

# REITS Association of Kenya (RAK)

## **REITS** ASSOCIATION OF KENYA Quarterly Newsletter

4th Edition | **October 2019**



## Message from **Chairman**

Welcome to the 4<sup>th</sup> edition of the RAK Newsletter, which aims to share information to apprise our stakeholders and members on developments within the Association and the industry.

As the organization working towards establishing an environment for investment into high quality real estate in Kenya, RAK is well positioned to engage with the government and various policy makers by lobbying to find solutions that support the progression and deepening of the industry. The Association recently lobbied the government for exemption of REIT investee companies, a move which further positions REITs as a viable and tax-efficient investable asset class. You will read more about this in an article inside that covers an update on the Finance Bill 2019.

In May, we hosted a breakfast forum themed 'Practically Growing Real Estate Investments in Kenya'. The forum served as a platform for the Association to bring like minded industry stakeholders to articulate the journey to listing a REIT and having discussions around pertinent issues on the steps to starting a REIT in this market. This is in line with RAK's task of introducing discussion forums to analyze applicable laws and legislation, trends and current issues and improve professionalism and knowledge within the real estate investment industry.

Additionally, we partnered with the NSE to conduct a comprehensive introduction training seminar on REITs on October 23<sup>rd</sup> 2019. This comes on the back of increased interest in the product among market stakeholders. More details regarding the training are inside the newsletter.

This edition also features an article from Triple OK Law Advocates, on the digitization of land records, which is critical to ensuring transparency and efficiency within the sector.

The 2nd REITs Conference scheduled for the first quarter of 2020, will aim to bring together developers and investors in order to highlight investable opportunities within both the real estate and capital markets. The conference will provide a highly interactive platform through plenary, breakout, deal making and networking sessions. We look forward to hosting you.

RAK continues to remain committed to growing the REITs sector in Kenya. We sincerely thank our members and stakeholders for the support offered so far.

*Mr. Edward Kirathe*  
**CHAIRMAN**

## What's Inside:

*The Regulations Issue*

**Message from the RAK  
Chairman**

**1<sup>st</sup> RAK Annual General  
Meeting (AGM)**

**RAK Stakeholders  
Breakfast Forum**

***Contributing Authors***

**Finance Bill 2019 will be a  
Huge Win for Kenyan  
REITs – Nozipho  
Makhoba**

**The Legal Framework  
Governing REITs in  
Kenya – University of  
Nairobi**

**Digitization of Land  
Records – Triple OK Law  
Advocates**

***Events***

**REITs Training – Pride  
Inn Hotel, Lantana,  
23<sup>rd</sup> October 2019**

**2<sup>nd</sup> REITs Conference**



# 1<sup>st</sup> RAK Annual General Meeting (AGM)

The REITs Association of Kenya (RAK) held its first Annual General Meeting (AGM) on 31<sup>st</sup> July 2019 at the Nairobi Securities Exchange (NSE) under the Chairmanship of Mr. Edward Kirathe. All resolutions submitted to the vote were adopted by the members.

The general meeting approved, among other resolutions the Association's audited accounts for the 14 months period ended 31 December. The general meeting also elected the officials, who had been since inception of the Association serving in an interim capacity. Following the meeting, the Main Committee is still comprised of 4 officials and 4 members, making the total members serving on the Main Committee 8.



## RAK Hosts a Stakeholders Breakfast Forum in Partnership with Kenya Property Developers Association (KPDA)

In line with RAK objective of promoting REITs as a viable investable asset class, RAK hosted a breakfast forum on Tuesday, 21<sup>st</sup> May 2019 at the Park Inn by Radisson Hotel, Westlands. The event was themed '*Practically Growing Real Estate Investments in Kenya*' and purposed to draw potential REIT issuers together to articulate the journey of listing a REIT and to encourage them to undertake an incubation process supported by RAK.

The key-note presentation was made by the RAK Chairman, Mr. Edward Kirathe. The presentation titled '*The Journey to listing a REIT*'; paved way for a panel discussion on topical areas of focus including; mechanics surrounding pension funds pooling together funds for a REIT; challenges to be overcome by the capital markets to get them comfortable with listing REITs; NSE's incubation programme and broad guidelines for admittance especially with regard to property funds.

The panel session drew expertise from a variety of industry experts to include Mr. Adil Suleiman, the Head of Actuarial Services at Zamara, Mr. Peter Waiyaki, Partner at Mboya, Wangong'u & Waiyaki Advocates, Mr. Ken Kaniu, Chief Executive Officer at Britam Asset Management, Mr. David Waggema, Head of Business Development at the Nairobi Securities Exchange (NSE) and Mr. Kenneth Mbae, Commercial Director at Centum Real Estate.

The event was well attended by over 100 market stakeholders comprising of Pension Funds, Institutional Developers, Development Finance Institutions, Fund Managers, Administrators, Trustees, Regulators, Associations, REITs, Commercial Banks, Property Services providers, Contractors, Architects, Lawyers and Financial and Tax Services Firms.





# Finance Bill 2019 will be a Huge Win for Kenyan REITS

*Nozipho Makhoba – Chief Executive Officer, STANLIB Fahari I-REIT*

In September 2019, Parliament approved the Finance Bill 2019 ending all speculation and anxiety since its publication as part of the Budget Speech for 2019/20 in June 2019. The Bill was however later rejected by the President of Kenya in October 2019 on grounds that the interest rate cap must be repealed. The much anticipated final approval of the Finance Bill 2019 will mark a significant milestone for real estate investment trusts (REITs) in Kenya as it ends a four year long period of uncertainty around the tax exemption status of REITs.

Up until this point, the Kenyan Income Tax Act had partially addressed the tax exemption of REITs. 'Partially' because section 20(1)(c) of the Income Tax Act provides that REITs are exempt from income tax but does not expressly provide for the exemption of REIT investee companies or subsidiaries from income tax. In a market where most property holdings are ring-fenced in special purpose vehicles (SPVs) or company structures, rather than in direct holdings, this gap in legislation simply rendered section 20(1)(c) ineffective in providing the intended income tax exemption.

The Finance Bill 2019 bridges this gap in legislation by proposing extending the exemption of REITs to cover the investee companies of REITs. It is understood that this will be achieved by way of a new section 20(1)(d) to provide for such exemption.

## Flow-through principle

As a general rule, globally, REITs are exempt from income tax as they are required to pass on to the investors a considerable portion of the distributable profits. REITs therefore provide a conduit for earnings to be **taxed at the investor level** and not at the fund level, similar to collective investment schemes. This is referred to as the 'flow-through' principle. Each country has its own specific REIT legislation that prescribes the rules for conduct of REITs. In Kenya, REITs have to comply with a number of regulatory requirements in order to maintain the tax exemption status. The requirements are contained in the Capital Markets (Real Estate Investment Trusts) (Collective Investment Schemes) Regulations, 2013 and include the following:

- ◆ An income REIT must distribute at least 80% of its distributable net earnings each year;
- ◆ An income REIT and development REIT must distribute any realised capital gains which have not been invested within a period of 2 years from the date of realisation to the unitholders within 2 months of the second year of such realisation;
- ◆ An income REIT's borrowings must not be in excess of 35% of total asset value;
- ◆ A development REIT's borrowings must not be in excess of 60% of total asset value.

Failure to comply with the above does not only result in the revocation of the REIT license but also in the REIT ceasing to be classified as a REIT for tax purpose thus causing the REIT to lose its tax exemption status.

## Significance of the tax exemption milestone

Kenya is the second country in Africa after South Africa to adopt REITs as a real estate investment vehicle. Globally, 38 countries have formally adopted REITs while a few others are still considering to including China, Poland, Ghana and Nigeria. The size of REITs has grown considerably over the years. The table below compares the size of REITs in various countries across the globe as at July 2019.

*Table 1<sup>1</sup>*

Country or Region	Market Capitalisation (USD bn)
USA	902.3
EUROPE	248.5
AUSTRALIA	82.8
UK	67.6
SOUTH AFRICA	30.3
KENYA	0.0*

**\*USD 0.015 bn**

Kenya still has only one listed and operational REIT – STANLIB Fahari I-REIT, which came into the market through an initial public offering (IPO) in November 2015. The fact that there are virtually no listed property funds in Kenya, let alone REITs (save for STANLIB Fahari I-REIT), explains why Kenya lags behind other countries in terms of the size of the listed property market. Countries that have adopted the REIT structure find it easier to attract foreign capital investment into REITs (though this depends on other fundamentals stacking up, eg. the performance of those REITs), the reason being that REITs are globally understood and are regulated, thus giving comfort to investors. The uncertainty around the tax exemption status of REIT investee companies in Kenya is known to have contributed to the delay in the establishment of more REITs in the Kenyan market. With that uncertainty finally being removed, it is anticipated that the number of REITs will increase.

<sup>1</sup> Source – STANLIB Anchor Stockbrokers, Various Indices July 2019



# Legal Framework Governing Real Estate Investment Trusts (REITS) In Kenya

*Paul M. Syagga, PhD, Department of Real Estate and Construction Management, University of Nairobi*

The real estate sector in Kenya is increasingly becoming one of the most attractive investment avenues in Kenya. This is courtesy of a bulging population coupled with increased urbanization and growing disposable income for many households. As a result, experts estimate that the industry will keep growing uninhibited in the foreseeable future.

The Kenya National Bureau of Statistics' (KNBS) annual Leading Economic Indicators released in August 2018 indicated that the real estate and the construction sector's contribution to GDP rose from 12.6% in 2010 to 13.8% in 2016. Real estate has consistently outperformed other asset classes in the last five years, generating returns of more than 25% per annum compared to an average of 10% in the traditional assets classes.



**University of Nairobi**

While investments in residential units targeting middle level and high-end markets have remained lucrative, with the government currently initiating various projects (Presidential Big Four Agenda Programme 2018) to realize affordable housing for Kenyans, the lower middle income segment of the residential market presents attractive opportunities for investors.

Equally, student housing in Kenya for university and post-secondary college students is now a powerful alternative asset which if appropriately promoted will definitely guarantee tenancing. Therefore, the development of student's accommodation may prove to be the next big thing in real estate.

## REIT as an Investment Vehicle in Real Estate

A Real Estate Investment Trust (REIT) is a regulated investment vehicle that facilitates collective investment in which third-party financing can be made available for the real estate sector.

REITs may operate in different ways. There are those that may acquire land, develop it and sell it at a profit (**D-REITs**), and those that may acquire already developed property or even develop the property for purposes of generating rental income (**I-REITs**). In the latter case, they will hold and manage the properties over a period of time. An **Islamic REIT** is a unique type of I-REIT that invests primarily in income-producing, Shari'ah - compliant real estate. A fund manager is required to conduct a compliance test before investing in real estate to ensure it is Shari'ah compliant and that non-permissible activities are not conducted in the estate and if so, then on a minimal basis.

In Kenya, REITs may be listed or unlisted. A listed REIT's units are traded on the Nairobi Securities Exchange like any other company share, offering investors a liquid stake in real estate. In practice, I-REITs are available for purchase to the general public, while the D-REITs are restricted to professional investors only.



In Kenya, REITs operate under the Capital Markets (Real Estate Investment Trusts) (Collective Investment Schemes) Regulations, 2013. They are structured as trusts rather than companies.

The Trustee acquires the property and holds it on behalf of the beneficiaries (individual and corporate investors). The Trustee is responsible for the appointment and supervision of the REIT Manager. It is also the Trustee's responsibility to ensure that the assets of the scheme are invested in accordance with the Trust Deed and the Offering Memorandum ensuring that distributions from the assets of the REIT are made in accordance to the Offering Memorandum as approved by the Capital Markets Authority (CMA). Therefore, the investment properties are held in the name of a corporate trustee who is the custodian of the REIT assets but managed by a corporate REIT manager. To act as REIT manager, you have to be licensed by the CMA.

Listed REITs units are traded on the Nairobi Securities Exchange (NSE) like any other company share, offering investors a liquid stake in real estate. Individuals and corporate investors may subscribe to a public offer in the NSE as was the case with of the first ever listing under the Regulations (2013) by STANLIB Fahari I-REIT in November 2015. The offer then required a minimum subscription of Kshs. 20,000 at 1,000 units and a nominal value of Kshs. 20.00 each.

The Regulations require REITs to distribute most of their net income to the unit holders. In Kenya, REITs are required to distribute at least 80% of distributable earnings to unit holders.

NSE listed REITs are held to the same standards and requirements of disclosure to investors on financial information and reports on material business developments and risks as other publicly traded companies. As such transparency in REITs operations provides a basis for investors to analyze and appraise REITs assets independently.

## Advantages of REITs

The launch of REITs in Kenya was to enhance financial inclusion in Kenyan capital markets, so that investors with less capital could invest in large-scale commercial, residential and industrial properties without requiring large sums of money. This should be a boon particularly for residential development that now has full Government support under the 2018 Big Four Agenda Programme. Unlike other sectors in real estate, demand for housing particularly for low and middle income wage earners remains insatiable.

Given the lower investment entry threshold, more investors entering the market would provide the much needed funds for real estate investment through REITs and as a result create a vibrant liquid market in otherwise immovable property. It accords the unit holder a hedge against inflation, as a result of ever increasing real estate rental incomes and capital appreciation even during inflationary trends. It also provides the investors with portfolio diversification since they have the advantage of investing in a variety of real estate from shopping malls, to office buildings, residential projects and industrial projects among others.

Registered REITs do not attract income tax, but must remit to the tax authorities the withholding tax on the dividends paid by the REIT. Instruments used in transfer of property to listed REITs are also exempt from stamp duty.

The current section 20 of the Act only exempts REITs from income tax without extending the exemption to subsidiaries and investee companies which are wholly-owned by REITs. Consequently, if a REIT invests in a company, the income of that company would be first subjected to corporation tax at the rate of 30 percent on the net profit before distribution to the REIT unit holders. Since the investee company is wholly owned by the REIT, as the law requires, the effect is to subject income due to a REIT to 30 percent corporation tax, hence negating the essence of the tax exemption to income of the REIT.

The Finance Bill 2019, however, provides that REIT wholly owned subsidiaries will also be exempt from income tax. REITs will therefore get income tax exemption extended to companies they use to hold their properties. The proposed amendments to Section 20 of Income Tax Act will ensure that the objectives of REITs are fully achieved as it exempts the income of investee companies fully controlled or owned by the REITs.



## Challenges in the use of REITs

REITs have opened the investment market in real estate to a larger population segment that would not have been the case previously, and is equally a tax efficient structure. If appropriately promoted, REITs have the potential to support the achievement of the provision of more housing under the Presidential Big Four Agenda Programme.

However, participants in REIT's investment should appreciate that REITs may grow at lower rates than normal companies due to the restriction to re-invest a maximum of 20% as the rest is distributed as dividends. While REITs are also eligible by law to borrow, debt financing could result in high interest rates depending on the current economic operating environment.

Investment in REITs is subject to real estate market cycles that may experience market volatility from time to time as a result of changes in the economy, government regulations or political activity.

## Digitization of Land Records

*Janet Othero (Senior Associate) and Cheptoo Langat (Pupil)*

**TRIPLEOKLAW**  
ADVOCATES



Previously, the Ministry of Lands has relied on a paper-based system to discharge its mandate. This system has proved untenable in this era of great technological advancement. The Ministry of Lands commenced a digitization exercise a couple of years ago which included scanning all lands office records. This is a project spearheaded by various ministries of the government to improve the efficiency of its services and operations by enhancing transparency in the system. As for digitization of the lands records, the main objective is to reduce the number of disputes pertaining to land and ease operations at the said office.

The digitization process has presented some discrepancies with existing law, that is the bulk of the content of a case lodged in court by the Law Society of Kenya. The suit seeks to quash a publication by the Ministry of Lands in the Daily Nation on the 4th April 2018, stating that land transactions will be processed online with effect from 13<sup>th</sup> April 2018. The orders sought in the suit amongst others, were to compel the Ministry of Lands to set up a consultative task force for the creation of electronic registration and conveyancing. This will be considered against the background of the proposed Land Registration (General) Regulations of November 2017 that were recently passed in Parliament. This article does not seek to analyze the merits and demerits of case.



## Challenges

The Land Act and Land Registration Act of 2012 were enacted with provisions requiring the National Land Commission and Ministry of Lands to come up with standardized conveyance forms and registration regimes. Parliament recently gazzetted the Land Registration (General) Regulations to give effect to electronic filing of registrable land documents. Of importance to note is that the regulations are subsidiary to the legislation in place and are mainly procedural. In its provisions relating to electronic registration and conveyancing, it does state that all dealings under the enabling Act shall be carried out in electronic form.

The Advocates Act at Section 34 stipulates that no unqualified person shall take instructions to draw or prepare any document or instrument relating to the conveyancing of property. The regulations appear to secure the role of advocates by providing standard forms that require attestation of advocates where required. The regulations do state that the electronic system will be configured paying regard to provisions of the Advocates Act on the qualifications of persons who may draw and engross conveyancing documents.

Currently, the Lands Information Management System (LIMS hereinafter) portal does not provide for an avenue for such inclusion of advocates to carry out transactions. It is configured in a way that any transactions have to be undertaken against a personal account of the parties to the transaction thereby removing advocates from the equation once documents are drafted. With the introduction of standard forms to the public, the role of advocates is further diminished from the process.

Moreover, the online portal contravenes Section 2 of the Stamp Duty Act as it purports to collect Stamp Duty whereas the Act states that it is the role of the Collector of Stamp Duty at the Kenya Revenue Authority (KRA hereinafter). The stamp duty is assessed under the LIMS portal and the stamp duty amounts are payable against a bank code or M-pesa paybill number issued under the same portal. These amounts are payable to a non-traditional KRA recipient account. It is also unclear how the payment of Stamp Duty and Capital Gains Tax will be done under the online system.

Further, there are valid concerns raised that there was no public participation in the digitization process. This is evidenced by the various gaps in the system, with no information available such as how to process documents under the Government Land Act (Repealed), new leases, sub-leases, extension of leases, change of user, letters of allotment and provisional certificate of titles. It also does not provide for simultaneous registration of documents such as discharge, transfer and charge. Further LIMS does not seem to consider the transfer and transmission of deceased person's property whose National ID cards and phone numbers have since been surrendered<sup>2</sup>.

There have been complaints that while digitization seeks to make the conveyancing process secure and efficient, the online system has failed to achieve this in its initial launch. For instance, in conducting a search manually, the process would take less than a week to complete. Under LIMS, the time taken has not been ascertained for reasons including not all the files were scanned and uploaded in the system. Further, official search results under the RTA system contained the entire history of the land, while the search results procured using LIMS do not contain the entire history.

One of the most overlooked issues arising is the security and privacy of the records and data. While with the manual system there was a degree of safety in that only authorized personnel could access the lands records, stakeholders are yet to be advised on the security features of LIMS from local and international hackers. The government has outsourced this service to a third party. There is no clarity regarding in which jurisdiction the data is housed and how the same can be accessed if the third party terminates its services with the government.



<sup>2</sup> The minimum requirement to open an account with the E-Citizen online platform where LIMS is hosted is a valid phone number and national identity card. A verification code is sent to the mobile phone number and only one phone number can be registered against a user or national identity card.





# REITS Training

**Past Event:** Nairobi Securities Exchange (NSE) in collaboration with REITs Association of Kenya (RAK) held a Real Estate Investment Trusts (REITs) training on Wednesday 23<sup>rd</sup> October 2019 at the Pride Inn Hotel Lantana. The training featured experts from various fields leading the various sessions.

*Details given below:*



## REAL ESTATE INVESTMENT TRUSTS (REITS) TRAINING

**Venue:** Pridelnn Hotel, Lantana, Nairobi

**Date:** Wednesday 23rd October 2019

**Time:** 8.00am – 5.00pm

### LEAD THE WAY

REITs present themselves as an investor-friendly, tax efficient vehicle for real estate investment. Accordingly, more effort needs to be put into making the REIT vehicle better understood by various stakeholders. This training aims at providing introductory knowledge about the functioning of REITS as a capital markets product. Some of the topical areas of focus include the various types of REITS and the regulatory framework and the tax and compliance framework of REITS. This seminar aims to form a base for subsequent topical areas of focus.

### SHOW YOUR SUPPORT

The Nairobi Securities Exchange (NSE) in collaboration with REITs Association of Kenya (RAK) will hold a full-day REITs workshop on Wednesday 23rd October 2019 from 8:00 am to 5:00 pm at Pridelnn Hotel, Lantana, Nairobi.

### CHARGES

Ksh. 25,000 (Excl. VAT)

**Registration Fee, Course Work Materials, Certificate, Meals and Refreshments**

**REGISTER THROUGH R.A.K AND ENJOY A 40% DISCOUNT**

◆ **Participants registering through RAK**

**Ksh. 15,000 (Excl. VAT)**

#### PAYMENT DETAILS:

Account name: Nairobi Securities Exchange Limited  
Bank: Kenya Commercial Bank  
Branch: Moi Avenue, Nairobi, Kenya  
Or MPesa Till Number: 733333

Kindly RSVP with payment by Wednesday 16th October with the RAK Secretariat on telephone through 020 283 1000 or by e-mail to Wendy Owade on [raksecretariat@nse.co.ke](mailto:raksecretariat@nse.co.ke) or [wowade@nse.co.ke](mailto:wowade@nse.co.ke)

### TARGET AUDIENCE

- Real Estate developers
- Regulatory institution who directly or indirectly regulate investments
- Portfolio & Fund managers
- Trading participants
- Investors keen to invest in REITS
- Custodians
- Insurance Companies
- Sacco's keen to invest in Real Estate
- Real Estate Lobby groups
- Graduates interested in pursuing a career capital markets

### COURSE COVERAGE

1. Overview of REITS
  - What is a REIT
  - Global developments and trends
  - An overview of REITs/property in the Kenyan market
2. Structure of REITS
  - Key features
  - Investment rules and borrowing powers
  - Criteria for converting a traditional investment into a REIT
  - REIT Regulatory and compliance requirements
3. Tax treatment of REITS
  - From the perspective of the REIT vehicle
  - From the perspective of the investor
4. Understanding how to invest in a REIT product
  - Advantages & Disadvantages
  - Tools to evaluate a REIT
  - Types of investors in a REIT
5. Legal framework guiding issuing of REITS in Kenya
  - CMA Regulations
  - NSE listing and trading rules
6. Real estate market cycles
  - The state of the sector and the competitive and strategic issues around REITS
  - Issues surrounding REITS in the Kenyan market
7. Trading REITS

**Q1 2020**

**SAVE  
THE  
DATE**

## 2<sup>nd</sup> REITS CONFERENCE

The conference will aim to bring together the demand and supply sides of the real estate sector to highlight investable opportunities within the industry. The event will be highly interactive, informative and engaging.

Wendy Owade, RAK Senior Administrator  
The Exchange, 55 Westlands Road

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