have issued $1 billion or more of non-convertible debt securities in registered offerings during the last three years in order to be eligible to use Form S-3.

## IV. NAREIT's Proposal

NAREIT respectfully submits for consideration by the Commission a modified standard for use of Form S-3 by debt-only issuers that would address the problems discussed above. NAREIT proposes that eligibility for use of Form S-3 by debt-only issuers should be based on:

1) the principal amount of debt securities ***outstanding***, rather than the principal amount *issued during a three year period*;

2) a dollar threshold (outstanding principal amount), such as ***$300 million to $500 million***, that is lower than that required to qualify as a WKSI and is more in line with that which makes equity issuers eligible to use Form S-3;

3) inclusion in the test of *all* debt securities issued in both registered and exempt offerings, rather than only those issued in *registered public offerings* during a three year period; and

4) inclusion in the test of *all* debt securities outstanding (whether or not convertible or exchangeable), rather than only *non-convertible* debt securities outstanding.

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[4] See Proposing Release at pp. 9-10: "These large issuers, defined as well-known seasoned issuers, include issuers that have issued for cash more than an aggregate of $1 billion in non-convertible securities, other than common equity, through registered public offerings over the prior three years. In adopting this definition, the Commission did not rely on investment grade ratings." See also Proposing Release at pp.20-21: "[w]e are proposing to revise the form criteria using the same method and threshold by which the Commission defined an issuer of non-convertible securities, other than common equity, that does not meet the public equity float test as a 'well-known seasoned issuer.' Similar to our approach with well-known seasoned issuers, we believe that having issued $1 billion of registered non-convertible securities over the prior three years would lead to a wide following in the marketplace. These issuers generally have their 1934 Act filings broadly followed and scrutinized by investors and the markets."

[5] It would also limit the ability of OPs to qualify as WKSIs by eliminating one of the three ways in which a majority-owned subsidiary can obtain WKSI status – by meeting the transaction requirement of General Instruction I.C.2. which the Commission is proposing to change.

NAREIT believes that its proposal is consistent both with past Commission rulemaking and with the Commission's long-standing objective to facilitate and expand capital market access for issuers with the required market following. NAREIT also believes that its proposal is consistent with the stated objectives of the Proposing Release. Modification of the eligibility criteria contained in Form S-3 General Instruction I.B.2. as proposed by NAREIT below would avoid the unintended elimination of use of Form S-3 by REIT OPs and the many adverse consequences that would flow from foreclosing access to Form S-3 by REIT OPs.

If the Commission cannot modify the Proposal to reflect the NAREIT proposal summarized above, NAREIT proposes as an alternative that the Commission adopt a less stringent test for Form S-3 transaction eligibility under General Instruction I.C.2. that would permit majority owned subsidiaries to use Form S-3 to register debt securities without a parent guaranty. This less stringent test would entail revising General Instruction I.C.2. to permit majority-owned subsidiaries of parent entities to register debt securities under General Instruction I.C.2. if the parent is eligible to use Form S-3 under General Instruction I.A. and satisfies the transaction requirement of General Instruction 1.B.1.

Each element of NAREIT's proposed alternative to the Proposal and the details of NAREIT's alternative proposal for subsidiaries of Form S-3 eligible parents are discussed separately below.

*Test Outstanding Debt Securities, Rather Than Debt Securities Issued During Prior Three Years*

As the first element of its proposal for a revised standard for eligibility for use of Form S-3 by debt-only issuers, NAREIT proposes that the Commission base Form S-3 access for these issuers on the principal amount of debt securities that are *outstanding* at the time eligibility is tested, rather than the amount of debt securities *issued* during the prior three years.

NAREIT believes that debt capital markets participants, including investors and research analysts, focus on the amount of an issuer's debt securities that are outstanding in the market and available for trading as the test for whether the issuer deserves their interest or the commitment of resources to research coverage, not on the amount that has been issued in a relatively recent period. Debt securities outstanding at any particular time may have been, and often were, issued more than three years before, since: 1) the average maturity of debt securities is in the five-seven-ten year range; and 2) debt securities typically have three or four year "no call" periods after the issue date. If an issuer continues to have a significant amount of debt securities outstanding at a given date, regardless of when the securities were originally issued, then buy side and sell side market participants will follow the issuer and provide the level and sophistication of analysis that the Commission cites in the Proposing Release as an appropriate test for Form S-3 eligibility.

This eligibility factor for debt-only issuers is also consistent with General Instruction I.B.1. to Form S-3, which requires for general Form S-3 eligibility a minimum aggregate market value of its voting and non-voting common equity held by non-affiliates (public float) in excess of $75 million, regardless of when or how the equity securities were issued. For a debt-only issuer, the principal amount of debt securities outstanding is the equivalent of public float for an issuer whose equity securities are listed for trading on an exchange, insofar as both parameters test the "market weight" of the issuer in the relevant sector of the capital markets.

*Reduce the $1 Billion Threshold to $300-500 Million of Outstanding Debt Securities*

Second, NAREIT proposes that the Commission reduce the $1 billion threshold contained in the Proposal to a lower amount, such as an amount between $300 million and $500 million of outstanding debt securities. In comparison to every other threshold for use of Form S-3 other than WKSI status, the proposed $1 billion threshold is exceptionally high. Moreover, using the same threshold for Form S-3 eligibility as for WKSI status appears to be contrary to the policy of creating a graduated system in which issuers of increasing sizes enjoy a progressively leaner regulatory regime based on their following in the marketplace.

Issuers with only $75 million of public float, and even "smaller reporting companies" (companies with less than $75 million of public float or less than $50 million of revenue if they have no determinable public equity float) are eligible for limited use of Form S-3. In this light, NAREIT respectfully submits that the proposed $1 billion threshold is disproportionately high.

As a general matter, listed REITs maintain a consolidated debt-to-total-market-capitalization ratio (*i.e.*, financial leverage) of 40% to 50%. That would mean that a REIT whose OP has at least $300 million of debt securities outstanding by definition would have at least the same amount of outstanding equity securities. In reality, because OPs typically also have bank debt and other traditional institutional loans on their balance sheets that are included in this ratio, the amount of enterprise equity is likely to be significantly higher than the principal amount of debt securities outstanding. Therefore, a threshold of between $300 million and $500 million of debt securities outstanding would identify REITs with a large consolidated equity market capitalization (generally $500 million and above), in addition to an amount of OP debt securities available for trading in the market amply sufficient to attract sophisticated coverage by investors and research analysts.

NAREIT believes that the $1 billion threshold greatly exceeds the amount necessary to ensure that an issuer and its debt securities are subject to the level of market attention and analysis cited in the Proposing Release. We believe that the $1 billion threshold would establish a standard that could be met by only a very limited number of issuers, since we believe that only a small segment of the largest domestic public companies have $1 billion of debt securities outstanding at any given date (regardless of the years in which the debt securities were issued). Lowering the threshold to $300 million or $500 million would still ensure that a company has a sufficient amount of outstanding securities to attract investor and analyst attention and to provide the level of trading volume required to justify debt capital markets research.

*Include Debt Securities Sold in Unregistered Offerings*

Third, NAREIT proposes that the Commission modify the Proposal to include not only debt securities issued in *registered* offerings, but also those issued in *exempt* offerings (such as, for example, so-called "Rule 144A" offerings) when determining the amount of debt securities outstanding for purposes of Form S-3 eligibility. This element of the proposal is based on NAREIT's understanding that market following for debt securities does not distinguish between debt securities issued in exempt Rule 144A and similar transactions and those issued in registered transactions, in part because these securities are available for trading under various Commission rules. The market for REIT OP debt securities is relatively unified, regardless of whether the securities were issued in exempt or registered offerings: the same investors purchase and sell these securities without regard to the type of transaction in which the debt securities were originally issued. For the same reason, both buy-side and sell-side analysts write research on all outstanding debt securities of an OP.

One reason for this lack of distinction is that most debt securities sold in Rule 144A and similar offerings are tradable immediately by the vast majority of debt securities market participants, and also become freely tradable by non-affiliates under Commission rules within a short period of time after they are initially sold. The vast majority of debt investors consist of mutual funds or large private funds that meet the requirement for being "qualified institutional buyers" or QIBs under Rule 144A and are therefore able to participate in trading immediately. After the recent amendments to Rule 144, the distinction in the market between registered, 144A and privately placed debt securities has been further reduced, and we understand that most investors in debt securities no longer demand a pricing discount (additional yield/wider spread) for securities issued in exempt transactions.[6]

NAREIT believes that this element of its proposal for debt-only issuers is consistent with General Instruction I.B.1. to Form S-3, which requires a minimum public float in excess of $75 million, regardless of whether the securities originally were restricted. For many Form S-3 eligible companies, the public float includes significant amounts of pre-IPO equity securities that were privately placed. Allowing debt-only issuers to count the principal amount of debt securities issued in exempt transactions towards their outstanding debt is entirely consistent with General Instruction I.B.1.

*Include Convertible, as well as Exchangeable Debt Securities*

Fourth, NAREIT proposes that, if revised, General Instruction I.B.2. should include not only *non-convertible* debt securities, but also *convertible,* as well as exchangeable, debt securities.[7] Differentiating between convertible and non-convertible debt securities was understandable when investment grade ratings were the principal criterion for determining eligibility to use Form S-3 for sales of debt securities. As the Proposing Release states, the original premise for General Instruction I.B.2. (*Primary Offerings of Non-convertible Investment Grade Securities*) was that such securities were bought and sold primarily, if not exclusively, on the basis of

[6] As a technical matter, NAREIT notes that the "issued for cash" component of the Proposal would have to be maintained in order to avoid double counting of securities issued in registered exchange offers, in which restricted debt securities are exchanged for unrestricted securities with identical terms and tenor shortly after the original issuance of the restricted securities.

[7] Although General Instruction I.B.2. refers only to non-<u>convertible</u> debt securities, we believe that it is appropriate to treat convertible securities (*i.e.*, securities of an issuer that can be converted into other securities of the same issuer) in the same manner as exchangeable securities (*i.e.*, securities of one issuer, such as an OP subsidiary, that can be exchanged for securities of another issuer, such as the parent REIT), and we believe that this is consistent with current views of the staff of the Division of Corporation Finance.

interest rate relative to the assigned rating.[8] The same cannot be said for convertible debt securities, when the linkage to an underlying equity security via the conversion feature made debt securities of different issuers non-fungible, even if a similar debt rating was assigned to the debt component of the bundled security. However, excluding convertible debt securities when testing Form S-3 eligibility no longer makes sense when the focus shifts from investment grade rating to market following.

It is our understanding that debt capital market participants, both on the sell side and on the buy side, follow significant issuers of debt securities without regard to whether the outstanding debt securities are equity-linked, conventional debt, or a combination of the two. Market participants are adept at analyzing the structural characteristics and pricing of convertible and other equity-linked bonds by focusing separately on the debt and equity components of the relevant debt security. While the difference between convertible/exchangeable and "straight" debt securities goes to the underlying investment thesis and valuation of the security, it has little or no bearing on the nature of the issuer and whether it and its securities are adequately scrutinized in securities markets. Limiting the test for Form S-3 eligibility to non-convertible debt would arbitrarily reduce the range of debt-only issuers that are eligible for access to the streamlined offering process of Form S-3 without any apparent policy justification.

For these reasons, if the Commission removes all references to investment grade ratings as a component of eligibility to use registration statements, and adopts criteria based in part on the level of outstanding debt securities and whether the securities markets are following an issuer and its securities, NAREIT believes that it would be appropriate to give full recognition to all of the factors considered by securities markets and conform the scope of market interest to Commission rules governing use of Form S-3 and other registration statements, as proposed by NAREIT.

At a minimum, NAREIT respectfully submits that the Commission should permit a debt issuer with a class of equity securities registered under Section 12 of the 1934 Act (as is the case for many REIT OPs) to include convertible, as well as exchangeable, debt in the "outstanding" test for Form S-3 eligibility, whether or not the equity securities into which the debt securities are convertible or for which they are exchangeable are listed on a national securities exchange. For debt-only issuers, Form S-3 General Instruction I.B.2. serves a purpose that is analogous to the role that Form S-3 General Instruction I.B.6. serves for issuers that do not have exchange-listed equity securities. Just as General Instruction I.B.6. does not require any minimum public float, General Instruction I.B.2. should permit use of Form S-3 regardless of whether the issuer has any exchange-listed securities, since the minimum amount of debt test is an indication of broad coverage in the marketplace.

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[8] See page 5 of the Proposing Release: "[t]he Commission adopted a provision in Form S-3 that a primary offering of non-convertible debt securities may be eligible for registration on the form if rated investment grade. This provision provided debt securities issuers whose public float did not reach the required threshold, or that did not have a public float, with an alternate means of becoming eligible to register offerings on Form S-3. In adopting this requirement the Commission specifically noted that commenters believed that the component relating to investment grade ratings was appropriate because *non-convertible debt securities are generally purchased on the basis of interest rates and securities ratings*." (emphasis added)

*Allow Access to Form S-3 for Issuances of Debt Securities by Majority-Owned Subsidiaries of Form S-3 Eligible Issuers*

Finally, if the Commission is not comfortable modifying the Proposal to reflect the changes proposed by NAREIT above, NAREIT respectfully requests that the Commission adopt a less stringent test for Form S-3 transaction eligibility under General Instruction I.C.2. If the Commission considers this alternative, we propose that a majority-owned subsidiary should be permitted to register debt securities for sale on Form S-3 pursuant to General Instruction I.C.2. if its parent issuer is eligible to use Form S-3 under General Instruction I.A. and meets the transaction requirement in General Instruction I.B.1., and we propose that no parent guaranty should be required under these circumstances.[9] This is particularly appropriate in the context of majority-owned OP subsidiaries where substantially all of the assets and revenues of the REIT reside in the OP and minority equity interests in the OP are exchangeable on a one-for-one basis for common shares of the REIT. This would preserve much of the access to public debt capital markets available to REIT OPs under current Form S-3 eligibility tests, as well as other similarly positioned parent/subsidiary enterprises.

While Form S-3 General Instruction I.C.2. is currently parallel to Form S-3 General Instruction I.B.2. (*i.e.*, provides for offerings of non-convertible investment grade securities), the reason for the parallel structure appears to be based on the use of investment grade rating as a criterion. Following the rationale set forth in the Proposing Release, if Form S-3 eligibility is to be based on market coverage of the issuer rather than on the rating of the securities, NAREIT submits that logic does not require that the same test should apply to both stand-alone debt-only issuers and debt-only issuers that are controlled by an S-3 eligible parent company.

In the case of majority-owned subsidiaries of parent entities that are eligible for general use of Form S-3 under current General Instruction I.B.1., consideration should be given to the fact that market participants follow the consolidated enterprise as a whole – in this context, the REIT and its subsidiary OP. In the case of REITs and their OP subsidiaries, market participants cover both the REIT parent, whose equity securities are typically listed for trading on a national securities exchange, and the OP subsidiary, which issues publicly traded debt securities. The fact that the REIT conducts substantially all of its business through the OP and controls it, both by virtue of its ownership of a majority of its voting securities and as its general partner, means that the REIT and the OP are, from an analytical point of view, the same enterprise. This is the case whether or not the REIT parent guaranties the debt of the OP and therefore Form S-3 eligibility for the OP subsidiary should not depend on whether the REIT parent is contractually obligated as a guarantor to the holders of the OP's debt securities. If allowing unrestricted eligibility for any majority-owned subsidiary of a Form S-3 eligible parent to use Form S-3 is not acceptable to the Commission, NAREIT believes that an appropriate limit could be established, based upon the level of consolidated assets and revenues represented by the subsidiary in order to ensure that the subsidiary and the parent are the same or substantially the same for financial and business purposes.

[9] If the Commission adopts this alternative, General Instruction I.C.2. to Form S-3 would need to be amended because it currently requires satisfying the transaction requirement of General Instruction I.B.2.

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NAREIT thanks the Commission for this opportunity to comment on the Proposal. Please do not hesitate to contact George Yungmann, Senior Vice President, Financial Standards at (202) 739-9432 or the undersigned, at (202) 739-9408, if you would like to discuss our comments and proposal.

Respectfully submitted,

Tony M. Edwards

Tony M. Edwards
Executive Vice President and General Counsel
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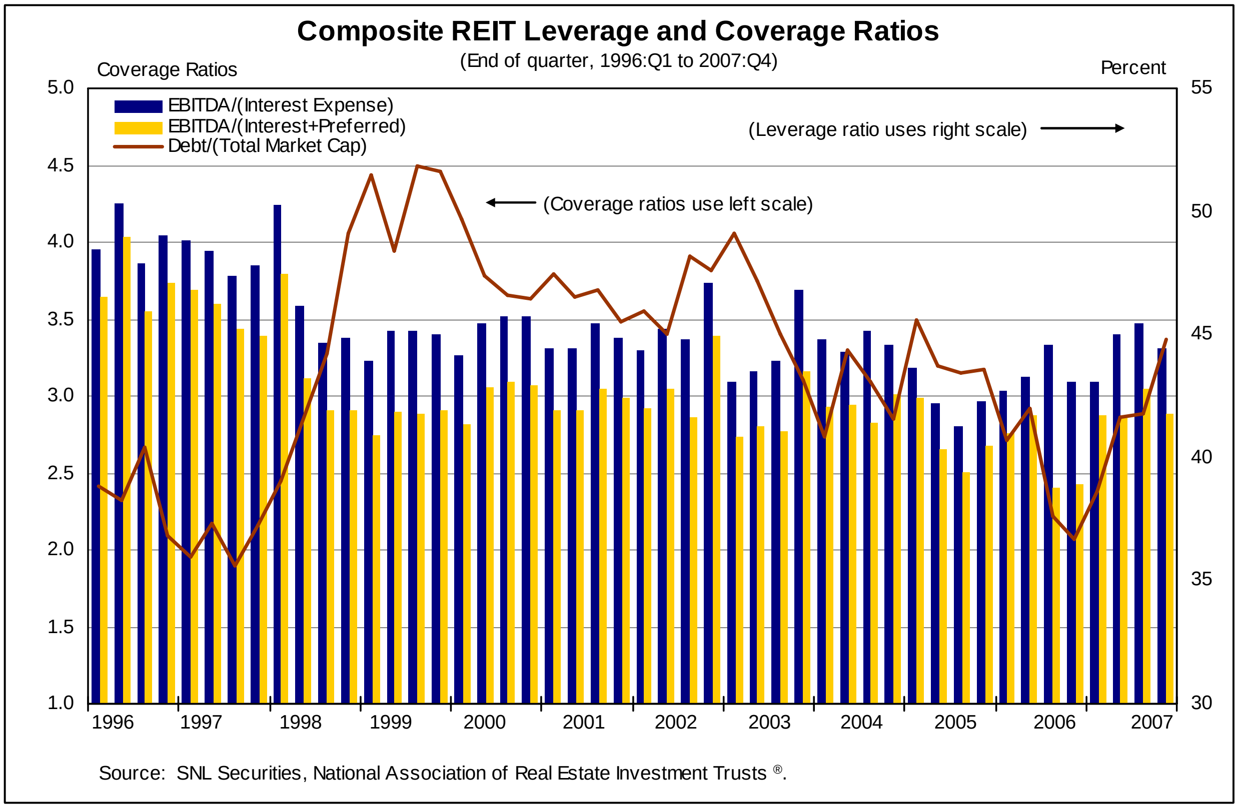
**ANNEX 1**


Composite REIT Leverage and Coverage Ratios
(End of quarter, 1996:Q1 to 2007:Q4)
Coverage Ratios
Percent
EBITDA/(Interest Expense)
EBITDA/(Interest+Preferred)
Debt/(Total Market Cap)
(Leverage ratio uses right scale)
(Coverage ratios use left scale)
5.0
4.5
4.0
3.5
3.0
2.5
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Source: SNL Securities, National Association of Real Estate Investment Trusts ®.