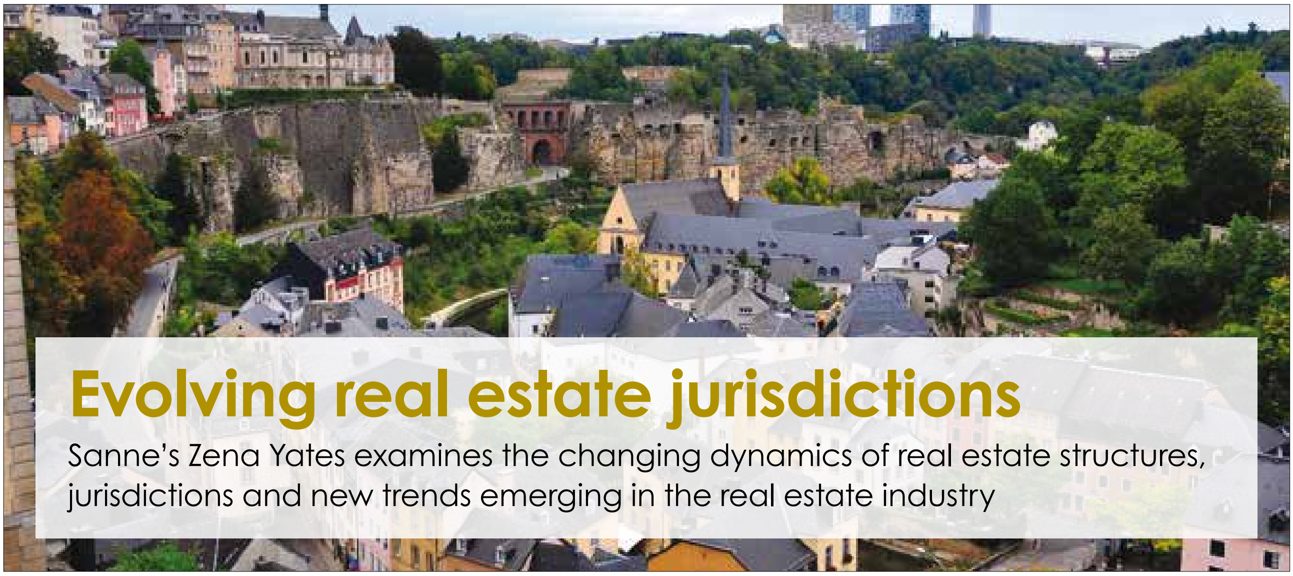

Evolving real estate jurisdictions

Sanne's Zena Yates examines the changing dynamics of real estate structures, jurisdictions and new trends emerging in the real estate industry

Luxembourg: the go-to onshore domicile

In recent years we have seen a move away from commingled real estate funds and a swing in popularity towards direct or joint venture deals. Currently, there seems to be another shift again as commingled real estate funds are rising back into popularity. These type of pooled funds provide smaller institutional investors with an opportunity to enter or re-enter the market. Competition for core assets has also intensified due to the growing capital chasing a relatively limited number of assets. This has led many investors to invest in more secondary assets and other areas of real estate such as retirement living, private rental accommodation, ground rents and student accommodation to provide their investors with opportunities to better returns. In order for these types of real estate investments to provide attractive returns lot sizes are usually large and generally via regulated fund vehicles. Such vehicles are often caught by the implications of increased regulation.

AIFMD

The biggest regulation impacting real estate fund managers in Europe, and also being felt further afield, is the pan-European marketing regulation the Alternative Investment Fund Managers Directive (AIFMD). With the full effect of the AIFMD now being realized, it would be natural to anticipate further consolidation of some managers as smaller players struggle to adequately service the requirements due to the increased complexity of the regulatory environment. The increased cost of the AIFMD can also be seen as a barrier to entry for newer managers as they try to launch their first funds into Europe.

Existing managers are now starting to feel the regulatory pressure as they try to cope with the increased burden of regulation, increased reporting requirements and the need to be more transparent. AIFMD compliance has certainly created an increase in fund reporting support by professional administration businesses like Sanne, whom have the expertise to provide reporting solutions and assist managers to navigate through the earlier cycles of AIFMD compliance.

Jurisdiction de jour

When setting up new real estate holding structures, managers appraise the use of offshore vs onshore vehicles. UK property managers often strongly favour the Channel Islands as an offshore domicile of choice, with volumes rising by over 50 percent in the past 5 years. This is due to the historic use of the popular and favorable Jersey Property Unit Trust regime, which is still commonly used today, and more recently the introduction of its Private Placement Fund regime. The regime offers managers more flexibility without the full costs and reporting required under the full AIFMD `passporting' compliance.

The Channel Islands also benefit from a highly skilled workforce, equivalent time zone with the UK and excellent transport links to and from Europe. Jersey is a well regulated jurisdiction for foreign investors with many sovereign wealth funds from Asia, North America and the Middle East setting up vehicles in the last 12 months. In addition, a number of high profile property funds are structured through Jersey including the second largest Real Estate Investment Trust listed on AIM.

The onshore jurisdiction of choice remains Luxembourg, with an established infrastructure of leading advisory, banking and service provider intermediaries. Luxembourg offers effective tax structuring opportunities for pan-European real estate companies which which utilize intermediary holding companies and asset owning companies through the SOPARFI regime, commonly using the private limited liability company (SARLs) and the benefits of the participation exemption relating to capital gains tax. Luxembourg has many double taxation treaties (including all the other major fund domiciles) which attracts investor cash flows while also benefitting from EU directives to offer efficient cross-border investment opportunities.

Most real estate funds are now using Luxembourg in some way, shape or form. The most commonly used structures are unregulated vehicles known as SARLs as outlined previously. Regulated fund structures offer many different scopes, there are various partnership models (similar to the UK limited partnership), SICAV (variable) of SICAF (fixed) designed for open and closed ended vehicles, and SICARS for development property projects. More recently, the SIF law has been introduced which offers the aforementioned type fund structures but under lighter supervision from Luxembourg's securities regulator, the CSSF.

Investors and advisors from Europe, US and Asia are comfortable with Luxembourg and the robust legal and regulatory structured framework. Since AIFMD came in to play funds often look at Luxembourg more closely as the concept of custody and depositary services was new to all other real estate jurisdictions. The Luxembourg political landscape is very stable and supportive of new regulatory enhancements to address investor protection. More and more real estate funds originating from Asia are now being set up in Luxembourg.

Luxembourg, for many years, has been a key location for fund managers to establish and build their own substance offering, with many more looking to set up dedicated offices to better equip themselves to handle the AIFMD in Luxembourg. Sanne has witnessed a growing need for professional assistance from managers looking to establish themselves operationally in this jurisdiction. The quality of service is paramount for them, as is the value add ability to navigate safely through the regulatory environment in Luxembourg.

Real estate debt

As banks continue to face their own challenge of increased regulatory demands and the need to deleverage balance sheets, non-bank lenders have become more prevalent in the real estate finance market. While banks are increasing their lending it would appear to be limited to prime investments, re-financing of existing portfolio investments and some core secondary assets. This has led to the increased use of non-bank lenders such as insurance companies, hedge funds, private equity funds and debt funds whom have responded with a positive appetite to offer debt secured against real estate assets.

We have also witnessed the foray by our real estate clients into real estate debt and we are now pursuing solutions for real estate managers looking to adopt different strategies in relation to their exposure to real estate.

Currency gains

There is an increase in the number of participants in all investor categories, with US and Asian investors still leading the way. For US-domiciled investors, the depreciation in the cost of Eurozone-based assets, from their perspective, is generating greater interest for those targeting exposure to this market. The current USD/EUR cross-currency environment provides US investors with a significant discount at a time when European asset values are rising in local currency terms.

Outlook

The weight of money has pushed yields down to pre-crash levels. Investors around the world see the UK market as a safe haven and we are certainly witnessing a continued surge into UK property. With supply limited, in relative terms, this has forced our clients to look at real estate sectors which they previously wouldn't have invested in. We have also seen increased investment into Eurozone cities such as Berlin, Dublin, Athens and secondary UK cities such as Birmingham and Manchester.

The current perspective is that for 2015, cross-border investors will have plenty of capital to deploy, and that whilst the UK has enjoyed investment recovery ahead of Europe, it still holds strong attractions for investors, and an uplift in investment turnover is expected.

As a global provider of real estate administration, we expect the demands for best in class real estate administration services to increase as managers seek to appoint specialist partners that can ease their regulatory pressure and reporting requirements. Sanne, like others in the market, see the rest of 2015 and 2016 as an exciting period of growth on a macro level. □

Zena Yates

Head of real estate

Yates heads Sanne's real estate business and has over 15 years' experience in the offshore financial services industry administering a wide variety of offshore real estate structures including limited partnership, corporate structures, private unit trusts and expert funds. She is responsible for the services and product offering of real estate, specializing in transaction management and the operation of multi-jurisdictional structures.