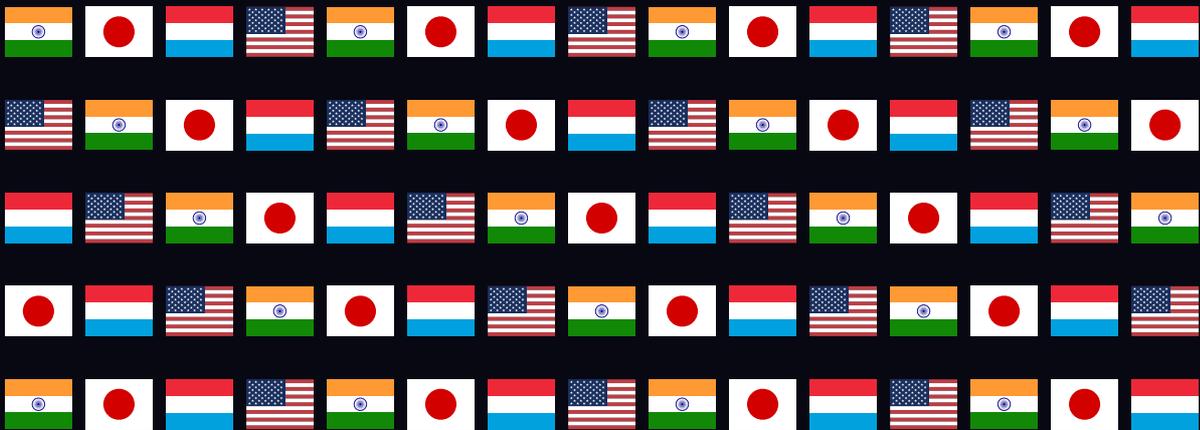


REAL ESTATE INVESTMENT TRUSTS

Japan



Real Estate Investment Trusts

Quick reference guide enabling side-by-side comparison of local insights, including into the definition, advantages and disadvantages of REITS, and market climate; organisational and governance considerations; key regulatory requirements, including for publicly traded REITS; categories of REIT and relevant property sectors; eligible investors; and recent trends.

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PRELIMINARY CONSIDERATIONS

Definition

What constitutes a real estate investment trust (REIT) in your jurisdiction?

A Japanese real estate investment trust (REIT) is a collective investment scheme utilising an investment corporation incorporated pursuant to the Investment Trust and Investment Corporation Act (ITA) as an investment conduit.

A REIT is a limited liability corporation that raises the necessary funds to purchase real estate and equivalent assets by issuing investment units to investors and by borrowing funds. A closed-end REIT is also permitted to issue bonds. A REIT may be listed or unlisted; an unlisted REIT is usually called a private REIT. The term 'J-REIT' often refers to a publicly-traded listed REIT. A listed J-REIT offers its investment units to a wide range of investors, including retail investors, through public offerings and by listing its units on a stock exchange. In contrast, a private REIT offers its investment units to a limited group of investors (typically institutional investors) by private placements of the investment units.

Under the ITA, REITs may have an open-end or a closed-end structure. In the case of a closed-end REIT, unitholders cannot require that their existing units be redeemed, except in the event of liquidation. In the case of an open-end REIT, unitholders are able to require that their existing investment units be redeemed at a then-fair price. While a listed J-REIT is required to be closed-end under the Tokyo Stock Exchange Securities Listing Regulations, a private REIT is usually structured as open-ended since its investment units are not listed; although the articles of incorporation of private REITs usually significantly restrict the timing and volume of permissible redemptions considering the illiquid nature of the underlying assets, namely real properties and their equivalents.

Pursuant to the ITA, an investment corporation is required to outsource substantially all of its operations to third parties, including the management of its assets. Compared to REITs in the United States or certain other foreign REITs, this external management structure is an important feature of REITs in Japan. The asset management company is usually a closely-held subsidiary or affiliate of the sponsor of the REIT.

Law stated - 10 November 2021

Pros and cons of REITs

Why were REITs created in your jurisdiction? What are the advantages and disadvantages of using REIT structures in your jurisdiction?

When the Japanese real estate market was in a slump, during the long deflation of the Japanese economy during the 1990s, the Japanese government decided to introduce measures to expand the liquidation and securitization of assets, including real estate, to stimulate the real estate market. In the course of this trend, in 2000, the ITA was amended to enable investment corporations to primarily invest in real estate and its equivalent assets, and, in 2001, the J-REIT market opened in the Tokyo Stock Exchange. In the same year, the first two J-REITs were listed on the Tokyo Stock Exchange.

The main advantages of using a REIT structure are tax advantages and a REIT is virtually the only structure available to form a listed real estate investment fund (although an investment trust can be listed as a real estate investment fund under the listing rules, only REITs (investment corporations) are currently listed in the REIT market).

Regarding tax advantages, unlike an ordinary corporation, distributions made by a REIT to its unitholders will be deductible from the taxable income of the REIT for Japanese corporate tax purposes (the 'tax conduit treatment'), subject to the satisfaction of certain requirements in relation to the REIT and the relevant fiscal period thereof. Furthermore, if a REIT satisfies certain conditions, the rate of real estate acquisition tax and registration tax thereby

payable are reduced to a certain extent.

In addition to the foregoing, REITs are created as a going concern vehicle with an indefinite term, whereby there is significantly less concern regarding exit strategies, compared with other types of real estate investment structures.

A disadvantage of using a REIT structure is the substantial costs and time required to form one, compared to other types of real estate investment structures, since a REIT must be managed by a registered asset management company and, in many cases, REIT sponsors have to establish and obtain a licence for an asset management company. It typically takes at least around a year until the listing of a J-REIT. Furthermore, generally speaking, REITs are highly regulated structures compared to other forms of private real estate fund structures and are required to comply with complex regulatory and tax rules.

Law stated - 10 November 2021

Market climate

How would you describe the state of the REIT market in your jurisdiction? How common are REITs in practice?

According to publicly available data, as of the end of August 2021, 62 J-REITs were listed, which had 4,393 properties in total, comprising around ¥20,969 billion in terms of total acquisition price. The total market capitalisation was around ¥17,582 billion as of that date. As of the end of June 2021, there were 38 private REITs under operation, which had 1,097 properties in total, comprising around ¥4,227 billion in terms of total acquisition price.

Due to the covid-19 pandemic, at the beginning of 2020, the J-REIT market plummeted temporarily; the total market capitalisation of listed J-REITs significantly reduced. However, around the middle of 2020, the market gradually turned around and has since recovered. The total market capitalisation of listed J-REITs and the Tokyo Stock Exchange REIT index (reflecting distribution) have already exceeded the pre-pandemic level.

However, there may be differences among the sectors. Logistics REITs are much more active than REITs in other sectors after the covid-19 pandemic started, while hotel REITs are in a severe condition.

It seems that there is a recent trend where private REITs are preferred to listed J-REITs. From 2017 to 2021, 10 J-REITs were listed while nearly 20 private REITs commenced operations.

There were also recent incidents of a hostile merger proposal and a hostile takeover attempt being made against listed J-REITs in 2019 and 2021, which were previously unseen in this market.

A REIT, whether listed or private, is a common structure used for real estate investment funds in Japan, in particular those formed as going concern funds. While recently a few going-concern type private real estate funds were formed using a limited partnership structure, REIT structures are still the only structure for listed real estate funds.

Law stated - 10 November 2021

ORGANISATION

Choice of entity and organisational requirements

What forms of entity are used for REITs and what basic organisational requirements apply?

The form of entity used for REITs is an investment corporation incorporated pursuant to the Investment Trust and Investment Corporation Act (ITA). Theoretically, it would be possible to use an investment trust structure under the ITA, but all REITs in Japan have been established in the form of an investment corporation thus far.

An investment corporation is a limited liability corporation. Pursuant to the ITA, an investment corporation is not

permitted to have any employees and is required to outsource substantially all of its operations to third parties, including its investment activities, the management and custody of its assets, and certain administrative functions. Investment activities are delegated to an asset management company, which must be a registered financial instruments business operator that is permitted to engage in an asset management business under the Financial Instruments and Exchange Act (FIEA) and satisfies certain additional requirements.

Each investment corporation has three organs, namely the unitholders' meeting, a board of directors composed of executive directors and supervisory directors, and an accounting auditor. The governance structure is similar to an ordinary joint-stock corporation, but in some respects, it is simplified considering its nature as a collective investment scheme. It also has a simplified equity structure (no classes of equity or issuance of warrants except for a rights offering, etc).

The unitholders' meeting may resolve only the matters provided for in the ITA and the matters authorised in its articles of incorporation. Typical matters taken up in a REIT unitholders' meetings are, among other things, the election of directors, amendments of the articles of incorporation, and approvals of a merger agreement. The appointment and removal of an asset management company are also subject to approval of the unitholders' meeting (except for the appointment of the initial asset management company). There is a deemed consent scheme, which permits REITs to stipulate that unitholders are deemed to give consent to matters in the agenda if they do not exercise their voting rights and no conflicting proposal has been submitted.

In terms of corporate governance, REITs are required to have at least one executive director and at least one more supervisory director than the number of executive directors to constitute the board of directors. The executive director represents the investment corporation and executes its operations and administers its affairs. The supervisory directors have a statutory duty to supervise the execution of the duties of the executive director. The ITA has detailed restrictions on who can serve as a supervisory director, particularly from the viewpoint of ensuring their independence from the asset management company and sponsor. The board of directors also supervises the execution of the duties of the executive director and, under the ITA, the executive director is required to obtain the prior approval of the board of directors in order to undertake certain important operations.

Under the ITA, an investment corporation must appoint an accounting auditor, which must be a certified public accountant or a public audit firm, by resolution at a unitholder's meeting.

Law stated - 10 November 2021

Partnerships as subsidiaries

Are REITs permitted to have partnerships as subsidiaries in your jurisdiction?

Under the ITA, a REIT in the form of an investment corporation is prohibited from having more than 50 per cent of the voting rights in a corporation, except for special-purpose vehicles incorporated outside Japan for the purpose of owning real estate under certain additional conditions. In addition, under Japanese tax law, a REIT in the form of an investment corporation can enjoy tax conduit treatment, if the proportion of the REIT's investments (including silent partnership investments) or shares in a corporation are less than 50 per cent of the total investments or shares in that corporation. Equivalent exceptions for overseas special purpose vehicles exist in the tax rules as well. These regulations were made to prevent a REIT from controlling another corporation.

It is not necessarily clear whether the above rules apply to partnerships because a partnership is not clearly regulated under the above rules, unlike a silent partnership.

Law stated - 10 November 2021

REITs as subsidiaries

Are partnerships permitted to have REITs as subsidiaries in your jurisdiction?

Under Japanese tax law, for a REIT to enjoy tax conduit treatment, the largest unitholder of the REIT and any group of persons having certain special relationships with the largest unitholder (including holding more than 50 per cent of the investments or shares in a corporation) should not collectively hold more than 50 per cent of the outstanding units or voting rights of the REIT at the end of the relevant fiscal period.

To have a REIT as a subsidiary, a partnership would have to hold more than 50 per cent of the units and the voting rights of the REIT, which would result in the REIT losing the tax benefit mentioned above. As losing the tax benefit has a material adverse effect on the REIT's operation, it is not practical for a partnership to have a REIT as a subsidiary. However, a parent-subsidiary relationship may be recognized, even under the situation where the holding ratio is 50 per cent or less pursuant to applicable generally accepted accounting principles, and thus theoretically a partnership may be able to have a REIT as a subsidiary while keeping its tax conduit status.

Law stated - 10 November 2021

Governance

What governance issues should the boards of REITs in your jurisdiction be aware of? How are these issues navigated in practice?

The most important issue could be the conflict of interest between the REIT and the sponsor, which is typically the major shareholder of the asset management company.

The sponsor of a REIT could materially influence the decision-making of the asset management company of the REIT and the REIT itself because the asset management company which manages the assets of the REIT is usually a subsidiary or related company of the sponsor. Close relationships among the asset management company, the REIT, and the sponsor could lead to acts that potentially give rise to conflicts of interest.

There are laws and listing rules tackling conflicts of interest. Among other things, these laws and rules require the prior approval of the board of the REIT, which is controlled by independent supervisory directors, to enter into certain material transactions with the parent company and certain other affiliates of the asset management company.

Given the importance of preventing conflicts of interest with a sponsor and other interested parties, a REIT and its asset management company usually establish voluntary conflict of interest rules in addition to what is provided under laws and regulations. In this regard, the voluntary rules of the asset management company often require prior approval from the REIT's board for the acquisition, disposition or leasing transactions or any other activity involving an interested party. The definition of 'interested party' in these voluntary rules is usually broader than the legal definition.

In addition, a REIT's board should carefully monitor the activities of the asset management company, including its compliance with laws, regulations and internal rules relating to, among others, transactions between the REIT and the affiliates of the asset management company. For example, an asset management company usually establishes a special decision-making process that is more stringent than required under applicable laws and regulations, with an investment management committee and a compliance committee (each of which usually has an independent member), with respect to the transactions between the REIT and interested parties. In addition, the internal rules of the asset management company usually set forth that, in principle, if the REIT is acquiring assets from an interested party, the acquisition price should not exceed the appraised value thereof; as for a sale of assets to an interested party, in principle, the assets should not be sold for less than the appraised value thereof. Other types of transactions with an interested party, such as leases and property management, should be done on arm's-length terms.

Recently, a hostile unitholder proposal for a merger and a hostile takeover bid were made against J-REITs. In this regard, boards' responses and decisions have become focused on protecting unitholder value. Since these cases, the discussion over the corporate governance of REITs has become active. Among the key topics are deemed consent schemes in unitholders' meetings and consolidation of units of REITs for squeezing out.

Law stated - 10 November 2021

KEY REGULATORY REQUIREMENTS

Sources of income

What are the basic source-of-income requirements for a REIT?

Under Japanese law, there is no clear provision regulating the basic source of income of a REIT.

However, under the Investment Trust and Investment Corporation Act (ITA), a REIT as an investment corporation is prohibited from doing any acts other than 'managing assets' as a business. Based on the rule, it is generally considered that a REIT's source of income should be substantially limited to rent from leasing real estate to a third party and should not be from the operation of a business, such as a hotel or retail activity; however, the limits are not clear.

For the avoidance of doubt, a REIT may invest in operational assets, including hotels, healthcare facilities or retail properties, if the REIT leases those properties to a third party that operates the properties and, therefore, the REIT's source of income is rent.

In addition, a REIT may invest in real estate in the form of securities issued by a real estate holding vehicle, including trust beneficial interests, shares, equity interests, and investment interests (including silent partnership investments), so long as the underlying real estate assets are leased to a third party and the real estate holding vehicle earns rental income. However, investments in REIT shares, equity interests and investment interests (including silent partnership investments) in a corporation must be limited to a minority stake for the REIT to qualify as a tax conduit under Japanese tax law (ie, a REIT cannot hold 50 per cent or more of the shares, equity interests, and investment interests (including silent partnership investments)).

Law stated - 10 November 2021

Asset composition

What are the basic asset composition requirements for a REIT?

The following are the four basic asset composition requirements for a REIT.

First, a REIT is defined under the ITA as a corporation incorporated based on the ITA for the purpose of investing mainly in 'specified assets'. The ITA limits specified assets to the following:

- securities;
- rights pertaining to derivatives transactions;
- real property;
- rights to lease real property;
- superficies rights;
- promissory notes;
- monetary claims;
- equity in investments in silent partnerships;
- renewable energy power generation facilities; and
- rights to operate public and other such facilities (PFI interests).

Second, for the conduit requirement from a tax perspective, the book value of the specified assets as described above must exceed half of the total amount of assets at the end of the relevant fiscal period. (Renewable energy generation facilities and PFI interests are included in the specified assets under the ITA, but these are not eligible for this tax rule purpose, except where the renewable energy generation facilities satisfy certain requirements. These rules are usually irrelevant for REITs, since REITs usually do not invest in these kinds of assets.)

Third, under Investment Trust Association regulations, a REIT's articles of association must stipulate that it aims to manage more than 50 per cent of its assets as investments in real estate or securities backed primarily by real estate.

Fourth, as for listed J-REITs, under the listing screening and de-listing standards, real estate, rights to lease real property, superficies rights, servitude rights, trust beneficiary interest thereof and the like (real estate, etc.) must comprise at least 70 per cent of the total assets under management and the ratio of all real estate, etc., real estate-related assets and liquid assets will be expected to be 95 per cent or more of the total assets under management.

Law stated - 10 November 2021

Distributions

What are the basic distribution requirements for a REIT?

A REIT must prepare statements on the distribution of monies for each fiscal period in accordance with the distribution policy in its articles of incorporation. They may distribute monies based on statements approved by the board of directors for their unitholders in accordance with the number of investment units held by each unitholder.

Unlike a stock corporation, a REIT may not distribute any property other than cash to their unitholders. In addition, as statements on the distribution of monies are prepared every fiscal period and a REIT cannot make any interim distributions, REITs customarily set their fiscal period to every six months in order to compete with ordinary stock corporations which typically distribute interim dividends.

With respect to the conduit requirement from a tax perspective, more than 90 per cent of the profits payable as dividends for the relevant fiscal period must be distributed to unitholders. In addition, if a J-REIT fails to make distributions for a certain fiscal period and monies are not distributed within one year thereafter, the J-REIT could be delisted under the Tokyo Stock Exchange de-listing standards.

A REIT may distribute monies to their unitholders in excess of their profits based on the statement on the distribution of monies, provided that these monies do not exceed the difference of the net assets stated on the balance sheet, less the net asset threshold. As the net asset threshold is generally ¥100 million, this restriction is not usually a material impediment to the distribution.

Distribution in excess of profits is also subject to the Investment Trust Association regulations. Under these regulations, a closed-end REIT may return capital up to 60 per cent of the difference of the amount of its accumulated depreciation as of the end of the relevant fiscal period, less the amount of its accumulated depreciation recorded as of the end of the preceding fiscal period.

Law stated - 10 November 2021

Consequences of non-compliance

What happens if a REIT fails to meet the basic regulatory requirements? Is relief available if a company fails to meet any of these requirements?

A REIT is required to be registered with the director of the relevant local finance bureau before starting any asset investment.

If there are sufficient grounds, such as where an executive or supervisory director is disqualified or the minimum net asset threshold is not met, the registration of a REIT may be revoked.

If necessary to protect unitholders and ensure the sound and appropriate management of a REIT's operations, the Securities Exchange Surveillance Commission may order a REIT to change its method of business or its asset management company or take other measures to improve its business operations to the extent necessary. Also, if a REIT does not meet the minimum net asset threshold, the director of the relevant local finance will notify the REIT that its registration will be revoked if it does not meet that threshold within a certain period of time.

A similar regulatory framework exists for the asset management company, which is also a regulated entity.

Law stated - 10 November 2021

Compliance best practices

What best practices should be considered to ensure compliance with the key regulatory requirements for REITs in your jurisdiction?

The asset management company plays an important role in ensuring compliance with the key regulatory requirements for REITs.

The asset management company must be an investment management business operator under the Financial Instruments and Exchange Act (FIEA). One of the requirements for investment management business operators is to have the necessary staff to appropriately conduct investment management. In addition, investment management business operators must have a system in place for appropriately performing financial instruments business activities.

To establish such a system, in addition to the legal requirement of having an investment manager and compliance officer with certain specialised knowledge and experience, asset management companies are encouraged to enhance staff training, regularly hold study sessions on compliance issues, or address those issues with external legal counsel on a daily basis.

Law stated - 10 November 2021

Public REITs – regulatory treatment

Are the requirements for a publicly traded REIT raising capital different from those imposed on private REITs or public non-REIT companies?

Publicly traded REITs (J-REITs) are different from private REITs as they are subject to the information disclosure regulations of the FIEA for publicly-offered securities upon commencement of any public offerings for raising capital. The regulations for disclosure upon issuance seek to provide the necessary information for making investment decisions upon the initial offering or sale of investment securities or corporate bonds. The disclosure mechanisms include securities registration statements, shelf registration statements and the issuance of a prospectus, and subsequent filing of an annual securities report for each fiscal period and other reports.

In addition, J-REITs apply to be listed on the Tokyo Stock Exchange when they execute an IPO. The exchange examines whether the REIT satisfies the listing rules. After listing, J-REITs must comply with the timely disclosure standards of the listing rules. The main information for timely disclosure relates to:

- decisions of the REIT;

- occurrences of certain events affecting the REIT;
- decisions of the asset management company;
- occurrences of certain events affecting the asset management company;
- assets under management of the REIT; and
- the financial statements of the REIT.

J-REITs are established under the ITA and cannot engage in any business other than 'managing assets'. Given a J-REIT's character as a collective investment scheme, its unitholders are not expected to be actively involved in its management; thus, a deemed consent scheme is permitted under the ITA (ie, REITs can stipulate in their articles of incorporation that unitholders are deemed to give consent to matters in the agenda of a unitholders' meeting if they do not exercise their voting rights and no conflicting proposal is submitted). Also, due to the characteristics of a J-REIT as an investment vehicle, J-REITs can enjoy tax conduit treatment under Japanese tax law.

On the other hand, public non-REIT companies established under the Companies Act can basically engage in any business set forth in their articles of incorporation. Unlike J-REITs, they are not entitled to enjoy tax conduit treatment or to adopt a deemed consent scheme for shareholder voting rights.

Law stated - 10 November 2021

Public REITs – ongoing requirements

What are the ongoing securities and disclosure requirements for publicly traded REITs?

The ITA establishes regulations for the disclosure of information by REITs to investors, which are equally applicable to J-REITs and private REITs. Specifically, these are the preparation and issuance of asset management reports to unitholders and the provision of financial statements after the end of each fiscal period.

Publicly traded REITs (J-REITs) are also subject to the ongoing disclosure requirements under the FIEA. FIEA requires the filing of an annual securities report for each fiscal period, semi-annual securities reports if the fiscal term is one year, and extraordinary reports if certain material events have occurred. As REITs customarily set their fiscal period every six months, they are not required to file semi-annual securities reports. Also, under the FIEA, if any party acquires more than 5 per cent of the units in a REIT, is, in principle, obliged to submit a large-volume holdings report to the Financial Service Agency (FSA). When a J-REIT offers new units, it must file a securities registration statement and deliver a statutory prospectus (that is virtually identical to a registration statement) to investors.

In addition, J-REITs are subject to the ongoing regulations of the Tokyo Stock Exchange, which are primarily comprised of de-listing regulations and timely disclosure standards. Also, the Tokyo Stock Exchange requires J-REITs to submit reports on the management structures of REIT securities issuers, etc. for each fiscal period. These reports describe:

1. the personnel of, and physical and capital relationships between, the REIT, its asset management company and its sponsors;
2. the policy for handling conflict-of-interest transactions that are based on item (1);
3. the management structure; and
4. specific transaction details with parties with special interest relationships, such as interested parties.

Law stated - 10 November 2021

Public REITs – listing rules

Do the stock exchanges in your jurisdiction have any special rules that do not apply to unlisted or private REITs?

The Tokyo Stock Exchange has listing and de-listing regulations and timely disclosure standards for the REIT market in the listing rules, which are applicable only to J-REITs. The main items of listing screening and de-listing standards are:

- asset composition requirements (real estate, etc must comprise at least 70 per cent of the total assets under management and the ratio of all real estate, etc, real estate-related assets and liquid assets is expected to be 95 per cent or more of the total assets under management);
- eligibility of the asset management company (asset management companies must be members of the Investment Trust Association);
- number of units listed (at least 4,000 units must be listed);
- refunds of investment units (a closed-end REIT's articles of incorporation may prohibit refunds upon unitholder request); and
- distribution (a J-REIT is subject to de-listing standards when a distribution of monies does not occur within one year after it fails to pay any dividend within a certain fiscal period).

Law stated - 10 November 2021

SCOPE OF ACTIVITIES AND INVESTMENTS

Categories of REIT and relevant property sectors

What kinds of REIT are available in your jurisdiction? In which real property sectors are REITs used?

The Investment Trust and Investment Corporation Act (ITA) establishes two distinct structures for REITs: investment trusts and investment corporations.

Investment trusts are sometimes called 'contract investment trusts', while investment corporations may also be referred to as 'corporate investment trusts'. These REIT structures may be created as either open-end or closed-end funds. Thus far, all REITs have been in the form of investment corporations. An open-end fund can redeem investments at the request of investors using assets in the fund. Investors in a closed-end fund cannot make such requests.

The Tokyo Stock Exchange's rules require funds to be closed-end, so all the listed J-REITs are closed-end. On the other hand, private REITs usually use the open-end investment corporation structure.

An investment corporation is defined under the ITA as an association incorporated based on the law for the purpose of investing mainly in specified assets. REITs currently in operation hold various types of real properties, such as office, residential, retail, logistical and hotel properties. Although REITs may invest in healthcare assets, the Ministry of Land, Infrastructure, Transport and Tourism (MLIT) set special guidelines in 2014 for investment in healthcare assets by REITs since they must consider the characteristics of the operational assets and the users of the healthcare assets. In addition, the ministry has also set guidelines for investment in hospitals by REITs. In addition, there are some special rules for the REIT which invests real property outside Japan under the listing rules of the Tokyo Stock Exchange.

Law stated - 10 November 2021

Special rules

Are there any special rules for different types of REIT?

First, the rules for private REITs, the units of which are not listed, are different from the rules for listed REITs (eg, tax requirement as an investment conduit and disclosure rule in the FIEA).

As for asset types, whether the REIT is listed or not, there are various types of REITs, including REITs focusing on a specific type of asset (office, residential, retail, logistics, hotel properties etc) and REITs that do not focus on a specific type of asset. As for geographic types, some REITs make it their policy to only invest in property in specific areas, some invest in property all around Japan, while a few invest in overseas assets. The application of fundamental rules (ie, ITA and the listing rules of the Tokyo Stock Exchange) do not depend on the type of REIT.

However, there is a special guideline from the MLIT for asset management companies managing a REIT investing in hospitals, which requires the asset management company to establish a good working relationship with the staff at the hospitals under management. There is also a special guideline from the MLIT for an asset management company to manage a REIT investing in healthcare properties (eg, residential properties with services for elderly people). In addition, there are some special rules for REITs investing in real property outside Japan under the listing rules of the Tokyo Stock Exchange.

Law stated - 10 November 2021

Eligible investment property

What assets are treated as qualifying real property under the REIT rules in your jurisdiction? Can REITs located within your jurisdiction invest in real property outside your jurisdiction?

Under the ITA, there is no requirement to be treated as qualifying real property. All real property under the Civil Code in Japan is treated as qualifying real property for REITs. REITs can invest in real property outside Japan as well.

Under the ITA, there is a special exception for REITs to hold voting rights in certain special purpose vehicles when it is necessary to invest in real property outside Japan; otherwise, in principle, REITs are prohibited from holding more than 50 per cent of the voting rights of another entity. The Tokyo Stock Exchange requires REITs to disclose policies and risks for investing in real property outside Japan if it is a REIT's policy to make such investments. Asset management companies of REITs should appropriately manage real property outside Japan, with adequate personnel and procedures for investment and management of real property outside Japan.

Law stated - 10 November 2021

Permitted activities

Are REITs in your jurisdiction allowed to engage in any ancillary non-investment activities, such as real property management and development?

The ITA prescribes what activities can be undertaken by investment corporations. Acquisition and disposition of securities and real properties are included. On the other hand, under the ITA, an investment corporation cannot develop land or construct a building by itself; produce, manufacture, or process commodities; or manufacture or install renewable energy power generation facilities.

Although a REIT cannot develop land or construct a building by itself, a guideline of the Financial Service Agency (FSA) states that REITs can order a third party to develop land, or construct or extend a building, unless such an order

materially affects the entire portfolio of the REIT, taking into account that the property cannot be used by existing tenants during the construction period and various risks relating to the development and construction of real property.

As for real property management, in most cases, REITs engage a property management company for a fee. A REIT cannot engage in real property management by itself because it has no employees. In addition, the FIEA allows asset management companies to only engage in specific activities as a licenced company. However, asset management companies can engage in property management activities, subject to a filing with the FSA; some asset management companies do engage in property management for REITs.

Law stated - 10 November 2021

Eligible investors

Who may invest in REITs in your jurisdiction? What types of investor do they typically attract? Are there any restrictions on foreign investors?

Anyone may invest in listed REITs. Financial Institutions (eg, banks and insurance companies) are the main investors in listed REITs, but individuals also can invest in listed REITs. Foreigners can also invest in listed REITs. Among financial institutions, trust banks hold a significant portion of listed REIT units on behalf of investment trusts investing in listed REITs and other types of institutional investors.

Generally speaking, the income of a REIT is more predictable and stable than that of other companies, because most of the revenue received and most of the costs to be paid by the REIT are determined in advance under agreements (eg, lease agreements, property management agreements). Therefore, it is generally believed that REITs attract investors who wish to earn a stable profit. According to the Tokyo Stock Exchange's survey in February 2021, 51.8 per cent of the units of listed REITs are held by financial institutions, 26.8 per cent by foreigners, and 10.6 per cent by individuals.

In general, under the Foreign Exchange and Foreign Trade Act, the acquisition of units of a REIT listed on the Tokyo Stock Exchange by a non-resident of Japan from a resident of Japan may be made without any restriction. Dividends and capital gains from REIT units are subject to taxation, depending on the taxpayer type of the investors. Taxation would also depend on factors such as whether the REIT is listed or not.

On the other hand, private REITs are usually offered and held only by certain types of institutional investors, due to securities regulation and tax consideration. Subsequent transfer restrictions are also usually imposed on units of private REITs.

Law stated - 10 November 2021

Transactions with non-REITs

Are there any special considerations when REITs negotiate purchases and sales or leases of investment real estate with non-REITs?

REITs and asset management companies must be prudent when negotiating purchases and sales or leases of real estate on behalf of unitholders. Among others, they should be careful when the counterparty in the negotiation is an interested party (eg, a parent company of the asset management company). For example, under the ITA, the approval of the board of the investment corporation is required for certain transactions between the investment corporation and an interested party of the asset management company. Asset management companies usually have internal rules for transactions between the REIT and interested parties.

There are no special regulations for transactions between REITs, unless they are managed by the same asset management company.

Acquiring non-REIT corporations**Are there any special considerations when REITs acquire non-REIT corporations?**

A REIT, which is an investment corporation investing mainly in real property, is established under the ITA, not the Companies Act of Japan ; as such, a REIT cannot merge with a joint-stock corporation established under the Companies Act. An investment corporation can only merge with another investment corporation. Other corporate procedures, such as company splits and share exchanges, cannot be used by REITs under the ITA.

REITs can acquire the equity of other entities, such as stocks of a joint stock company, because they are specific assets under the ITA. However, the ITA prohibits REITs from holding more than 50 per cent of the voting rights of other companies unless the exception for investment in real property outside Japan is applicable. Similar rules exist in the tax rules as well. In addition, the listing rules of the Tokyo Stock Exchange require listing REITs to invest a certain percentage of their assets in real property etc, so there is a limitation on the amount of equity in a REIT's portfolio.

Law stated - 10 November 2021

UPDATE AND TRENDS**Recent developments**

What have been the most noteworthy recent developments affecting REITs in your jurisdiction, including any significant legal or regulatory changes and commercial trends?

Recently, some REITs experienced hostile unitholder proposals or hostile takeover attempts.

In 2019, Star Asia proposed a merger with Star Asia Investment Corporation to Sakura Sogo REIT Corporation (Sakura Sogo) without the prior consent of Sakura Sogo. In connection with the offer, the executive director and asset management company of Sakura Sogo would be changed. The proposal was approved at the unitholders' meeting of Sakura Sogo, and it merged with Star Asia in 2020.

In 2021, Starwood commenced a tender offer for the units of Invesco Office REIT, Inc. (IOJ) without the prior consent of IOJ. Starwood announced that a consolidation of units of IOJ to squeeze out the remaining unitholders will be carried out after the investor purchases a certain amount of units. The tender offer of Starwood failed, but Invesco, the sponsor group of IOJ, made a counter tender offer as a white knight, which succeeded. Consequently, IOJ was delisted in November 2021.

Since these cases, the discussion over the corporate governance of REITs has been active. Among them, deemed consent scheme in the unitholders' general meeting and consolidation of REIT units to squeeze out unitholders are hot topics.

In addition, the ongoing covid-19 situation has affected REITs in Japan. In March 2019, the REIT market went down, and the total market capitalisation of listed REITs was significantly reduced, although it has gradually recovered. The impact of the pandemic would be high if the REIT's business depends on tenants' revenues (ie, the rent payable to the REIT is proportional to the revenue of tenants on the property).

Law stated - 10 November 2021

Jurisdictions

 India	AZB & Partners
 Japan	Mori Hamada & Matsumoto
 Luxembourg	Loyens & Loeff
 USA	Sullivan & Worcester LLP