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REIT Regimes in EU Countries – Institutional Environment versus Attractiveness of Real Estate Investment Vehicles*

Abstract

Substantial changes in the financial regulation of indirect real estate market are highly visible in EU countries over the past decade. Recent regulation amendments enabled structuring of real estate investment vehicles exempt from taxation on entity level with the purpose of increasing investments in real estate markets Most of initiatives for establishing tax transparent real estate investment vehicles have followed United States REIT (Real Estate Investment Trust) model, with legal adaptation in order to conform with domestic law traditions and market structures. Comparison of introduced formats indicates their heterogeneity with negative consequences for European indirect real estate market development and integration. Law and finance literature suggests importance of differences in regulatory regimes but papers relating quality of legislation and performance of specific organizational formats are scarce. In this paper we argue that certain legislative provisions are key determinants of real estate investment vehicles attractiveness and consequent commercial real estate market development.

Keywords: indirect real estate investments, REIT, tax transparent investment vehicle, regulatory regimes, commercial real estate market

1 Introduction

Frequent contractions on real estate markets in the first half of the last century resulted in the withdrawal of capital from real estate investments. The effects of shrunk investment gradually grew stronger and the need for redefining the manner of investment into real estate became more obvious. A search to increase liquidity of real estate investment was identified as the key issue in promoting real estate as a separate asset class. With the purpose of neutralizing

* This paper is part of research project Croatian Financial Markets and Institutions in the Process of EU Accession supported by Ministry of Science, Education and Sports of the Republic of Croatia, project number - 081-0811403-1411

negative characteristics of direct investment, new indirect investment forms have emerged which positively transformed specific real estate investment characteristics. Transformation of direct real estate investment into indirect investment vehicles is often described by the term of real estate securitization. Indirect investments, as opposed to direct ones (real estate ownership), suppose investment into financial assets derived from real estate. Financial assets appear in various forms of financial instruments, but the term primarily refers to marketable securities. Usage of the term indirect property vehicles is typical of British authors, while American ones mostly use the term public real estate market to describe indirect segment.

Indirect real estate investment records global development in the past several decades. The growth of investment in real estate through public investment forms has brought about an increase in the transparency of prices with much greater market liquidity in comparison with direct investment. Development of indirect investment vehicles is equally important for all investor groups. Small private investors, who face limited entry into direct markets due to required investment capital, are able to participate on indirect markets with small investment amounts. An increased exposure to real estate of institutional investors began in 1970s as a consequence of two important factors: introduction of regulatory provisions on mandatory diversification of asset portfolios and a simultaneous quick development of real estate securitization. In recent years real estate is becoming more and more represented in asset portfolios due to institutional investors' focus on total return (investment with prominent income and capital component) and increase in targeted allocation of real estate in the portfolio (Hoesli and Lekander, 2005).

There are several models of regulated collective schemes designed for investment into real estate, which in spite of differences regarding regulatory framework and market conditions in particular countries can be put under a common denominator of “real estate investment funds“. The development of regulated collective forms for investing into real estate began in 1960 with the appearance of REIT (REAL Estate Investment Trust) model in the USA. Until 1990s, only a few countries had introduced a special regulation for real estate funds. Original investment formats were based on American model (Australia, Netherlands) or on already existing models for investing into securities (Switzerland, Germany). As late as in 1990s, when REIT regimen became generally accepted as a quality regulation, its introduction into numerous countries began. In the early years, the reasons for introducing a regulation were mostly described by the need for participation of small investors on real estate investment markets with a tax treatment identical to the treatment of direct investment. The success of REITs in USA led regulators in other countries to put all the more ambitious goals in front of this organizational scheme, e.g. a more efficient market evaluation and allocation of the capital; easier access to commercial real estate market; increased tax transparency; decreasing of real estate finance through banking loans; participation of institutional investors on residential real estate market etc. (HMRC, 2006).

A legal transplantation of the REIT regime has been performed with adjustments regarding legal tradition and market conditions which negatively influenced market perception of the newly adopted formats and fulfillment of regulatory objectives. Introduction of REIT regime is followed by an increase in publicly quoted real estate investment vehicles, but their long term market life is connected with clearly defined propositions which determine their activity. The paper aims to define propositions for quality regulation of tax transparent real estate instruments through an overview of regulatory models with proven market success. Our desire is to contribute to better understanding of the influence of insitutional environment on organizaitonal formats and encourage empirical research of regulation and market perception which may be useful to policymakers, real esatate managers and finally, investors.

2 Regulations of Real-Estate Funds in US and EU

Regulation defines allowed organizational structure in relation to targeted investment profile of collective investment schemes. Competitiveness of organizational structures is mostly encouraged by tax privileges which aim to abolish discrimination in the taxation of indirect investment over direct investment. The reasons for such specific treatment in the taxation of investment funds are the following (Thuronyi et al., 1998): absence of specific tax regulations results in double taxation which limits development of funds; neutrality of tax regulations relevant for investment decisions; foundation of fiscal regimes on the flow of information between authorized managers and tax administration; assessment of the impact of alternative tax regimens. Regulated structures (funds, corporations) which are exempt from taxation at the entity level are subsumed by the term “tax transparent investment vehicles“. In addition to tax exemption, the regulatory framework also covers (Brown, 2006): establishment of funds; limitation of investment activities; demand for reports and supervision of the conformity between regulatory provisions and business practice. Real estate funds are often regulated separately due to specific investment nature of the real estate. A trade-off between operative limitations and tax privileges is characteristic for all types of funds, but is of special importance in tax transparent real estate investment vehicles because certain regulatory provisions annul the advantages of the preferred tax status. The historic development of real estate funds in the remainder of this paper stresses the relationship of regulatory issues and market reactions

2.1 Evolution of REIT Industry in USA

REIT (Real Estate Investment Trust) is an investment entity created for investments into real estate with a privileged tax status after meeting legal criteria related to organizational, investment and operative aspects. Various demands and limitations were prescribed in order to ensure special status only to business organizations which derive income from passive real estate investments and distribute majority of taxable income through dividends. REITS are mostly classified according to the type of investment property. Three basic categories of REITs are: Equity REITs, Mortgage REITs and Hybrid REITs. Equity companies are the predominant category of REITs. Their activity is based on direct ownership of commercial real estate and/or indirect ownership through shares in partnerships; majority of their income is generated through letting the real estate. Mortgage companies deal with direct financing of real estate by issuing mortgage loans and/or indirect financing by investing into mortgage securities. The operation of hybrid REITs combines the activities of equity and mortgage companies.

The history of REITs begins in 1960 when American Congress adopted a law (Real Estate Investment Trust Act) which allowed incorporation of this type of investment companies. Legislative framework has been modified several times to remain in tune with market demand as well as to underline privileges other than tax transparency (Madlem and Sykes, 2000): high and stable yield; potential for attractive total return; liquidity, professional management; risk mitigation by diversification of portfolio; regular market supervision of the performance. Legal provisions may be grouped into the following categories (Imperiale, 2006):

- Organizational form and ownership structure – REIT must be founded in the form of a taxable corporative entity which is managed by an authorized body. It must have at least one hundred shareholders and not more then 50% of shares may be owned by five or fewer persons.

- Assets – REIT must have at least 75% of assets in the form of real estate, government bonds and liquid monetary instruments at the end of each fiscal year. The REIT may not have more than 25% of assets in the form of securities issued by other issuers. The value of securities of a particular issuer may not exceed 5% of the total value of the REIT's assets. The REIT may not own more than 10% of shares issued by a single other issuer[1],
- Income – REIT must derive at least 75% of its gross income from business activities related to real estate. The fund many not derive more that 30% of its annual gross income from the sale of real estate which it has owned for less than four years and shares which it has owned for less that six months.
- Income distribution – REIT must pay out at least 90% of its annual taxable profit in dividends. If the proposition on mandatory distribution is met, the REIT may deduce the dividend paid-out from its tax duty on the basis of a federal income tax.

Regulatory reforms important for REIT industry in the USA commenced in early 80s with the passing of Economic Recovery Act, which introduced tax privileges for certain real estate investment forms[2]. The Act set in motion an investment avalanche, which resulted in the escalation of real estate prices and gradual fall of the yield rate. Only a few years later, the consequences of overbuilding led in turn to the revocation of privileges by the Tax Reform Act from 1986. The Act was a turning point in the development of REIT industry as it allowed such companies to be vertically integrated and to internally manage real estate portfolios. The legislation which mandated external management had been a limiting factor of REITs further development for a long time. Funds were not allowed to internalize their management function which turned out to be the main reason for the interest conflict between external management and shareholders. Given the opportunity for internal management, the efficiency of management and congruence of structure with market demand were significantly enhanced. The index of total return grew by 149% from 1991 to 1995, while market capitalization increased from 8.5 billion USD to 56 billion USD. This period is also characterized by a great increase in the share of equity REITs from 64% of total capitalization at the end of 1990 to 87% at the end of 1995 (Wang and Erickson, 2003.). The major growth factor of equity funds was the appearance of UPREIT[3] organizational form which facilitated the acquisition of real estate. UPREIT companies are characterized by the ownership of the shares in "operative partnerships". Operative partnerships are formed in such a way that existing partnership structures bring real estate portfolio into the operative partnership, while the contribution of REITs pertains to monetary funds which are collected by initial public offering. The shares which real estate owners hold in operative partnerships are interchangeable for money or shares in REIT funds following the expiration of an agreed period. REITs are always a major partner and largest shareholder in operative partnership. UPREIT structure was established in order to encourage transfer of existing partnerships into REITs with option to defer tax obligations while REITs were enabled to create portfolios without significant employment of their own funds. Introduction of UPREIT structure is generally considered to be the most important factor in the sudden growth of REIT industry in the 90s.

In addition to the new organizational form, the greatest impact on industry growth had the amendment of regulations which limited the investment of pension funds into REITs. The change in regulations resulted in an increase of investment into the REIT sector by pension funds, which in turn attracted a larger investment community to REIT shares. A weak participation of institutional investors in the ownership structure, changed in a short time in such a way that institutional investors became predominant (Ziest, Sirmans and Friday, 2003). The third significant characteristic of that period was an increase in the number of

[1] Not applicable to shares in other REIT companies and own subsidiaries.
[2] Privileges pertained to Real Estate Limited Partnerships.
[3] UPREIT - Umbrella Partnership Real Estate Investment Trusts

funds which specialized in particular real estate sectors (residential real estate, offices, shopping centers, industrial real estate, hotels etc.). This resulted in an increased efficiency of the management and better business performance. Further key changes happened at the end of the 90s through legal provisions which updated the Law from 1960[4]. Besides other changes, certain provisions were eliminated which had previously excluded the income derived from letting from a tax exempt category whenever REIT performed services for lessees that had not been considered tax exempt; taxes at investor's level on receipts related to retained capital gains were abolished and the rule that a REIT could not derive more than 30% of its total income from the sale of assets which were not considered a long term investment asset was again introduced.

Introduction of positive legal changes coincided with a prominent bear market. Therefore, equity REIT funds in the last two years of last century (occurring for the first time from 1971 to 1975) registered consecutive negative total annual yields. The decline was preceded by two spectacular years, 1996 and 1997, in which total yields reached +35.3% and +20.3%, respectively[5]. Such swift turnaround of the market trend again shook the reputation of REITs. Towards the end of 1999, the shares of most REIT funds were traded at a discount of 20% to 25% of the net asset value, while US commercial real estate market saw an increase in the occupancy rate and rent level as a consequence of strong economic growth. The arrival of a new century marked a new favorable period for REITs which stretched through the first five years. REITs recorded total yields of 26.4% as early as in the year 2000. Positive results continued in the following years, with annual yields between 3.8% and 37.1% between 2001 and 2006. The price of REITs shares in this period did not correspond to the conditions in commercial real estate markets. This can be thought of as the mature developmental phase in which investors recognized advantages of REITs such as the stability of annual dividend yields and a low correlation with other asset classes[6].In a twenty-five year period (1981-2005) REITs achieved 13.23% in the average annual rate of total return[7]. Graph 1 show that 9.02% of total yield (68% of the average annual total return) was realized from dividends. In the mid 2007 the long term successful period for the REIT industry ended with the appearance of the large global financial crisis originating in the US mortgage market. The year 2008 was the second worst year (1974 being the first one) in almost a fifty-year-long history of REITs with a fall of total return of 37.3%. In the USA there were 136 public REIT funds operating at the end of 2008 with a total market capitalization of 191.6 billion USD. The size of the crisis is best illustrated by a fact that at the end of 2006 there were 183 REITs with market capitalization over 438 billion USD. Another great turnaround occurred during 2009 and 2010 when the entire industry grew at high rates of 27.5% and 27.6%, respectively, proving the vitality of the REIT model.

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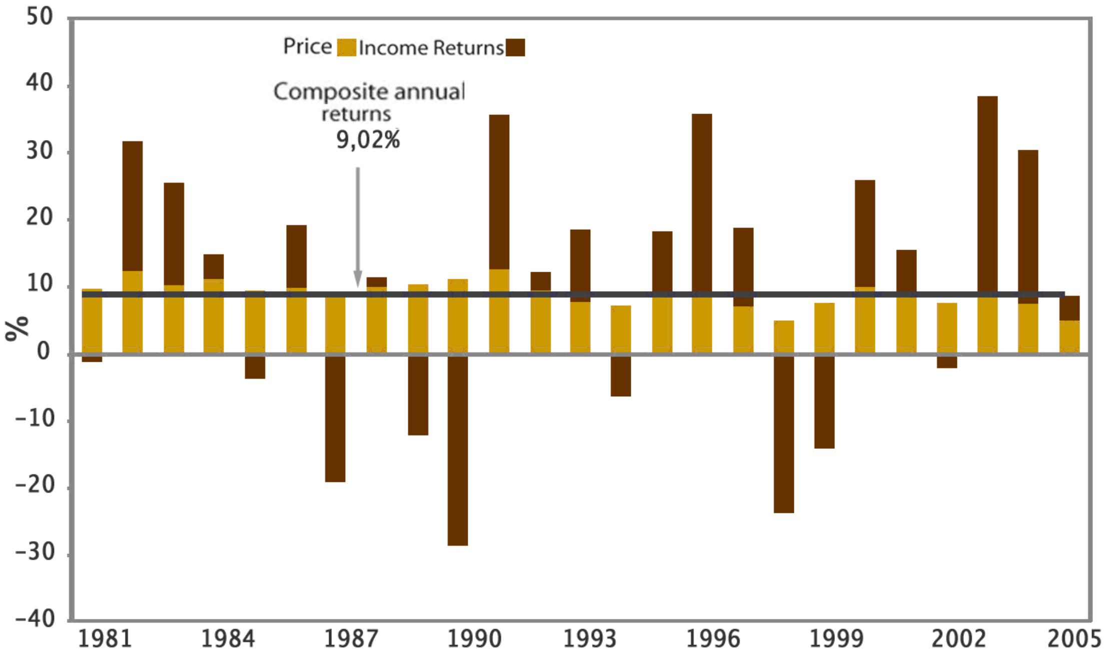
[4] Referrs to REIT Simplification Act from 1997 and REIT Modernization Act from 1999

[5] Data for a total annual yields are taken from the Internet page of American National REIT Association (NAREIT). Data for all companies relate to FTSE NAREIT All REITs Index and for equity companies to FTSE NAREIT All Equity REITs Index.

[6] REIT industry is often considered as a separate asset class.

[7] Refers to FTSE NAREIT Composite Index.



Graph 1: REITs Annual Total Returns (1981-2005)
Source: NAREIT - FTSE NAREIT U.S. Real Estate Index Historical Values & Returns

2.2 Tax Transparent Real Estate Vehicles in EU

EU is moving in the direction of creating a single market for investment funds which should become a recognizable product of the European financial industry. A group of EU directives which aim to allow activity of investment funds on the entire market with a single authorization of a particular member country is titled UCITS (Undertakings for Collective Investment in Transferable Securities). Real estate funds are not included in UCITS and are classified as "non-harmonized funds" that are characterized by national regulation and generally greater flexibility of the investment policies. The term "non-harmonized funds" pertains to a very heterogeneous group of investment products which covers several types of alternative investment funds[8] as well as traditional types of funds which do not fall under UCITS for various reasons.

Structures of real estate funds in EU member countries are significantly divergent in terms of operative demands, investment rules and financial limitations. A comparison of different structures points to the lack of a common European regulation which negatively influences Pan-European real estate investment flows and commercial real estate market integration. Eicholtz and Kook (2007) list the following negative consequences of the current situation: distortion of the competition due to different market environments; limitation of cross-border investment and consequential diversification in the whole spectrum of real estate sector on domicile markets (lack of specialization); negative impact on investment performance of limited geographic diversification; discrimination of investors from smaller countries without tax transparent structures; suboptimal allocation of assets into real estate; and negative influence on market stability and investment security.

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[8] The so called alternative investment funds usually imply real estate funds, hedge funds and private equity funds.

The most famous European model of a tax transparent real estate fund is German regulatory regime for open real estate investment funds (Offene Immobilienfonds). Open funds represent assets with no legal personality that are governed by a managing company and enjoy tax exempt status. The shares of open funds are not traded on secondary market, but their buying and selling is done exclusively through the management company (Focke, 2006). The mechanism of mandatory buyout of investment shares, as a mode of maintaining liquidity, completely defines the investment profile of open real estate funds since their yields are defined by the movement of net asset value. Net asset value is determined by the rent income, real estate maintenance cost and the real estate market value. Real estate market value is determined periodically (at least once a year) by an independent assessment body. The assessment mostly employs the income approach according to the principle of “long term sustainable value“ which results in a significant “smoothing“ of real estate price dynamics and often strongly differs from market prices. A low oscillation of the asset value guarantees relative stability of return which in combination with tax transparency determines the investment profile of the open funds in the direction of stable long term investments. Measurement of asset value by valuation methods is the most controversial element of German open funds which is linked to the great “liquidity crisis“ in 2004-2005. Buy out of investment units was suspended for the first time in history due to a massive requests and the procedure for liquidating the fund was subsequently initiated (Bannier, Fecht, Tyrell, 2007). The crisis warned of liquidity risks of open type real estate funds. It is emphasized in the paper because it points to important investment characteristics of regulated models which are defined by the way of fund collection and investment shares price formation. The organizational form is defined by the possibilities of emitting investment shares and it defines the investment profile of funds with regard to the following: liquidity of shares; correlation of price and net asset value; and flexibility of investment strategies. Open model is a highly liquid investment vehicle with limited capabilities for realizing countercyclical strategies (due to the necessity of high shares of liquid assets in the portfolio). It was originally designed to reliably reflect the value of fundamental assets, but targeted advantages may easily become a threat for the entire industry in periods of investors' distrust in the investment unit price generated by the valuation procedure. German open funds are important for analyzing the relationship of the quality of regulation and market acceptance of an investment vehicle since their development can also be followed through the phases defined by changes in regulatory framework[9]. Regardless of significant differences in structure of American REITs and German open real estate funds, their development stresses the key importance of regulatory characteristics for the market life of indirect investment vehicles.

Previous paragraph probably gives partial explanation of the fact why, besides in Germany, open real estate funds exist for a longer time only in Switzerland. Nowadays, 14 out of 27 member countries of the European Union have some form of a tax transparent collective scheme intended for investing into the real estate (Figure 1). Regulatory models introduced in last years are mainly structured according to the American model. This is often emphasized by the usage of the American acronym (REIT) in the title of domicile vehicle. This prevalent trend of legal transplantation is best illustrated by the term “REIT-like“, which is in the literature used for newly introduced formats.

[9] Detailed overview of regulatory evolution is found in Focke, 2006

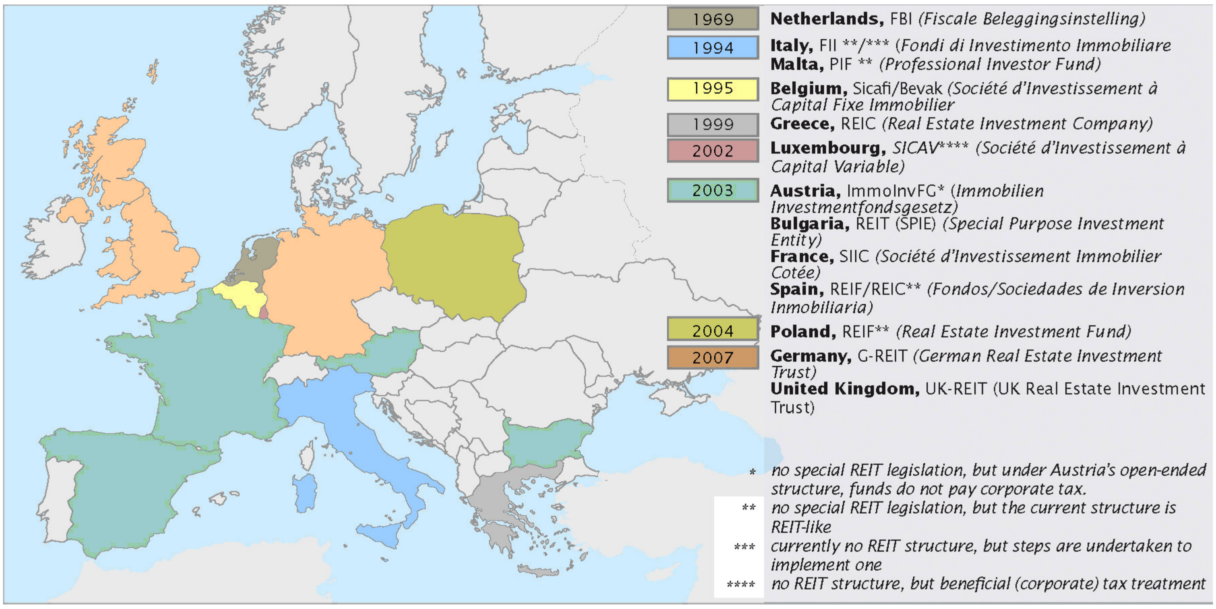

Figure 1: Tax transparent real estate funds in EU
Source: Eichholtz, Kook, 2008.

Of 13 member countries which have not introduced tax transparent structures, 9 are new member states. Of 14 members which do have such structures, 9 of them introduced transparent structures after year 2000. After 2007 REIT structures were introduced in Italy (SIIQ –Societa di Investimento Immobiliare Quotate), Spain (SOCIMI – Sociedad Cotizada de Inversion en el Mercado Inmobiliario) and Finland (REIT – Real Estate Investment Trust).
Adoption of new models in Italy and Spain points to the practice of frequent legislative changes in countries which already possess such structures (e.g. Netherlands introduced significant amendments in 2001, which were again changed in 2007). Large German and British financial markets introduced REIT structures after a number of unsuccessful attempts to introduce the original models and after the crisis of established regimens (German open funds). The arguments of German Financial Ministry stood in favor of the necessity of implementation of the REIT model due to preserving the competitiveness of German financial industry. It was also stated that REIT introduction would result in significant fiscal and economic benefits such as: more efficient use of assets tied in real estate and transfer of real estate management from proprietors to specialized subjects (Lachner and von Heppe, 2006). Introduction of REIT concept in Germany stresses the importance of international regulatory standardization in the function of harmonizing investment characteristics of collective schemes with investment demand for increasing foreign real estate investment. A discussion in the next chapter attempts to identify investment characteristics of real estate funds which are attractive in market sense and recognize regulatory provisions which influence their formation.

3 Legal Determinants of Real Estate Funds Development

Development of real estate funds on particular markets is not linked solely to the regulatory framework, but also depends on numerous factors such as: maturity and size of the capital market; size of commercial real estate market; investment costs; and return in relation to return of competitive investments (etc.) Development level of a financial system and commercial real estate market should be specifically emphasized because they influence investors' preferences and diversification potential through different real estate segments and geographic areas. Even though the volume of indirect investment into real estate is determined by various factors, the importance of specially designed collective investment schemes is confirmed by market evolution on most advanced financial markets. The example of Great Britain is indicative because its financial system and commercial real estate market are considered ones of the most advanced in the world. However, British authorized public funds have never become an accepted investment vehicle because of nontransparent fiscal regulation. The underdevelopment of public liquid investment vehicles and the fact that foreign funds (especially German open-end funds) are among the largest investors on British commercial real estate market are of key importance for introduction of REIT model into British market. Tax transparency is only one characteristic of models attractive in market sense, although the analysis of regulation in different countries leads to the conclusion that this advantage is often introduced while other important characteristics are neglected. The attractiveness of indirect real estate investment from an investor's perspective depends on the perception of the investment profile of the vehicle which is determined by a larger number of propositions. The analysis of long term successful models found out that investors prefer liquid tax transparent vehicles with stable long term returns. The remainder of this paper discusses legal determinants of the investment profile through organizational aspects; tax treatment; investment activity and managerial aspects; investors' protection; with a concluding comment on the heterogeneity of current European structures.

A) Organizational Aspects

Organizational form is defined by the mode of buying and selling investment shares. The shares of closed-end funds (US REITs) are traded on secondary market. The obligation of a quotation on an organized market is prescribed for public vehicles, while it is not mentioned for specially designed formats intended for qualified investors. Buying and selling of shares on capital market ties their value to overall market movements and influences the volatility of the capital component of return[10]. Public quotation offers easier access to capital but also has shortcomings since market does not always value of real estate companies in line with the value of fundamental assets. The sentiment of stock market defines the movement of price, so market price often exhibits a strong deviation in relation to the net asset value which is the reason for introducing propositions on the possibility of leaving stock-exchange quotation. The measure justifies itself on developed investment markets, while it can totally annihilate the liquidity of stocks on smaller markets. Volatility is mitigated by provisions which regulate obligatory diversification of the ownership structure (a minimum number of shareholders and maximum share of an individual shareholder in the ownership are specified) and with magnitude of portfolio investors' exposure to real estate funds. An open-ended model offers superior liquidity, but is not considered appropriate for the analysis due to non-market valuation of the asset value.

B) Tax Treatment

Tax exemption at entity level is the most important regulatory issue in the development of investment funds. Real estate funds are intended to be profiled by tax propositions as pass-through vehicles with passive investment strategies. The stability of a dividend component of return is determined by the obligation to distribute the largest part of the earnings to the investors (90% for US REIT funds). A model of avoiding double taxation by a deduction of the amount of paid out earnings from tax duty is called Distribution-Deduction Tax Prototype (Thuronyi, 1998). Passiveness of strategies is defined by a tax distinction of the investment activity (letting real estate) and other modes of generating return from real estate (trading, building). This approach is significant for real estate investment because rental yields are

[10] Investment in REITs is often called total return investment due to the stability of dividend yields and a moderate long term capital appreciation.

characterized by smaller volatility than yields from other activities which are considered highly risky on cyclical real estate markets. Earnings from investment activities are completely free from taxation, while earnings from other allowed activities is taxed at corporate tax rates. The need for a quality design of a tax treatment is evident in the treatment of different real estate activities because the approval of privileges discriminates real estate companies within corporate tax framework. The building of portfolio and generation of rental returns are encouraged to decrease the exposure of a banking sector to long term financing of commercial real estate and more efficient use of fundamental assets by users. A tax treatment encourages certain investment activities and removes the need for additional regulation.

C) Investment Activity and Managerial Aspects

Portfolios must consist mostly of real estate (percentage of minimum total real estate assets is prescribed) and a minimum percentage of income that must be derived from real estate is specified. Due to increasing investment flexibility and implementation of countercyclical strategies, the allocation minimum sometimes also includes highly liquid financial assets. Funds are usually allowed to allocate a smaller part of assets to other investment classes with a limitation of the share of assets in the portfolio of a particular issuer and the share of ownership at other issuers. Indirect investment into real estate companies is allowed and is considered investment into real estate, but diversification rules are applied in order to positively influence the risk. Limits on leverage are usually expressed as the size of debt vs. asset value. A lower ratio is deemed undesirable due to its negative influence on investment flexibility and it primarily points to the inconsistency in the regulatory model. The share of a particular real estate in the portfolio is defined (usually 20% of the net asset value), but it is important to emphasize that diversification potential is defined by the prescribed minimum size of the fund. The minimum asset value of the fund must be significant because of a high average value of a particular commercial real estate. Incorporation propositions must allow fund structuring by taking real estate into the portfolio in order to avoid “blind pooling“. All qualified investors must be allowed to establish funds without a mandatory authorization of a management company and with an opportunity of internal management.

D) Investor Protection

Investor protection is the basic motive of investment regulation. Thus, all aforementioned provisions could be understood in the light of increasing investors' safety. Overprotective regulation often has a counter effect because it makes instruments insufficiently attractive to target investor groups. With regard to specificity of real estate, we would herein like to mention certain regulatory provisions and practices which we deem especially important for investors' protection. The criterion of business transparency needs to be modified by introducing specific mandatory reports. The prospects of real estate funds must contain basic guidelines for the intended investment strategy (type of real estate, investment horizon, targeted return etc). It is also desirable to inform investors of any strategic changes appearing due to new circumstances. Lack of transparency in real estate markets makes it difficult to value fundamental assets and necessitates transparent valuation procedures. A quality regulation of assessment methods is necessary to enable investors to follow the movement of investment prices in relation to asset value and compare market performance with that of direct investment markets.

A comparison of REIT regulatory regimes in EU countries is a demanding task because of different legal traditions and plenitude of regulations which shape their investment characteristics. The most valuable attempt of comparing tax transparent real estate funds in EU countries was performed within the initiative for establishing a single pan-European REIT structure. For the needs of this initiative a study was conducted which shed light on the problems of current fragmented national models and looks for the optimal solution of a common structure (Eichholtz and Kook, 2007). The study contains a thorough comparative analysis of existing national models and we herein present some of its conclusions in a succinct form. Tax transparency is a principle honored in all regulatory frameworks, but the amount of mandatory distribution and distribution base are significantly different. The most common pay out is between 80% and 100% of earnings. While in some countries the prescribed percentage is lower (Greece, 35%), some countries do not prescribe the mandatory payout (Malta, Poland, Spain). Many regimes prescribe a minimum percentage of assets which must be invested into real estate and there are also frequent provisions on the types of real estate which may be invested into. Rules are often prescribed for the minimum or maximum allocation of assets into liquid financial instruments. Since a high level of debt is connected with high investors' risk, regulators mostly limit the level of allowed leverage. Leverage is limited to 10% of the asset value in Spain, while in Great Britain it is not limited at all. In other countries the range is between 40% and 60% of the asset value. Provisions stating the minimum number of investors and maximum percentage of ownership of a particular investor are frequent, but are also not present in all countries. .A comparison of European tax transparent structures shows the discrepancy of all models in relation to the American standard. The lack of key propositions and unnecessary limitations have also been obvious in recent regulatory attempts which point to the difficulties in transplanting legal constructs between different legal and market entities. Still, regional integration is proceeding in the direction of similar legal and regulatory frameworks and it removes the barrier for real estate cross border investments. Initiatives for harmonizing real estate funds have gained a stronger swing only in recent years. Although they are still quite away from a sound regulative framework it is reasonable to expect that a pan-European model will unlock presently closed door to the development of indirect real estate investments and integration of EU commercial real estate market.

4 Conclusion

A historical development of real estate funds on markets where regulated formats have been present for over 50 years shows the importance of certain regulatory provisions in the formation of investment profile of indirect instruments and their harmonization with the needs of investment community. Organizational formats which are attractive in market sense are characterized by tax transparency, liquidity and stability of returns. American REITs have all these characteristics which is the reason of their domestic success and increasing global popularity evident from the adoption of REIT model into investment legislations of numerous countries. REIT model combines flexibility of financial market instruments (shares) with stability of investment assets (real estate) in the form of a passive investment vehicle which is exempt from taxation after distribution of its earnings. Different REIT-like regimes which were introduced into EU member countries in previous decades have significantly contributed to further fragmentation of regional indirect real estate market. Such fragmentation inhibits competition of real estate companies and it had a particularly discriminating impact on the competitiveness of indirect markets (funds, companies) in relation to direct ones, which are not burdened with numerous regulatory restrictions. Development of a uniform institutional framework is of great importance for the development of private and institutional real estate investments within EU and for activity of real estate funds on the entire EU territory.

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