by NAREIT

Frequently Asked Questions About REITs

Answers to fundamental questions about REITs

Real Estate Investment Trusts, or REITs, are a practical way for all investors to invest in large-scale, income-producing, professionally managed companies that own commercial real estate. As an investment, REITs historically provide portfolio diversification plus strong and reliable dividend income. Publicly traded REITs have demonstrated superior long-term risk-adjusted returns, as well as the liquidity and transparency of public capital markets. Here are answers to fundamental questions about REITs.

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REITs: Building Dividends and Diversification®

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The Basics of REITs

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What is a REIT?

A REIT is a company that mainly owns, and in most cases, operates income-producing real estate such as apartments, shopping centers, offices, hotels and warehouses. Some REITs also engage in financing real estate. The shares of many REITs are traded on major stock exchanges.

To qualify as a REIT, a company must have most of its assets and income tied to real estate investment and must distribute at least 90 percent of its taxable income to its shareholders annually. A company that qualifies as a REIT is permitted to deduct dividends paid to its shareholders from its corporate taxable income. As a result, most REITs remit at least 100 percent of their taxable income to their shareholders and therefore owe no corporate tax. Taxes are paid by shareholders on the dividends received and any capital gains. Most states honor this federal treatment and also do not require REITs to pay state income tax. Like other businesses, but unlike partnerships, a REIT cannot pass any tax losses through to its investors.

Why were REITs Created?

Congress created REITs in 1960 to make investments in large-scale, income-producing real estate accessible to average investors. Congress decided that a way for average investors to invest in large-scale commercial properties was the same way they invest in other industries — through the purchase of equity. In the same way shareholders benefit by owning stocks of other corporations, the stockholders of a REIT earn a pro-rata share of the economic benefits that are derived from the production of income through commercial real estate ownership. REITs offer distinct advantages for investors: portfolio diversification, strong and reliable dividends, liquidity, solid long-term performance and transparency.

How Does a Company Qualify as a REIT?

In order for a company to qualify as a REIT, it must comply with certain provisions within the Internal Revenue Code. As required by the Tax Code, a REIT must:

- Be an entity that is taxable as a corporation
- Be managed by a board of directors or trustees
- Have shares that are fully transferable
- Have a minimum of 100 shareholders
- Have no more than 50 percent of its shares held by five or fewer individuals during the last half of the taxable year
- Invest at least 75 percent of its total assets in real estate assets
- Derive at least 75 percent of its gross income from rents from real property or interest on mortgages financing real property
- Have no more than 25 percent of its assets consist of stock in taxable REIT subsidiaries
- Pay annually at least 90 percent of its taxable income in the form of shareholder dividends

How Many REITs are There?

As of Jan. 1, 2011, there were 153 REITs registered with the Securities and Exchange Commission in the United States that trade on one of the major stock exchanges — the majority on the New York Stock Exchange. These REITs have a combined equity market capitalization of $389 billion.

Additionally, there are REITs that are registered with the SEC but are not publicly traded, and REITs that are not registered with the SEC or traded on a stock exchange. Internal Revenue Service shows that there are about 1,100 U.S. REITs that have filed tax returns.

Characteristics of Publicly Traded REITs

	PUBLICLY TRADED REITS
Overview	REITs that file with the SEC and whose shares trade on national stock exchanges.
Liquidity	Shares are listed and traded, like any other publicly-traded stock, on major stock exchanges. Most are NYSE listed.
Transaction Costs	Brokerage costs the same as for buying or selling any other publicly traded stock.
Management	Typically self advised and self managed.
Minimum Investment Amount	One share.
Independent Directors	Stock exchange rules require a majority of directors to be independent of management. NYSE and NASDAQ rules call for fully independent audit, nominating and compensation committees.
Investor Control	Investors re-elect directors.
Corporate Governance	Specific stock exchange rules on corporate governance.
Disclosure Obligation	Required to make regular financial disclosures to the investment community, including quarterly and yearly audited financial results with accompanying filings to the SEC.
Performance Measurement	Numerous independent performance benchmarks available for tracking listed REIT industry. Wide range of analyst reports available to the public.

Characteristics of Non-Exchange Traded REITs and Private REITs

NON-EXCHANGE TRADED REITS	PRIVATE REITS
REITs that file with the SEC but whose shares do not trade on national stock exchanges.	REITs that are not registered with the SEC and whose shares do not trade on national stock exchanges.
Shares are not traded on public stock exchanges. Redemption programs for shares vary by company and are limited. Generally a minimum holding period for investment exists. Investor exit strategy generally linked to a required liquidation after some period of time (often 10 years) or, instead, the listing of the stock on a national stock exchange at such time.	Shares are not traded on public stock exchanges. Existence of, and terms of, any redemption programs vary by company and are generally limited in nature.
Typically, fees of 10-15 percent of the investment are charged for broker-dealer commissions and other up-front costs. Ongoing management fees and expenses also are typical. Back-end fees may be charged.	Varies by company.
Typically externally advised and managed.	Typically externally advised and managed.
Typically $1,000 - $2,500.	Typically $1,000 - $25,000; private REITs that are designed for institutional investors require a much higher minimum.
Subject to North American Securities Administrators Association (NASAA) regulations. NASAA rules require that boards consist of a majority of independent directors. NASAA rules also require that a majority of each board committee consist of independent directors.	Not required.
Investors re-elect directors.	Investors re-elect directors.
Subject to state and NASAA regulations.	Not required.
Required to make regular SEC disclosures, including quarterly and yearly financial reports.	Not required.
No independent source of performance data available.	No public or independent source of performance data available.

What Types of REITs are There?

The REIT industry has a diverse profile, which offers many investment opportunities. REITs often are classified in one of two categories: equity or mortgage.

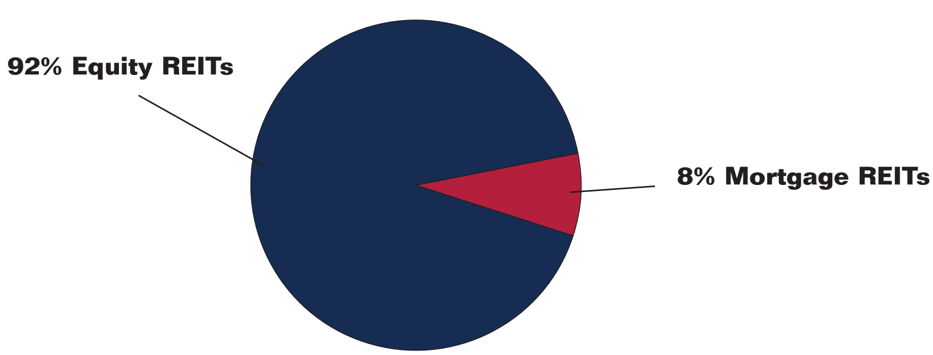
Equity REITs

Equity REITs mostly own and operate income-producing real estate. One major distinction between REITs and other real estate companies is that a REIT must acquire and develop its properties primarily for its own portfolio rather than to resell them once they are developed.

Mortgage REITs

Mortgage REITs mostly lend money directly to real estate owners and operators or extend credit indirectly through the acquisition of loans or mortgage-backed securities. Today's mortgage REITs generally extend mortgage credit only on existing properties. Many mortgage REITs also manage their interest rate and credit risks using securitized mortgage investments, dynamic hedging techniques and other accepted derivative strategies.

Types Of REITs



Listed REITs as of Feb. 1, 2011
Source: NAREIT®

Who Manages a REIT?

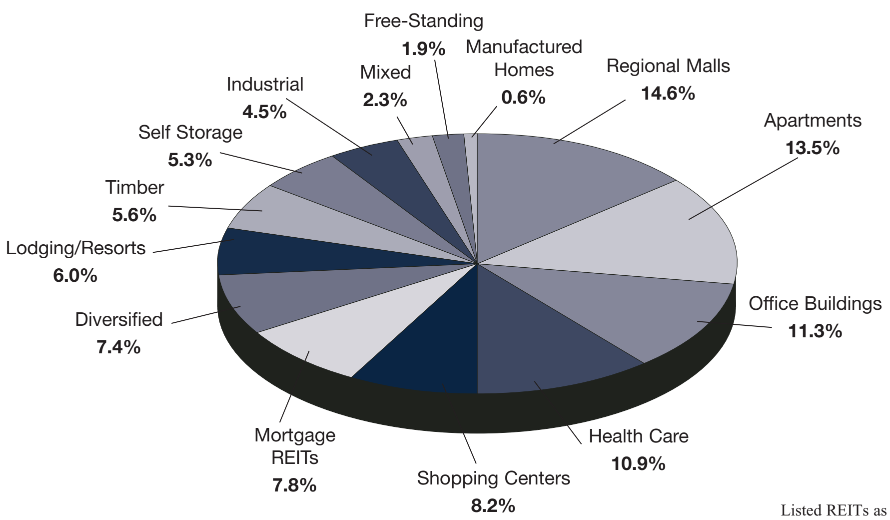
Like other publicly traded companies, a REIT's executive management team operates the company, deciding what properties it will own and manage. Management's decisions are overseen by a board of directors that is responsible to the shareholders. As with other corporations, REIT directors are typically well-known and respected members of the real estate, business and professional communities. Many of today's REITs became public companies within the past 15 to 20 years, often transforming to public ownership what previously had been private enterprises. In many cases, the majority owners of these private enterprises became the senior officers of the REIT and contributed their ownership positions to the REIT.

What Types of Properties Do REITs Own and Manage?

REITs own and manage a variety of property types: shopping centers, health care facilities, apartments, warehouses, office buildings, hotels and others. Most REITs specialize in one property type only, such as shopping malls, timberlands, data centers or self-storage facilities.

Some REITs invest throughout the country or in some cases, throughout the world. Others specialize in one region only, or even in a single metropolitan area.

Listed REITs Invest In All Property Types



Listed REITs as of Feb. 1, 2011
Source: NAREIT®

How Are REITs Different from Partnerships?

REITs are not partnerships. Most publicly traded REITs are vertically integrated real estate companies that develop, own and actively manage commercial real estate. Shares in these companies are traded, the same as other stocks, on major exchanges, providing complete liquidity and market pricing. Publicly traded REITs are subject to the same financial disclosure requirements as other publicly traded companies. Independent corporate governance consultants have rated the REIT industry's governance among the best of all U.S. industry groups.

Important Differences: REITs vs. Partnerships

	REITs	Partnerships
Liquidity	Yes; publicly traded REITs are listed on stock exchanges and trade throughout the day	No. When liquidity exists, generally much less than listed REITs
Minimum Investment Amount	None	Typically $2,000 - $5,000
Reinvestment Plans	Yes, including some at discounts	No
Ability to Leverage Property Investments without Incurring UBIT for Tax- Exempt Accounts	Yes. In most cases this makes REITs suitable for individual IRAs, 401(k), and other pension plans	No
Investor Control	Yes, investors re-elect directors	No, controlled by general partner who cannot be easily removed by limited partners
Independent Directors	Yes, stock exchange rules or state law typically require majority to be independent of management	No
Beneficial Ownership	At least 100 shareholders required; SEC-registered REITs have thousands	Shared between any number of limited and general partners
Ability to Grow by Additional Public Offerings of Stock or Debt	Yes	Rarely
Ability to Pass Losses on to Investors	No	Yes
Information to Investors	Form 1099	Schedule K-1
Subjects Investors to State Taxes	Only in state where investor resides	Yes, for all states in which it owns properties

How Do REITs Use Partnerships?

Like other industries, the real estate industry, including REITs, often uses partnerships to co-venture with others. In addition, REITs are typically structured in one of three ways: the traditional REIT, the umbrella partnership REIT (UPREIT) and the DownREIT.

A traditional REIT is one that owns its assets directly rather than through an operating partnership.

In the typical UPREIT, a REIT partners with others, and the partnership is termed the "operating partnership." In return for their respective contributions, the REIT as well as the other partners receive interests in the operating partnership called operating partnership units (OP units). The REIT typically is the general partner and the majority owner of the OP units. For the partners contributing property to the operating partnership, any capital gain tax liability is deferred until such time as the OP units are converted into common shares of the REIT.

After a period of time (often one year), the non-REIT partners may enjoy the same liquidity of the REIT shareholders by tendering their units for either cash or REIT shares (at the option of the REIT or operating partnership). This conversion may result in the partners incurring the tax liability that had been deferred at the UPREIT's formation. However, the unitholders may tender their units over a period of time, thereby spreading out such tax. In addition, when a partner holds the units until death, the estate tax rules operate in such a way as to provide that the beneficiaries may tender the units for cash or REIT shares without paying income taxes.

A DownREIT is structured much like an UPREIT, but the REIT owns and operates properties other than its interest in a controlled partnership that owns and operates separate properties.

Why Invest in REITs?

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Who Invests in REITs?

Individual investors of all ages, both in the U.S. and worldwide, invest in REITs directly or through REIT mutual funds. Other typical buyers of REITs are exchange traded funds, pension funds, endowments, foundations, insurance companies and bank trust departments.

Investors typically are attracted to REITs for their high levels of continuing current income and the opportunity for long-term growth. These are the basic characteristics of commercial real estate investment.

Today, a broad range of investors are using REITs to help achieve the investment goals of diversification, dividends, liquidity, performance and transparency.

Why Should I Invest in REITs?

REITs are total return investments. They typically provide high dividends plus the potential for moderate, long-term capital appreciation. Long-term total returns of REIT stocks are likely to be somewhat less than the returns of higher risk, high-growth stocks and somewhat more than the returns of lower risk bonds.

REITs are required by law to distribute each year to their shareholders at least 90 percent of their taxable income. Thus, REITs tend to be among those companies paying the highest dividends. The dividends come primarily from the relatively stable and predictable stream of contractual rents paid by the tenants who occupy the REIT's properties. Because rental rates tend to rise during periods of inflation, REIT dividends tend to be protected from the long-term corrosive effect of rising prices.

The low correlation of listed REIT stock returns with the returns of other equities and fixed-income investments varies over time. Thus, including listed REITs in your investment program helps build a more diversified portfolio.

REITs historically offer investors:

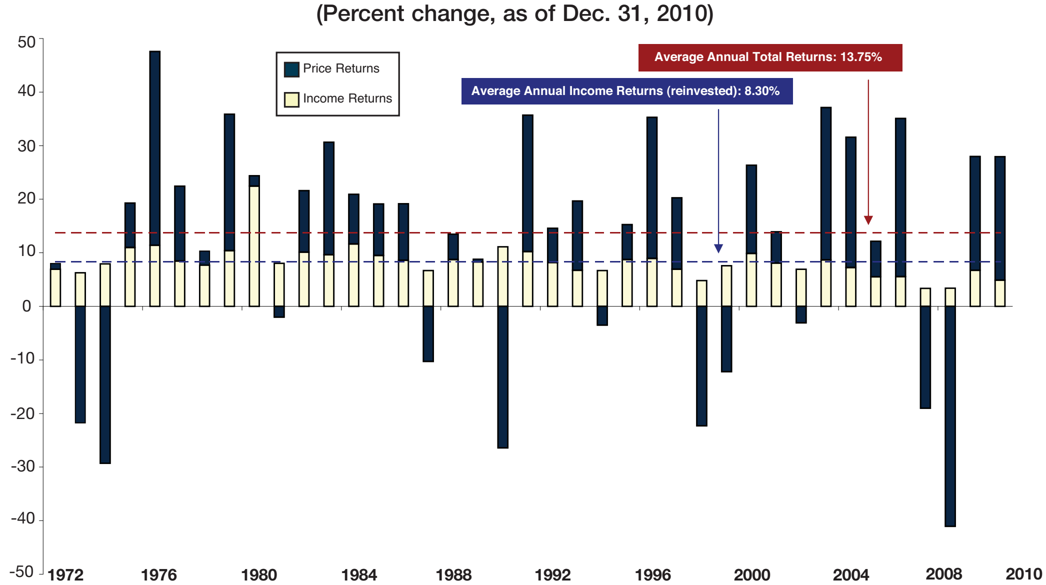
- Income & Long-term Growth: REITs provide competitive long-term rates of return that complement the returns from other stocks and from bonds.
- High Dividend Yield: Significantly higher on average than other equities, the industry's dividend yields historically have produced a

steady stream of income through a variety of market conditions.

- **Liquidity:** Shares of publicly traded REITs are readily converted into cash because they are traded on the major stock exchanges
- **Professional management:** REIT managers are skilled, experienced real estate professionals
- **Oversight:** Independent directors of the REIT, independent analysts, independent auditors, and the business and financial media monitor a publicly traded REIT's financial reporting on a regular basis. This scrutiny provides investors with a measure of protection and more than one barometer of the REIT's financial condition.
- **Disclosure obligations:** REITs whose securities are registered with the SEC are required to make regular SEC disclosures, including quarterly and yearly financial reports.

FTSE NAREIT All Equity REITs Return Components

(Percent change, as of Dec. 31, 2010)



Source: NAREIT

Is Homeownership a Substitute for Investing in REITs?

A house is a consumption good, not an investment, particularly when financed with a sizeable mortgage. It does not produce current income, but rather requires regular mortgage interest, real estate tax and insurance payments, plus other occasional expenditures, to be properly maintained.

In contrast, REITs represent investment in commercial real estate, which generates continuing income flow from rents.

A widely used index of single-family house prices nationwide gained 3.80 percent compounded on average from 1987 to the third quarter of 2010. Equity REITs, meanwhile, produced a 2.34 percent compound annual return on a price-only basis, but with dividends reinvested, REITs' compound annual total return for the same period was 9.54 percent.

Additionally, an investment in a REIT represents an investment that is diversified across a range of real estate properties in a variety of geographic locations. By comparison, a home's investment risk is not diversified, but rather highly concentrated in a single location.

The low correlation of REIT returns with house price returns, combined with the historically attractive total returns of REITs, make it no surprise that REITs show up in the optimal portfolios designed for both homeowners and renters.

How to Invest in REITs

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How Do I Invest in a REIT?

An individual may invest in a publicly traded REIT, which is listed on a major stock exchange, by purchasing shares through a securities dealer. As with other publicly traded securities, investors may purchase common stock, preferred stock or debt securities. An investor can enlist the services of a broker, investment advisor or financial planner to help analyze his or her financial objectives. These professionals may be able to recommend appropriate REIT investments for the investor. An investor may also contact a REIT directly for a copy of the company's annual report, prospectus and other financial information. Much of this information is available on a company's website. The website REIT.com lists most publicly traded REITs. Many financial websites and local libraries offer a wide range of investment research and information on REITs.

Another alternative is to diversify your investment further by buying shares in a REIT mutual fund or exchange-traded fund. A list of such funds also is available at REIT.com. Investors can compare and evaluate the performance of funds through information sources such as Morningstar®, Inc. These sources can offer detailed information on funds' past performance, current portfolio holdings and costs of investing.

What Should I Look for When Investing in a REIT?

The market usually rewards companies that demonstrate consistent earnings and dividend growth with higher price-earnings multiples. Thus, investors should look for REITs and publicly traded real estate companies with the following characteristics:

- A demonstrated ability to increase earnings in a reliable manner. For example, look for companies with properties in which rents are below current market levels. Such properties provide upside potential in equilibrium markets and downside protection when economic growth slows.

- Management teams able to quickly and effectively reinvest available cash flow. The ability to consistently complete new projects on time and within budget. Creative management teams with sound strategies for developing new revenue opportunities.

- Strong operating characteristics, including effective corporate governance procedures, conservative leverage, accepted accounting practices, strong tenant relationships and a clearly defined operating strategy for succeeding in competitive markets.

How Do REITs Measure Earnings?

Like the rest of corporate America, the REIT industry uses net income as defined under Generally Accepted Accounting Principles (GAAP) as the primary operating performance measure.

The REIT industry also uses funds from operations (FFO) as a supplemental measure of a REIT's operating performance. NAREIT defines FFO as net income (computed in accordance with GAAP) excluding gains or losses from sales of most property and depreciation of real estate. When real estate companies use FFO in public releases or SEC filings, the law requires them to reconcile FFO to GAAP net income.

Most real estate professionals as well as investors believe that commercial real estate maintains residual value to a much greater extent than machinery, computers or other personal property. Therefore, they view the depreciation measure used to arrive at GAAP net income as generally overstating the economic depreciation of REIT property assets and the actual cost to maintain and replace these assets over time, which may in fact be appreciating. Thus, FFO excludes real estate depreciation charges from periodic operating performance. Many securities analysts judge a REIT's performance according to its adjusted FFO (AFFO), thereby deducting certain recurring capital expenses from FFO.

NAREIT's April 2002 "white paper" on FFO discusses the definition in detail, advises REITs to adopt certain computational and disclosure practices and recommends that REITs disclose additional information about other financial calculations such as details on capital expenditures. The white paper is available at NAREIT's website, REIT.com.

How Do Investors Gauge a REIT's Ability to Pay Dividends?

Many investors often look at the payout ratio as the measure of a REIT's ability to pay its current dividends. Because real estate depreciation is a large non-cash expense that likely overstates any decline in property values, dividend per share divided by net income per share likewise understates a REIT's ability to sustain dividend payments. Therefore, the payout ratio, calculated as dividend per share divided by funds from operations (FFO) per share, or as dividend per share divided by adjusted funds from operations (AFFO) per share, is used by many as a more accurate measure of the REIT's ability to pay dividends.

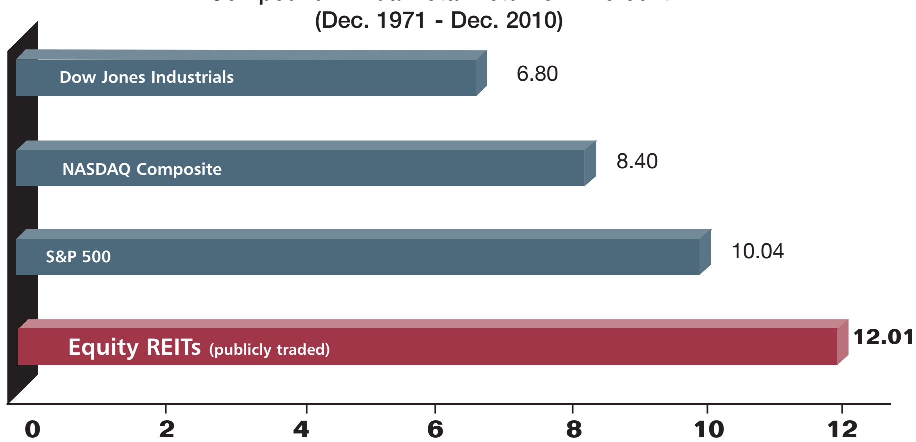
What Factors Contribute to REIT Earnings?

Growth in earnings typically comes from several sources, including higher revenues, lower costs and new business opportunities. The most immediate sources of revenue growth are higher rates of building occupancy and increasing rents. As long as the demand for new properties remains well balanced with the available supply, market rents tend to rise as the economy expands and increases demand for space. Low occupancy rates in underutilized buildings can be increased when skilled owners upgrade facilities, enhance building services and more effectively market properties to new types of tenants. Property acquisition and development programs also create growth opportunities, provided the economic returns from these investments exceed the cost of financing. Like other public companies, REITs and publicly traded real estate companies also increase earnings by improving operating efficiency and taking advantage of new business opportunities.

The REIT Modernization Act (RMA), which took effect on Jan. 1, 2001, provides REITs with other opportunities to increase earnings. Prior to the enactment of the RMA, REITs were limited to providing only those services that were long accepted as being "usual and customary" landlord services, and were restricted from offering more advanced services provided by other landlords. The RMA allows REITs to own taxable subsidiaries that can provide the competitive services that many of today's tenants desire, as well as to provide services like real estate asset management for other investors.

REITs Measure Up Over Time

Compound Annual Total Returns In Percent
(Dec. 1971 - Dec. 2010)



Source: NAREIT®
Past performance is no guarantee of future results.

How Are REIT Stocks Valued?

Like all companies whose stocks are publicly traded, REIT shares are priced by the market throughout the trading day. To assess the investment value of REIT shares, typical analysis involves one or more of the following criteria:

- Anticipated growth in earnings per share
- Anticipated total return from the stock, estimated from the expected price change and the prevailing dividend yield
- Current dividend yields relative to other yield-oriented investments (*e.g.,* bonds, utility stocks and other high-income investments)
- Dividend payout ratios as a percent of REIT FFO (see pages 16-17 for discussion of FFO and payout ratios)
- Management quality and corporate structure
- Underlying asset values of the real estate and/or mortgages, and other assets.

Stocks of REITs that are registered with the SEC but not publicly traded on an exchange should be valued in consultation with a qualified financial advisor.

What Real Estate Fundamentals Should I Consider Before Investing?

REIT investors often compare current stock prices to the net asset value (NAV) of a company's assets. NAV is the per share measure of the market value of a company's net assets. At times, the stock price of a REIT may be more or less than its NAV. Investors should understand some of the fundamental factors that influence the value of a REIT's real estate holdings. One critical factor is how well balanced is the supply of new buildings with the demand for new space. When construction adds new space into a market more rapidly than it can be absorbed, building vacancy rates increase, rents can weaken and property values decline, thereby depressing net asset values.

In a strong economy, growth in employment, capital investment and household spending increase the demand for new office buildings, apartments, industrial facilities and retail stores. Population growth also boosts the demand for apartments. However, the economy is not always equally strong in all geographic regions, and economic growth may not increase the demand for all property types at the same time. Thus, investors should compare the locations of properties of different companies with the relative strength or weakness of real estate markets in those locations.

Information on company properties is available at their websites, and links to these sites are available at REIT.com. Information on local and regional real estate markets is available in the financial press or at research sites on the Internet such as www.ppr.info or www.tortowheatonresearch.com.

What Role Do REITs Play in Retirement Savings Plans?

As the baby boom generation moves into its retirement years, a progressively larger segment of our society will come to depend on retirement plans for their income. Additionally, this population of retirees will be living longer. Unlike their parents and grandparents, today's 65-year-old retirees will have to live on their retirement benefits for an additional 20, 30 or even more years.

In the United States, the median life expectancy of a 65-year-old man and woman is 85 and 88, respectively. However, because the "median" represents the exact *mid-point* of the group's age range, *half* of this population will live longer, often much longer, than the median life expectancy.

The growing population of retirees who may spend a third or more of their lifespan in their retirement years is creating new challenges for retirement plan sponsors. Plan sponsors today must select investments that deliver a consistently high level of *income* to meet the current needs of the expanding crop of baby boom generation retirees, but also generate portfolio *growth* to ensure that the needs of retirees are met three decades in the future, and to offset the effects of *inflation* in the process.

Many plans are turning to increased allocations to real estate, including REITs, for solutions to these problems. The requirement that REITs pass at least 90 percent of their taxable income through to shareholders in the form of dividends makes them a strong income generating investment. However, as stocks, REITs also provide the opportunity for capital appreciation. This combination of investment characteristics makes them effective in extending the lives of retirement portfolios.

Taxes and REIT Investment

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How Do Shareholders Treat REIT Dividends for Tax Purposes?

For REITs, dividend distributions for tax purposes are allocated to ordinary income, capital gains and return of capital, each of which may be taxed at a different rate. All public companies, including REITs, are required early in the year to provide their shareholders with information clarifying how the prior year's dividends should be allocated for tax purposes. This information is distributed by each company to its list of shareholders on IRS Form 1099-DIV. An historical record of the allocation of REIT distributions between ordinary income, return of capital and capital gains can be found on NAREIT's website at REIT.com.

A return of capital distribution is defined as that part of the dividend that exceeds the REIT's taxable income. A return of capital distribution is not taxed as ordinary income. Rather, the investor's cost basis in the stock is reduced by the amount of the distribution. When shares are sold, the excess of the net sales price over the reduced tax basis is treated as a capital gain for tax purposes. So long as the appropriate capital gains rate is less than the investor's marginal ordinary income tax rate, a high return of capital distribution may be attractive.

Are REIT Dividends Subject to the 15 Percent Maximum Tax Rate?

In May 2003, the U.S. Congress passed the Jobs and Growth Tax Relief Reconciliation Act, which cut income tax rates on most dividends and capital gains to a 15 percent maximum through 2010. Because REITs do not generally pay corporate taxes, the majority of REIT dividends continue to be taxed as ordinary income up to the maximum rate of 35 percent.

However, REIT dividends will qualify for a lower tax rate in the following instances:

- When the individual taxpayer is subject to a lower scheduled income tax rate;
- When a REIT makes a capital gains distribution (15 percent maximum tax rate), or a return of capital distribution, as described on page 23;
- When a REIT distributes dividends received from a taxable REIT subsidiary or other corporation (15 percent maximum tax rate); and
- When permitted, a REIT pays corporate taxes and retains earnings (15 percent maximum tax rate).

In addition, the maximum 15 percent capital gains rate applies generally to the sale of REIT stock.

Available data indicate that about 23 percent of REIT dividends qualified for the lower 15 percent capital gains rate in 2009. Of this amount, 57 percent represented capital gain distributions and 43 percent represented return of capital, which is taxed at a capital gain rate when the stock is sold.

How Do the "Section 1031 Like-Kind Exchange" Rules Affect REITs?

Section 1031 of the Internal Revenue Code generally permits tax deferral when investment property or property used in a trade or business is exchanged for "like-kind" property as long as the exchange is completed within 180 days of the transfer of the taxpayer's exchanged property. Non-simultaneous exchanges also are permissible under section 1031 if certain criteria are met. These exchanges are known as "like-kind exchanges." An example of a like-kind exchange would be an exchange of an apartment building in Baltimore for an apartment building in San Diego. Consequently, REITs routinely use section 1031 in conducting their own investment operations.

However, REIT stock does not qualify as investment property, and accordingly, it is not possible to effect a like-kind exchange of real estate for REIT stock. Although REIT stock cannot qualify for like-kind exchange treatment, another provision of U.S. tax law (Section 721 of the Internal Revenue Code) does permit owners of real property to exchange their property for partnership interests on a tax-deferred basis if certain conditions are met. Relying on this provision, many REITs own the majority, if not all, of their properties through an operating partnership (OP) in which they hold the majority interests. The operating partnership most often pertains to an umbrella partnership REIT or (UPREIT), but also may pertain to a DownREIT.

From time to time, real estate owners may transfer properties on a tax-deferred basis to an OP in exchange for OP units. The OP units ultimately are exchangeable into REIT stock or cash in a taxable transaction, and they allow their owners to receive partnership distributions typically similar to the REIT distributions they would receive had they converted the OP units into REIT stock. The Web sites of many REITs contain information about transfers of properties in exchange for OP units.

What is "Unrelated Business Taxable Income" (UBTI) and Can REIT Dividends Constitute UBTI?

In very general terms, "unrelated business taxable income" (UBTI) is income earned by an otherwise tax-exempt entity that is considered taxable income to the entity, typically because it is derived from a business activity unrelated to the tax-exempt purpose of the entity. For example, an individual retirement account (IRA) is typically considered tax-exempt, but if it earns UBTI, it must pay tax on that income.

In general, REIT dividends do not generate UBTI (at least no more than dividends from non-REIT stocks). See Revenue Ruling 66-106, in which the IRS specifically held that dividends from a REIT generally do not generate UBTI; and Revenue Ruling 2006-58, which held that a charitable remainder trust is not subject to unrelated business taxable income as a result of being allocated excess inclusion income from a REIT. Nevertheless, there are exceptions to the general rule, such as when a pension plan owns more than 25 percent of a REIT's stock and in the case of certain mortgage REITs that use financings considered to be "taxable mortgage pools."

Because the answers to these questions are complex, it is important to consult with a competent tax advisor for answers applicable to your specific situation.

Global Real Estate Investment

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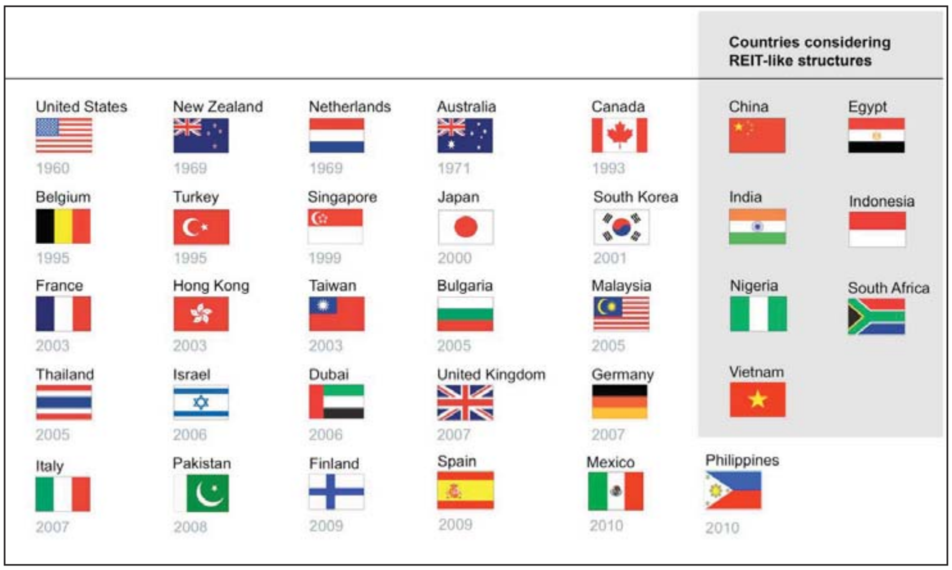
How is the Global Listed Property Market Configured?

While the U.S. remains the largest and most efficient listed real estate market, the listed real estate market is increasingly becoming global. The growth is being driven, importantly, by the appeal of REITs. More than 30 countries now have REIT legislation, and more are exploring it.

Global REIT Chronology

Countries with Existing REIT-Like Structures



The most comprehensive index for the REIT and global listed property market is the FTSE EPRA/NAREIT Global Real Estate Index Series, which was created jointly by the index provider FTSE Group, NAREIT and EPRA, the European Public Real Estate Association. The index is used by a variety of institutional investors, money managers and funds to manage real estate investment on a global basis. It contains both REITs and non-REIT listed property companies. The Global Index Series contains the Developed Markets indicies and the Emerging Markets indicies.

As of Dec. 31, 2010, the FTSE EPRA/NAREIT Developed Market Real Estate Index included more than 282 listed real estate companies in 21 countries around the globe. On an equity market capitalization basis, approximately 45 percent of the index's value was in North America; approximately 39 percent was in Asia; and approximately 16 percent was in Europe.

The FTSE EPRA/NAREIT Emerging Market indices provide investors with a diverse representation of more than 89 publicly traded equity REITs and listed property companies from 14 emerging markets across the Americas, Europe, the Middle East, Africa and Asia.

What Benefit Does a Global Listed Real Estate Allocation Provide in a Global Investment Portfolio?

Research done by the investment consulting firm Ibbotson Associates showed that an allocation to global listed real estate improves the returns of a global investment portfolio.

Ibbotson charted risks and returns for various asset classes (stocks, bonds, real estate and cash) for the period 1990-2007 and constructed optimized portfolios of these assets – with and without an allocation to global listed real estate – at a variety of levels of portfolio risk (volatility). The firm's research showed that the addition of global real estate boosted the returns of portfolios throughout the risk spectrum. For example, an optimized portfolio of moderate risk (defined by a 10 percent standard deviation) produced an average annual return of 9.9 percent without a global real estate allocation, and 10.9 percent with a 20 percent global real estate allocation – an increase of 102 basis points.

Both the historical and forward-looking analyses concluded that U.S. real estate should be between one-third and two-thirds of the real estate allocation in an optimized global portfolio.

How Can I Add a Global Listed Real Estate Allocation to My Portfolio?

The easiest and most cost-efficient way to add a global listed real estate allocation to a portfolio is purchasing an investment in a mutual fund or exchange-traded fund of these securities. A list of such funds can be found at REIT.com.

Glossary of REIT Terms

Adjusted Funds From Operations (AFFO) — This is a measure of a real estate company's cash flow generated by operations. AFFO is usually calculated by subtracting from funds from operations (FFO) certain "non cash" revenues and expenses and normalized recurring expenditures that are capitalized by the REIT and then amortized, but which are necessary to maintain a REIT's properties and its revenue stream (*e.g.*, new carpeting and drapes in apartment units, leasing expenses and tenant improvement allowances). This calculation also is called cash available for distribution (CAD) or funds available for distribution (FAD).

Capitalization Rate — The capitalization rate (cap rate) for a property is determined by dividing the property's net operating income by its market value (or purchase price). Generally, high cap rates indicate higher returns on investment.

Cost of Capital — The cost to a company, such as a REIT, of raising capital in the form of equity (common or preferred stock) or debt. The cost of equity capital generally is considered to include both the dividend yield as well as the expected equity growth either by higher dividends or growth in stock prices. The cost of debt capital generally is the after-tax interest expense on the debt incurred.

DownREIT — A DownREIT is structured much like an UPREIT, but the REIT also owns and operates properties other than its interest in a controlled partnership that owns and operates separate properties.

EBITDA — Earnings before interest, taxes, depreciation and amortization. This measure is sometimes referred to as net operating income (NOI).

Elective Stock Dividend — Elective stock dividends are dividends comprised of a combination of cash and stock. Under IRS Revenue Procedure 2008-68, so long as a REIT provides its shareholders with a choice between cash or stock (and so long as at least 10 percent of the total dividend is available in cash), the entire dividend distribution is treated as a distribution of cash for purposes of the tax rules to qualify as a REIT.

Glossary of REIT Terms

Equitization — The process by which the economic benefits of ownership of a tangible asset, such as real estate, are divided among numerous investors and represented in the form of publicly traded securities.

Equity Market Cap — The market value of all outstanding common stock of a company.

Equity REIT — A REIT which owns, or has an "equity interest" in, income-producing real estate (rather than making loans secured by real estate collateral).

Funds From Operations (FFO) — The most commonly accepted and reported supplemental measure of REIT operating performance. Equal generally to a REIT's net income, excluding gains or losses from sales of property or debt restructuring, and real estate depreciation charges.

Implied Equity Market Cap — The market value of all outstanding common stock of a company plus the value of all UPREIT partnership units as if they were converted into the REIT's stock. It excludes convertible preferred stock, convertible debentures and warrants even though these securities have similar conversion features.

Leverage — The amount of debt in relation to either equity capital or total capital.

Mortgage REIT — A REIT that makes or owns loans and other obligations that are secured by real estate collateral.

Net Asset Value (NAV) — The net "market value" of all of a company's assets, including but not limited to its properties, after subtracting all its liabilities and other obligations.

Positive Spread Investing (PSI) — The ability to raise funds (both equity and debt) at a cost significantly less than the initial returns that can be obtained on real estate acquisitions.

Real Estate Investment Trust Act of 1960 — The federal law that authorized REITs. Its purpose was to allow small investors to pool their investments in real estate in order to get the same benefits as might be obtained by direct ownership, while also diversifying their risks and obtaining professional management.

Glossary of REIT Terms

Real Estate Investment Trust (REIT) — A REIT is a company dedicated to owning and, in most cases, operating income-producing real estate, such as apartments, shopping centers, offices and warehouses. Some REITs also are engaged in financing real estate.

Securitization — Securitization is the process of financing a pool of similar but unrelated financial assets (usually loans or other debt instruments) by issuing to investors security interests representing claims against the cash flow and other economic benefits generated by the pool of assets.

Straight-lining — Real estate companies such as REITs "straight-line" rents because generally accepted accounting principles require it. Straight-lining averages the tenant's fixed rent payments over the life of the lease.

Total Market Cap — The total market value of a REIT's (or other company's) outstanding equity securities and indebtedness.

Total Return — A stock's dividend income plus capital appreciation, before taxes and commissions.

UPREIT — In the typical umbrella partnership REIT (UPREIT), the partners of the existing partnerships and a REIT become partners in a new partnership termed the operating partnership. For their respective interests in the operating partnership (OP units), the partners contribute the properties from the existing partnership and the REIT contributes the cash proceeds from its public offering. The REIT typically is the general partner and the majority owner of the operating partnership.

After a period of time (often one year), the partners may enjoy the same liquidity of the REIT shareholders by tendering their OP units for either cash or REIT shares (at the option of the REIT or operating partnership). This conversion may result in the partners incurring the tax deferred at the UPREIT's formation.

Learn more at:

REIT.com™
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Information is based on quarterly net total returns of FTSE NAREIT Equity REIT Index, the National Council of Real Estate Investment Fiduciaries' (NCREIF) Open-End Diversified Core Equity (ODCE) Funds Index and NCREIF/Townsend Fund Indices, 1992q1-2010q3. Fees and expenses are assumed to be 50 bps per year for publicly traded equity REITs, and fees and expenses for core, value added and opportunistic funds are as reported by NCREIF. However, actual REIT fees and expenses may be higher or lower, which could affect significantly the stated portfolio results. All REIT data are derived from, and apply only to, publicly traded securities. While such data is believed to be reliable, data is subject to change or restatement. NAREIT does not warrant or guarantee for the accuracy or completeness of such data, and shall not be liable for such data or any errors or omissions therein.

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