SUMMARY OF S. 1568: REIT IMPROVEMENT ACT OF 2003

- Congress created real estate investment trusts ("REITs") in 1960 to enable small investors to participate in real estate through professionally managed companies. REITs are corporations or business trusts that combine the capital of many investors to own, operate or finance income-producing real estate, such as apartments, storage facilities, hotels, shopping centers, offices, and warehouses.

- Publicly traded REITs are total return investments that typically provide high dividends, the potential for moderate, long-term capital appreciation, and a measure of portfolio diversification to investors from all walks of life. By law, REITs must distribute at least 90% of their taxable income, resulting in a regular and consistent income to shareholders. Additionally, studies have shown that because there is a relatively low correlation between REIT and publicly traded real estate stock returns and the returns of other market sectors, REITs provide a significant source of portfolio diversification.

- As described below, S. 1568, the REIT Improvement Act of 2003 (RIA), would help REITs by removing uncertainties in the application of the REIT rules, by ending discrimination against foreign investors in REITs, and by imposing monetary penalties for minor violations in lieu of catastrophic REIT disqualification.

- The RIA has three goals.

  ► To make a number of minor corrections in the REIT tax rules, including most importantly fixing an unintended problem arising from the REIT Modernization Act of 1999 that now causes a company to lose its REIT status by holding commercially ordinary debt, *e.g.*, a loan to a small tenant to finance tenant improvements.

  ► To conform the tax treatment of foreign institutional investors in publicly traded REITs to that of similar investment in other publicly traded companies and to conform the tax treatment of REIT capital gains distributions to foreign institutional investors to that of ordinary REIT distributions. The change would parallel the existing Tax Code rule for a foreigner's sale of a publicly traded REIT's stock.

  ► To provide the IRS with tools to impose monetary penalties for reasonable cause violations of REIT tests in lieu of the loss of REIT status. This is similar to a test that was enacted as part of the REIT Simplification Act of 1997, as well as "intermediate sanction" legislation Congress passed a few years ago for tax-exempt organizations.

- The RIA is the result of over two years of dialogue with the Joint Committee on Taxation, staff from the tax-writing committees and the Department of the Treasury.

- The RIA is projected to have a modest revenue cost of $147 million over ten years.

- As with past REIT legislation, the industry has attracted broad bipartisan support for the RIA.