

Mr Thomas Neumann  
Executive Director – Securities Supervision/Asset-Management  
BaFin - Federal Financial Supervisory Authority  
Lurgiallee 12  
60439 Frankfurt  
Germany

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Dear Mr Neumann

### **AIFMD: German Open Ended Funds, listed property companies and REITs**

We would like to thank you for giving us the opportunity to meet with you on 10th May 2011 to discuss the application of the AIFMD to property companies (including REITs). As organisations that represent European and US listed property companies we are keen to ensure an appropriate and consistent application of the Directive on a European and global basis. It was therefore very helpful for us to discuss this with you and better understand the developing position of the German regulators on this issue.

At that meeting, you asked us to provide information that would help in identifying the distinguishing characteristics of listed property companies in Germany and the German open ended funds (GOEFs) - being the predominant form of real estate investment vehicle in Germany.

Although the German Property Federation (ZIA), were not present at the meeting on the 10<sup>th</sup> May, we have discussed this letter with ZIA and they are fully supportive of our comments. ZIA, who are copied in this letter, represent all sectors of the German property markets, including GOEFs and property companies including G-REITs.

### ***Background information***

Whilst the fact that GOEFs fall within the scope of the AIFMD is non-contentious, on the other hand, German property companies (whether or not they are listed on the public markets), do not generally expect to fall within scope – on the basis that their corporate and management structure are no different to “normal” corporate operating businesses.

The markets perceive the GOEF market segment as clearly distinguishable from the listed property sector, including REITs. Representatives for the listed property sector are the more recent initial public offerings by GSW, Alstria REIT and - outside Germany, but with German assets - Gagfah. Across Europe and globally, equivalent entities would be the likes of Unibail Rodamco (France), British Land (UK) and Simon Property Group (US).

### **Characteristics of GOEFs and listed property companies**

Annex I attached with this letter highlights and contrasts the key structural features of these two types of vehicle. Having undertaken this analysis, we are confident that the differences between the GOEFs and the corporate property sector are sufficiently clear and identifiable within the context of the German market, to enable a sensible interpretation of the scope of the AIFMD. The table should also provide useful indicators for distinguishing more generally

between funds and operating companies and thus contribute to establishing an agreed set of common criteria as a firm basis for sensible and consistent interpretation of the AIFMD at a European level.

G-REITs are property companies that are granted a particular corporate taxation status provided they comply with certain requirements (the main requirements being minimum levels of annual dividend distribution and maximum limits on non-real estate related business). If these conditions are not met, the REIT does not benefit from this tax treatment and is taxed like any other corporate property company. For the purposes of our analysis, we do not therefore distinguish between REITs and property companies and refer only to property companies.

### *Determining AIFMD scope for property businesses – “defined investment policy”*

The AIFMD seeks to regulate alternative investment fund managers, not all businesses carrying on commercial activities of a particular nature. Accordingly, our fundamental assumption, which we also understand to be that of the BAFIN, is that the objective of the legislator was not to scope within the AIFMD, **all commercial activity relating to real estate**<sup>1</sup>. An entity that owns and manages buildings – the core activity of a real estate company – should therefore only fall within the scope of the AIFMD if it is an investment fund. The fact that some real estate businesses are clearly fund managers and should therefore be regulated as such cannot mean that all real estate businesses should fall within the scope of the AIFMD.

Under the AIFMD, an AIF is defined as any collective investment undertaking, (including investment compartments thereof), not being an UCITS and raising capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors.

In our view, the term “defined investment policy” is critical in enabling regulators to distinguish between businesses engaged in fund management which belong within the scope of the AIFMD, and other businesses. A real estate fund management business (such as a GOEF) will always have a “defined investment policy” which it agrees with its investors and with which it must comply while it manages investors’ money. Investors in an operating property company, on the other hand, will generally have no agreement with the company’s management for any particular “defined investment policy”: the company’s management (like that of any other operating business) is free to determine its business strategy from time to time.

Our view is that the wording of the AIFMD (including in particular the focus on a “defined investment policy”), together with the identifiable features detailed in Annex I, provides the basis for establishing a distinction between property funds (such as GOEFs, which are within the scope of the AIFMD), and property companies (which should generally fall outside its scope), consistent with the objective of the legislation.

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<sup>1</sup> For example: - acquiring, developing, refurbishing, leasing, managing, marketing, selling real estate and all other real estate related services.

As shown in the attached Annex, the structure of an investment policy set up by a classical fund is significantly different from the general business purpose contained in the articles of association of a listed company which will be continuously interpreted by its Board. Following logical interpretation of the AIFMD, the term "defined investment policy" can only include those investment strategies which are agreed in advance between the fund management and the investor in the prospectus and subscription documents and where the investor therefore relies on the fact that no other investment decisions, except for those he has explicitly approved, will be adopted by the management. He will also rely on the fact that this investment policy is under review and scrutiny by the regulator authority (BAFIN).

By contrast, when an ordinary listed company raises money from investors through public offerings, the money it raises is its own and can be invested in accordance with a very broad strategy, as defined by its management board. A regulator will never be requested nor obliged to review those decisions. Unlike a fund, a listed company can be subject to, or be a participant in regular merger and acquisition activities with competitors or investors depending on the market's perception of its ongoing strategy and performance.

### **Conclusion**

In summary, we believe that a "defined investment policy for the benefit of the investors", as stipulated by AIFMD, should be interpreted as one which is (i) based on a written contractual arrangement between the investor and the fund manager as part of investor's decision to invest, (ii) cannot be changed without the prior approval of investors or regulatory authorities and (iii) is executed by the fund manager on behalf of and for the benefit of the investor. The above interpretation, combined with the identification of specific features at a national level along the lines of those detailed in Annex I, should enable a sensible interpretation of the legislation and draw a line between funds and normal corporate operating businesses, including the corporate property sector.

We trust you will find our comments to be helpful and welcome the opportunity to discuss this further with you at your convenience. If you have any questions please do not hesitate to call Gareth Lewis on +32 2739 1014.

Kind regards  
Yours sincerely



Philip Charls  
CEO  
EPRA  
[www.epra.com](http://www.epra.com)



Steve Wechsler  
CEO  
NAREIT  
[www.reit.com](http://www.reit.com)

cc. Axel Von Goldbeck CEO, ZIA

## German Open Ended Funds (GOEFs) and listed property companies

Issue	GOEFs	Listed Property Companies (including G-REITs)
<b>Legal form</b>	<u>No legal personality</u> <ul style="list-style-type: none"> <li>• Fund assets - clearly separated from those of the management in a legally separated pool of assets; no employees or staff</li> <li>• Fund manager - clearly identifiable and contractually bound to manage in accordance to a fund prospectus</li> </ul>	<u>Joint stock corporation</u> <ul style="list-style-type: none"> <li>• Capital divided into share capital</li> <li>• Listed on an organized stock market</li> <li>• Statutes established with own Board (Vorstand) staff and business infrastructure, staff resources</li> </ul>
<b>Operational term</b>	<u>Usually unlimited</u>	<u>Unlimited</u> <ul style="list-style-type: none"> <li>• Not established for an agreed limited period of life</li> </ul>
<b>Management</b>	<u>External</u> <ul style="list-style-type: none"> <li>• Managed by an external management company</li> <li>• Management company is mandated to strictly execute the contractual terms and conditions which define the legal relationship of the manager to the investors</li> <li>• Controls established to make sure there is no deviation from contractual terms</li> <li>• Regulatory body warrants to the public that conditions and terms are fully adhered to</li> </ul>	<u>Internal (Vorstand; Aufsichtsrat)</u> <ul style="list-style-type: none"> <li>• Managed internally by the Board in accordance with normal corporate governance</li> <li>• Supervised by a Supervisory Board (Aufsichtsrat) with important powers like nominating the Board Members and the "CEO" (Vorstandsvorsitzender)</li> <li>• Board has direct responsibility for defining and implementing the strategy to be adjusted and changed from time to - not bound to a prospectus' mission</li> <li>• Management must act in good faith and at its own discretion in the interests of the company, the shareholders as a whole, the employees and the public, including its reputation (section 76 I AktG; Hüffer § 76 AktG, 12). None of these goals have a specific priority so that within those multiple objectives the board can make decisions individually</li> <li>• Management is not mandated by the shareholders nor has to act solely in their interests - it has to represent those multiple goals</li> <li>• Annual shareholder meetings to approve certain key measures of policy and policy changes on the basis of present majority of votes</li> </ul>

Issue	GOEFs	Listed Property Companies (including G-REITs)
<b>Employees</b>	<u>Fund has no employees</u> <ul style="list-style-type: none"> <li>No legal personality – do not directly hire employees</li> <li>Manager employs staff as required for the management of the fund</li> </ul>	<u>Directly hired employees</u> <ul style="list-style-type: none"> <li>Company has its own permanent staff to run its business, covering back office (HR, IT, legal, etc.) and front office (property management, etc.)</li> <li>Employment infrastructure is created to serve the companies purpose indefinitely - it cannot be terminated other than by ordinary corporate insolvency or liquidation procedures</li> </ul>
<b>Structure</b>	<u>Open ended</u> <ul style="list-style-type: none"> <li>Fund size changes depending on investor demand; redemption schemes</li> </ul>	<u>Closed ended</u> <ul style="list-style-type: none"> <li>Fund size is effectively constant, with its value changing according to market pricing</li> <li>Equity raising in accordance with capital market rules and capital increase strategy as defined by Board</li> </ul>
<b>Investment/ disinvestment</b>	<u>Based on underlying asset values</u> <ul style="list-style-type: none"> <li>Subscription and redemption of units based on net asset value; secondary trading relatively rare</li> <li>Retail funds - accessible to all investors, with a view to offer redemptions as frequently as possible (legislation changed recently)</li> </ul>	<u>Based on price on the public markets</u> <ul style="list-style-type: none"> <li>Raising capital through stock exchange IPO - general offering of shares to the public, i.e. any investor who wishes to buy shares, the rules for which are harmonized in the EU already for many years.</li> <li>Shares principally traded in secondary market (i.e. on the stock exchange) with pricing set by that market</li> <li>Occasional use of ability to issue new shares to new or existing investors</li> </ul>
<b>Relationship with investors</b>	<u>Documented in a legal contract (prospectus/subsription documents) between the manager and unitholders</u>	<u>No contractual relationship with shareholders</u> <ul style="list-style-type: none"> <li>Investors are simply part owners of the company, with a proportionate right to distributions declared and assets on a winding up, and voting rights in general meeting</li> <li>Management is not mandated by the shareholders nor has to act solely in their interests - it has to represent multiple goals (continuation of company, employees, public interests)</li> <li>Annual shareholder meetings to approve certain key measures of policy and policy changes on the basis of present majority of votes</li> </ul>

Issue	GOEFs	Listed Property Companies (including G-REITs)
<b>Assets /Permitted activities</b>	<u>Fund assets continue to belong to investors</u> <ul style="list-style-type: none"> <li>Investments of the fund continue to belong to investors in the fund, the manager manages those investment on investors' behalf</li> </ul>	<u>Assets belong to the company</u> <ul style="list-style-type: none"> <li>Assets managed by companies on its own account</li> <li>Assets of any kind can be invested</li> <li>Company can invest in participations (non-assets) like minority or majority shares in subsidiaries (e.g. development activities, asset management, property management, facility management, technical equipment, fund management, administrative services)</li> </ul>
<b>Permitted activities</b>	<u>Additional business activities restricted</u> <ul style="list-style-type: none"> <li>Fund must only invest in assets delivering a return, ie. Fund composes of a diversified real estate assets portfolio only</li> </ul>	<u>Additional business activities possible</u> <ul style="list-style-type: none"> <li>Above activities can be provided also by Company itself</li> <li>Activities can be in relation to Company's assets or third party assets</li> </ul>
<b>Investment strategy</b>	<u>Specified in detail in the fund prospectus</u> <ul style="list-style-type: none"> <li>Deviation not allowed - management is answerable solely to investors</li> </ul>	<u>Determined by the Management Board</u> <ul style="list-style-type: none"> <li>Set by the Board, acting in good faith subject to fiduciary obligations to shareholders and other stakeholders</li> <li>Subject (in certain cases) to shareholder approval (e.g annual general meetings) – management has broad flexibility</li> </ul>
<b>Distribution policy</b>	<u>Specified in fund prospectus (subject to available profits)</u> <ul style="list-style-type: none"> <li>Minimum distribution of 50%</li> </ul>	<u>Determined by management (subject to distributable profits)</u> <ul style="list-style-type: none"> <li>Management decides based on strategic decisions to grow, invest in assets or people or infrastructure, research etc</li> <li>Legally distributable profits determined by International Accounting Standards (IFRS) and corporate law</li> <li>Only REITs have to observe certain minimum distributions - if they want to safeguard their tax privileges. Otherwise suffer penalties or they convert into the regular tax framework for corporates</li> </ul>
<b>Regulatory framework</b>	<u>Product focused</u> <ul style="list-style-type: none"> <li>Regulation by financial services regulator (BAFIN)</li> <li>Supervision and control framework through Audit, Valuation committee, depositary and BAFIN</li> </ul>	<u>Company law and listing rules</u> <ul style="list-style-type: none"> <li>Not product focused (as for other listed companies)</li> <li>E.g EU law requires IFRS audited financial statements</li> </ul>

Issue	GOEFs	Listed Property Companies (including G-REITs)
<b>Financing</b>	<u>Limitations (50%/30%) set to protect a low risk profile to the benefit of retail investors</u>	<u>Broad access to bank finance and to capital markets (as for other listed companies)</u>  <u>Flexible finance strategies at corporate or asset level including hedging, swaps, options etc.</u>