STANLIB Multi-Manager

The Educator

Introduction to and tax treatment of REITS

In The Educator, we address a number of topics with the ultimate goal of providing a better understanding of investing clients' money.

Listed property sector – introduction of REITS in South Africa

"A regular company makes profit and pays taxes on its entire profit. There-after, the decision is made as to how to allocate after-tax profits between dividends and reinvestment. A REIT simply distributes all of its profits and gets to skip the taxation"

Little is known to investors about the Real Estate Investment Trust (REIT) regime (pronounced "reet") that came into effect in South Africa on 1 May 2013. The new regime has however, brought SA in line with international best practise.

In this issue of Educator we briefly discuss the rationale for the REIT structure and how the new legislation impacts you as a shareholder in listed property stocks and/or as an investor in a property Collective Investment Scheme (CIS).

Allow both PLSs and PUTs to convert to a REIT

Prior to SA REIT legislation, there were historically two forms of listed property investment entities, namely Property Loan Stock (PLS) and Property Unit Trusts (PUTs). The complexity around PLSs and PUTs was difficult for investors to understand and caused confusion as to how income distribution was taxed.

The new regulations are aimed to incorporate listed property stocks (PLS and PUTs) under a single umbrella, namely REIT and thus provide clarity on how these entities will operate under the new regulatory framework and manner in which investors will be taxed.

	PLS	PUT	New REIT
Capital Gains Tax – sale of assets	✓	x provided profits are distributed to shareholders	x
Permitted to invest in other listed companies	✓	x	✓
Gearing limits	Limited to amount stated in company's articles	60% - subject to unit holder approval	Below 60% of its gross asset value
Legal form	Companies Act	Collective Investment Scheme Act	Company REIT and Trust REIT
Management company/ administration	External or internal	External	External or internal

Taxation – how it impacts you as a natural person

SA REITs provide a simple and clear tax structure.

Income tax - distributions

	Distribution	PUT
New REIT	"Income distribution"	• At least 75% of the net income (pre-tax profits) will be distributed • Income is then taxed in the investor's hand (gross income) • No interest exemption on income – taxed from the first cent • Taxed at investor's applicable marginal* income tax rate

*Take note: Where the recipient is a non-resident investor, the dividend will remain exempt from income tax. Effective 1 January 2014, a 15% withholding tax is imposed on their distributions or the double tax agreement rate where applicable.

Security Transfer Tax (STC)

Shareholders are exempt from STC when buying or selling REIT shares.

Capital Gains Tax

Shareholders/unit holders will continue to be exempt from Capital Gains Tax (CGT) until such time as they sell out of their REIT investment/CIS.

Summary

- Converting PLSs and PUTs to REITs allows for better uniformity, transparency, tax dispensation and investor protection
- REITs are globally recognised and in line with international standards
- Under the REIT regime, the South African listed property market is positioned to benefit from increased interest from foreign investments on the back of more transparent and now single-tax rules
- Investors can be certain that 75% of the net income will be distributed – flow through of net property income
- Income distribution is taxed at the investor's marginal tax rate

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