

Recommendations Towards the Revitalization of J-REITs and Japanese Real Estate Investment Market

- The final report of the Forum for Building Up the Real Estate Investment Market that is Trusted by Investors -

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The Forum for Building Up the Real Estate Investment Market
that is Trusted by Investors

Recommendations Towards the Revitalization of J-REITs and Japanese Real Estate Investment Market

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I. Members of the "Forum for Building Up the
Real Estate Investment Market that is
Trusted by Investors"

Forum for Building Up the Real Estate Investment Market that is Trusted by Investors

List of Members of the Forum

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Hideki Kono (Observer)
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Forum for Building Up the Real Estate Investment Market that is
Trusted by Investors:

List of Members of the Working Group

As of May 25, 2009

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Riichi Morihiro, Chief Operating Officer, Nippon Building Fund Management Ltd.

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Masaru Itagaki, Managing Director, Asset Finance Department, Nomura
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II. The Final Report (Summary)

Recommendations Towards the Revitalization of J-REITs and Japanese Real Estate Investment Market

- The Final Report of the Forum for Building Up the Real Estate Investment Market that is Trusted by Investors -

(Summary)

1. Introduction

Since its commencement in 2001, Japanese REITs (J-REITs) had grown steadily and also made significant contributions to urban development and other aspects in Japan through acquiring properties as well as increasing the value of owned properties. However, triggered by the subprime loan problems, J-REITs turned to a downward trend. With the number of properties acquired by J-REITs quickly decreasing, they have entered an adjustment phase for the first time. The J-REIT market is the basic foundation of the real estate investment market in Japan. It is required to enhance investor trust in J-REITs, to reactivate them as early as possible, and to reconstruct a good circulation of funds around real estate. By doing so, the rehabilitation of cities and local communities must be promoted.

2. Necessity of Reorganizing J-REITs through Mergers and Other Measures

With regard to the J-REIT market, it has been pointed out that the entire market is being damaged by the fact that there are few mergers and acquisitions, despite a market environment favorable for buyers as exemplified by the existence of many investment corporations that have a low PBR (price-to-book ratio). There is also a strong opinion claiming that it is more desirable for pension funds and other investors to invest in investment corporations with larger total assets. Mergers serve as a measure that would allow them to expand their asset size without spending a lot of money. It would also help meet the expectations of investors and further activate the J-REIT market. The Forum held discussions, as described below, concerning the reorganization of J-REITs. Given that the relevant systems have been revised to date in a way that should contribute to promoting mergers, the Forum expects the J-REIT market to make further developments through mergers

between investment corporations and other measures using these systems.

- (1) The present formula used to determine whether conduit requirements are satisfied includes both income for taxation purposes and profits for accounting purposes in a mixed way. In order to resolve the unstable nature of the conduit determination, revisions have been sought so that the judgment should be based on profits for accounting purposes, not including income for taxation purposes. There has also been a concern that investment corporations might hesitate to merge with other investment corporations because the present conduit requirements could not necessarily be satisfied after the merger. We believe this concern has been appeased, as the fiscal 2009 tax reform revised the formula used to judge the conduit nature.
- (2) In the case of a merger between investment corporations, the surviving investment corporation is required to pay the so-called merger grants to the unitholders of the dissolved investment corporation in order to adjust the fractions of the merger ratio or to make other adjustments. However, there is no explicit provision in the Investment Trust Law and the concern was that this might discourage mergers between investment corporations. We believe this concern was eased as the Financial Services Agency revised the relevant Cabinet Office Ordinances and its Inspection Guidelines in an effort to clarify the legitimacy of practical application.
- (3) As for the delisting and liquidation of investment corporations, which are legally possible, there are such issues of concern as how opposing unitholders should be protected, the contraction of the J-REIT market due to sales of investment properties, and the impact on the overall real estate market. Accordingly, the Forum believes that investment corporations should endeavor to stay in the J-REIT market through such measures as mergers, changes in sponsors and switches of asset management companies.

3. Corporate Governance of J-REITs

Recently, administrative penalties were imposed on multiple asset managers for such activities as those that constituted conflicts of interest with the investment

corporations, and it has been pointed out that corporate governance of asset managers should be reinforced. Given this situation, the Forum held the below outlined discussions concerning specific measures to reinforce their governance capabilities while making comparisons to systems of various countries.

(1) The world's REIT systems are divided into externally-managed REITs (such as Japan) and internally-managed REITs, or a combination of externally- and internally-managed types (such as the U.S.). Both types have their respective advantages, and no general valuation can be made concerning which is more beneficial for investors. However, we believe there is a common global endeavor to enhance the trust of investors by aligning the interests of asset managers and investors as much as possible.

(2) Such schemes as internally-managed REITs and the stapled securities system in other countries can be informative. However, if we are to attempt to introduce similar systems in Japan, there are still many issues that need to be examined, including the avoidance of taxation before paying dividends and discernment as to how the system would be positioned in relation to relevant laws and regulations. While it is important to continue examination among related parties on these ideas, it is essential for each J-REIT to voluntarily work on measures that should further enhance the trust of investors. Efforts to reinforce investor trust in J-REITs would include the following measures.

(a) Strengthen monitoring by investment corporations of the fiduciary duties and other responsibilities being performed by their asset managers

Executive directors of investment corporations have an important mission to conduct monitoring, as representatives of investors, whether the asset managers are fulfilling their fiduciary duties, duties of diligence of a good custodian and other duties towards the investment corporations. For this purpose, investment corporations would need to secure personnel and budgets that are required to conduct such monitoring, so as to allow the executive directors to sufficiently and proactively achieve their missions.

(b) Appoint outside directors for asset managers

From the viewpoint of reinforcing corporate governance of asset managers, etc.,

asset managers would appoint outside directors who are highly independent and can be expected to monitor the asset managers' business executions with a perspective of securing the interests of investors.

(c) Further elaborate the compensation systems of asset managers

Further elaboration would be made to the compensation systems of asset managers in a way that should contribute to the alignment of interests between asset managers and investment corporations.

4. Financing by J-REITs

Under the global credit crunch, strengthening the financial standing of individual J-REITs is a critical issue. In this regard, the Forum conducted discussions, as presented below, concerning a wide variety of options that could be introduced to Japan, on the condition that it is necessary to fully discern whether such options are suitable in terms of investor protection and systems in Japan.

(1) Diversification of Financing Methods by J-REITs

In order for individual J-REITs to construct a stable financial foundation that allows them to avoid over-dependence on loans, etc., they may dynamically collect investment funds to lower borrowing ratios or take other measures. Within the market environment where capital increases through public offering are difficult due to stagnant stock prices, the only practical way is to increase capital by way of third-party allocation, since the Investment Trust Law allows J-REITs to issue nothing but ordinary investment units (an equivalent of common stocks in stock-related vocabulary). However, if capital increases are conducted through third-party allocation within a situation where investment unit prices are falling, investors may not necessarily come to welcome them. Given such situations, the Forum has conducted the following studies concerning the diversification of financing, referring to cases in foreign countries where financing methods for REITs have been as diversified as those for general operating companies.

a) Rights Issue (capital increase through unitholder allocation)

Rights Issue is used by foreign REITs particularly as a means to procure funds in times of recession. Japan has seen no case of use of this method, although the

Investment Trust Law does not specifically ban it. Meanwhile, there are issues to be examined from the viewpoint of protecting investors. Such issues include: investors who do not or cannot agree to additional investment will lose their rights and cannot enjoy benefits, possibly resulting in decreases in per-unit investor equity or dividend. Therefore, related parties should prudently examine the preparation of systems that will make it possible to appropriately conduct capital increases through unitholder allocation.

b) Convertible bonds (investment corporation bonds with subscription rights to new investment units)

Although it is recognized that the issuance of convertible bonds by J-REITs is difficult under the Investment Trust Law, many countries including the U.S. allow the issuance of such bonds. If convertible bonds were issued at a time when investment unit prices remained stagnant, it would allow such expectations as reduced borrowing ratios as conversion rights are executed through the process in which investment unit prices should recover to the level of the NAVs. On the other hand, there is also a concern that, depending on how the conversion prices of the convertible bonds are set, a significant level of dilution would be caused through their conversion into a huge amount of investment units. Therefore, prudent investigations should be made on such issues as fully securing governance and the need for system design for investor protection, while considering the possibility of their introduction in Japan.

c) Classified stocks (classified investment units)

Issuance of classified investment units would be difficult under the Investment Trust Law, but they are generally used in the U. S. In Japan, approving the issuance of classified investment units so as to meet various types of investors' needs is expected to help investment corporations improve their financial standing and increase investor trust. However, the issuance of preferred investment units might also bring about a negative impact, as it would make all outstanding investment units subordinate to them and have a major impact on existing investors. Because of this, prudent investigations should be made on this issue while considering the possibility of their introduction in Japan as well as focusing on fully securing governance and protecting investors.

d) Acquisition of treasury stocks (acquisition of treasury investment units)

As a rule, the Investment Trust Law prohibits investment corporations from acquiring treasury investment units. Meanwhile, the acquisition of treasury stocks by REITs is permitted in such countries as the U.S., and is utilized for their capital and dividend policies, etc. Now that investment units are listed, pricing measures on investment units by investment corporations are important in order to enhance investor trust. On the other hand, depending on the source of funds to acquire treasury investment units, care must be taken with regard to the relationship with existing creditors and to fair and equal handling of all unitholders. Accordingly, prudent investigations should be made as to how systems should be to take into account investor protection, while considering the possibility of approving the acquisition of treasury investment units in Japan.

(2) Necessity for Individual J-REITs to Reinforce their Financial Strategy Functions

Given the credit crunch currently prevailing, it has become important for individual J-REITs to reinforce their finance strategies and to improve their financial standing. Because of this, it is important for individual J-REITs to work to reinforce their financial strategy functions by such measures as securing staff that are highly capable in financial matters, in an effort to heighten investor trust.

Some investment corporations have been pointed out to have problems in redeeming the investment corporation bonds they issued. Investment corporations with upcoming maturity dates of these bonds must work to secure funds for redemption well in advance, through such measures as new borrowings from financial institutions and selling properties at appropriate prices.

(3) Necessity of Loans Provided Appropriately by Financial Institutions

J-REITs' main business is owning properties over the long term and leasing them for rent; they are not involved in risky business like that of real estate development. In spite of this, if financial institutions should refuse refinancing deals, it may force the unreasonable sale of properties in the real estate market that is said to have no buyers, and the drops in real estate prices might have a significant impact on the financial system and real economy. Due to this concern, we expect financial institutions to appropriately respond to refinancing requests

from J-REITs after fully reviewing their assets under management and other factors.

Moreover, although J-REITs have enhanced their presence as major buyers of income-generating properties, they are now adding to the “no buyer” situation in the real estate market, as the recent circumstances of stagnant stock prices and the credit crunch have made it difficult for them to newly procure funds and their property acquisition amounts have dropped rapidly. In order to stabilize Japan’s real estate market and the entire economy, it is important to revive the function of J-REITs as property buyers, such as encouraging investment corporations with high credit to buy blue-chip properties and stabilizing management by expanding their size through mergers, etc. For these issues, financial institutions should agree to requests for new loans as much as possible and contribute to the vitalization of the Japanese economy through supporting real estate buyers.

(4) Roles of the Government and Other Institutions

The financial operations of J-REITs must be conducted appropriately with the initiative of the private sector. However, if some investment corporations should go bankrupt, not only would investors lose confidence, but J-REITs would likely cause a crash in the real estate market by dumping properties and other actions. To prevent such from happening, the Japanese government took such measures as providing financial support under its “Emergency measures for activating housing and real estate markets” and conducted system reforms to facilitate mergers in the previous fiscal year. In addition, the government announced the “Countermeasures to Address the Economic Crisis” in April 2009 and stated that it will implement the “provision of funds to J-REITs through a Fund to be jointly established by the government and the private sector, etc.” The desire is that the measure will be implemented without delay. However, loans and other support by the Fund are nothing but a safety net. Individual J-REITs must not feel too secure to neglect voluntary efforts in improving their financial standing, reinforcing their governance, and so on. The measure should also not set back reorganization in the market. In designing detailed systems for preventing such moral hazards, it is expected that J-REITs must make further management efforts as conditions for obtaining support from the Fund.

5. Promoting Real Estate Investment by Retail Investors, Pension Funds and Other Investors

J-REITs are backed by stable rental income, and their dividends and investment unit prices should also be stable. Recently, however, it has been pointed out that their investment unit prices are strongly linked to stock prices and that, as the background of this linkage, owners of investment units are mostly foreign investors and the like, who are inclined to sell investment units to meet immediate needs for money or for other purposes. Considering the original characteristics of investment units, investors are supposed to be retail investors and pension funds, etc. who intend to own investment units for a long time. Still, we can hardly say that investment units have sufficiently reached such investors. Accordingly, the Forum held the following discussions concerning how to encourage the holding of investment units by them.

(1) Promoting Diffusion to Retail Investors

Since the recognition rate by retail investors of J-REITs remains at around one-third that of stocks, we expect that operators, related groups and other players will cooperate and endeavor to conduct promotion and other activities, and that securities companies and banks will make efforts such as proactive sales promotions as sales channels.

(2) Promoting Diffusion to Pension Funds

Pension funds abroad invest a great deal of funds in real estate, but many of Japan's public pensions make no investment in real estate. Since the entire real estate market in Japan is huge at approximately 2,300 trillion yen and has the potential to produce significant added value, we expect pension funds to proactively investigate investment in this class. On the other hand, developing products that satisfy the needs of pension funds is also important. To encourage them to invest, it is also important to investigate the use of advisory and other services by real estate investment advisors, and to study the necessity of organizations for investment education and enlightenment such as the Pension Real Estate Association (PREA) in the U.S.

6. Investigations on Real Estate Appraisals

Appraisals play a major role as a useful referential index for justifying the reasonability of trade prices, and the appraisal system has been revised as necessary in line with the expanded use of appraisals and other factors. However, it is pointed out that, when calculating using the discount cash flow (DCF) method, it is important in appraisals currently employed for properties subject to securitization, the appraisal values vary in accordance with variations in the discount rate and other yield factors even though rental income is stable. Since J-REITs disclose appraisal values and they have a major impact on the investment behavior of investors, real estate appraisers are expected to fully examine the grounds of the yields they appraised, such as the discount rates, and to describe the grounds in the appraisal statements in an easy to understand way, while J-REITs are expected to enhance their disclosure. Moreover, further investigations are required concerning the continuous appraisal of properties on the assumption of continuous ownership such as J-REITs.

7. Information Disclosure by J-REITs

(1) Information Disclosure by J-REITs

Individual J-REITs are endeavoring to provide information through timely disclosure, but it is pointed out that more unified disclosure is called for because the content of disclosure is not consistent among the respective corporations. Although providing information is accompanied with such problems as related costs, etc., it is desirable that individual J-REITs will discuss with market-related parties in efforts to make improvements in their endeavors to provide information useful for investment judgment.

(2) Housing Price Indices

Some people point out that, in Japan, the lack of such indices as the S&P/Case-Shiller Home Price Indices in the U.S. is one reason why the housing values perceived in the market are lower than what they are supposed to be. Therefore, we believe it is necessary for Japan to develop housing price indices based on actual selling prices and to make them widely available.

8. Other Issues for Activating the Real Estate Investment Market

(1) Development of Diversified Business Methods

The Forum discussed that investigations should be made into development of new business methods to allow the realization of a variety of businesses that meet market demands.

(2) Privately-Placed Real Estate Funds, Etc.

Privately-placed funds account for a large proportion in the real estate investment market. Presently, the credit crunch makes it difficult for many of them to be newly formed, and they are faced with the problem of redeeming their CMBSs (commercial mortgage backed securities). While the trends of privately-placed funds have a major impact on the real estate market, it may be possible to expect them to serve as new buyers of properties. Therefore, it is necessary for parties involved in the market to unite and study how to activate the real estate investment market in areas other than J-REITs, as well.

III. The Final Report (full version)

Recommendations Towards the Revitalization of J-REITs and Japanese Real Estate Investment Market

- The Final Report of the Forum for Building Up the Real Estate Investment Market that is Trusted by Investors -

1. Introduction

Since its commencement in 2001, the Japanese market of listed real estate investment trusts (J-REITs) had grown steadily in terms of market size, number of acquired properties and number of listed issues. J-REITs had also made significant contributions to urban development and other aspects in Japan through acquiring properties with abundant funds as well as increasing the value of owned properties. However, triggered by the subprime loan problems that occurred in 2007, the entire J-REIT market turned to a downward trend. With the number of properties acquired by J-REITs quickly decreasing, the J-REIT system has entered an adjustment phase for the first time in the seven years since its commencement. As a J-REIT went bankrupt for the first time in J-REIT history, and also due to appreciation of the Japanese yen, globally decreased stock prices, worsening economic indicators and other factors, the Tokyo Stock Exchange REIT Index momentarily marked an all-time low of 704 points. Though the REIT Index later rose again to the 900-point level (as of June 24, 2009), there is no telling how it will behave over time. Thus, we believe it a pressing task to enhance investor trust in J-REITs.

The Forum set up a specialized Working Group after the Third Forum for Building Up the Real Estate Investment Market that is Trusted by Investors was held on October 29, 2008 to conduct wide-ranging discussions on activating Japan's real estate investment market with a focus on J-REITs, including the reorganization of J-REITs through mergers and other measures, the necessity of reinforcing the governance of J-REITs, financing by J-REITS and the promotion of real estate investment by retail investors, pension funds and other investors. The Forum has summarized the discussion results, as presented below.

2. Necessity of Reorganizing J-REITs through Mergers and Other Measures

With regard to the J-REIT market, it has been pointed out that the entire market is being damaged by the fact that there are few mergers and acquisitions, despite a market environment favorable for buyers as exemplified by the existence of many investment corporations that have a low PBR (price-to-book ratio). There is also a strong opinion

claiming that it is more desirable for pension funds and other investors to invest in stable investment corporations with larger total assets. Mergers between investment corporations serve as a measure that would allow the creation of a larger investment corporation without spending a lot of money. This would help meet the expectations of investors and further activate the J-REIT market as well.

The Forum held discussions, as described below, concerning mergers and other forms of reorganization of J-REITs. Given that the relevant systems have been revised to date in a way that should contribute to promoting mergers, the Forum expects the J-REIT market to make further developments through mergers between investment corporations and other measures using these systems.

- (1) The present formula used to determine whether conduit requirements are satisfied includes both income for taxation purposes and profits for accounting purposes in a mixed way. In order to resolve the unstable nature of the conduit determination, revisions have been sought so that the judgment should be based on profits for accounting purposes, not including income for taxation purposes. There has also been a concern that investment corporations might hesitate to merge with other investment corporations because the present conduit requirements could not necessarily be satisfied after the merger. We believe this concern has been appeased, as the fiscal 2009 tax reform revised the formula used to judge the conduit nature. The revisions included that a conduit shall distribute at least 90% of the distributable income (not the income for taxation purposes) for accounting purposes and that the negative goodwill generated upon a merger (unrealized gains of the absorbed investment corporation obtained by the surviving investment corporation) shall be deducted from the distributable income for accounting purposes in the fiscal year when the merger takes place. Moreover, the revisions allowed the surviving investment corporation, if it obtains negative goodwill, to deduct the unrealized gains from the distributable income in the fiscal year when the unrealized gains occur. We believe that this has also eased the concern that, when conducting mergers, investment corporations must pay cash dividends equivalent to the unrealized gains in order to keep satisfying the conduit requirements.
- (2) In the case of a merger between investment corporations, the surviving investment corporation is required to pay the so-called merger grants to the unitholders of the dissolved investment corporation in order to adjust the fractions of the merger ratio or to

adjust dividend of profits when the settlement periods of the merging parties differ. There were doubts concerning the practical application of this rule because there is no explicit provision in the Investment Trusts and Investment Corporations Law (hereinafter, the “Investment Trust Law”), and the concern was that this might discourage mergers between investment corporations. However, we believe this concern was eased as the Financial Services Agency revised the relevant Cabinet Office Ordinances (enforced on January 23, 2009) and its Inspection Guidelines (applied on January 30, 2009) in an effort to clarify the legitimacy of practical application.

- (3) When conducting an M&A, there may be fractions of investment units (less than one unit per unitholder) to be issued to the unitholders of the dissolved investment corporation. If that is the case, the Investment Trust Law requires that the number of investment units equivalent to the sum of the fractions be sold on the stock exchange market and the proceeds from the sale be paid to the unitholders according to the fractions. This raised a concern that the investment unit price might drop significantly on the stock exchange market due to the sale. However, there were many in the Working Group pointing out that such a result could be avoided by, for example, trading on the ToSTNeT (Tokyo Stock Exchange Trading Network System) market.
- (4) As to the calculation method for a fair merger ratio upon merging, it is important to provide investors with sufficient explanation and disclosure concerning the thinking behind the calculation, the rationality of evaluations, etc.
- (5) The Forum also discussed the delisting and liquidation of J-REITs as a form of reorganization. Both ways are legally possible, but there are such issues of concern as how opposing unitholders should be protected, the contraction of the J-REIT market due to sales of investment properties, and the impact of their fire sale, etc. on the overall real estate market. Accordingly, investment corporations should endeavor to stay in the J-REIT market through such measures as mergers, changes in sponsors and switches of asset management companies.

3. Corporate Governance of J-REITs

Recently, administrative penalties were imposed on multiple asset managers, to which investment corporations entrust management of their assets, for activities that constituted conflicts of interest with the investment corporations or for their inadequate internal control

systems. Given these incidents, it has been pointed out that corporate governance of asset managers should be reinforced partly as a means of strengthening the trust of investors. Against this background, the Forum held the below outlined discussions while making comparisons to systems of various countries.

- (1) The world's REIT systems are largely divided into externally-managed REITs (Japan, Australia and Singapore) and internally-managed REITs, or a combination of externally- and internally-managed types (such as the U.S. and European countries). Both the externally-managed and the internally-managed types have their respective advantages, and no general valuation can be made concerning which is more beneficial for investors. However, as exemplified by the stapled securities system in Australia, there have been attempts to align the interests of asset managers and investors by listing the shares of asset managers and investment units of the managed REITs together for trading while basically maintaining the externally-managed system to avoid taxation on the REITs before distributing dividends. As such, we believe there is a common global endeavor to enhance the trust of investors by aligning the interests of asset managers and investors as much as possible.
- (2) In the J-REIT system, the Investment Trust Law and the Financial Instruments and Exchange Law oblige asset managers to provide asset management services with fiduciary duties (loyalty to the trustors' interests) and care of a good custodian on behalf of the investment corporations, which are trustors. Along with these duties, it is important for asset managers to make efforts to further align their interests with the interests of investment corporations, which are an assembly of investors, so as to enhance the trust of investors. In this regard, such schemes as internally-managed REITs and the stapled securities system implemented in other countries can be informative. However, if we are to attempt to introduce similar systems in Japan, there are still many issues that need to be examined. As for the internally-managed REIT, for example, an investment corporation would have to be a format that is more similar to a corporation under the Company Law as it manages assets by itself and, also from the perspective of a comparison with other legal systems, it would not be able to avoid taxation before paying dividends. With regard to the stapled securities system, there also appear to be many issues to be examined, as Japan has had no cases of trading shares of multiple companies as a single unit and there would be a need to discern how the system would be positioned in relation to the Financial Instruments and Exchange Law as well as other relevant laws and regulations. While it is important to continue examination among related parties on

such ideas as internally-managed REITs and the stapled securities system in pursuing ideal J-REITs that secure the trust of investors, it is essential for each J-REIT to voluntarily work on measures that should further enhance the trust of investors at an early stage. Efforts to further reinforce investor trust would include the following measures.

(a) Strengthen monitoring by investment corporations of the fiduciary duties and other responsibilities being performed by their asset managers

Executive directors of investment corporations have an important mission to conduct monitoring, as representatives of investors, whether the asset managers that manage assets based on entrustment agreements with investment corporations are fulfilling their fiduciary duties, duties of diligence of a good custodian and other duties towards the investment corporations.

In order to reinforce their monitoring functions, investment corporations would need to secure personnel and budgets (such as increasing the number of directors and outsourcing some of the monitoring functions as needed) that are required to monitor how their asset managers are performing their fiduciary duties, duties of diligence of a good custodian and other duties, so as to allow the executive directors of the investment corporations to sufficiently and proactively achieve their missions.

(b) Appoint outside directors for asset managers

From the viewpoint of reinforcing the corporate governance of asset managers and enhancing the trust of investors, asset managers would appoint outside directors who are highly independent and can be expected to monitor the asset managers' business executions with a perspective of securing the interests of investors.

(c) Further elaborate the compensation systems of asset managers

Further elaboration would be made to the compensation systems of asset managers in a way that should contribute to the alignment of interests between asset managers and investment corporations.

Furthermore, in an attempt to align the interests between asset managers and investment corporations, investment corporations would own shares of asset managers in order to be able to have a certain influence on the asset managers. However, this would require prudent examination from the viewpoint of protecting investors, etc. as it would also cause

investment corporations to bear the business risks of asset managers.

4. Financing by J-REITs

When acquiring real estate in accordance with the investment judgment of asset managers, J-REITs encourage retail investors to invest their money while procuring part of the funds required for the acquisitions by borrowing loans from financial institutions, issuing investment corporation bonds or through other measures. Covering part of the procured funds with low-cost borrowings should enable J-REITs to acquire properties dynamically and pay high dividends to investors, among other things. As such, procuring funds in combination with equity financing (investment by investors) and debt financing (loans, etc.) is a procurement method commonly employed worldwide. However, the global credit crunch has made it difficult to further increase capital. On the other hand, REITs around the world with particularly high dependence on debt financing are found to have difficulty in securing refinancing of their borrowings, and the U. S. has seen the bankruptcy of a REIT (a Chapter 11 bankruptcy case). In Japan, it has also become a major management issue for J-REITs to avoid default caused by violating the LTV provisions (pledges on borrowing ratios), which are financial covenants in loan contracts, and there is a concern that a growing number of J-REITs may be forced to sell their properties at disadvantageous prices in order to repay loans.

Characteristically, investment unit prices are supposed to be backed by assets under management that are expected to produce stable income gains. In reality, the prices have decreased significantly due to such factors as globally stagnant stock prices and worsening economic indices. Furthermore, increases in the number of properties sold as a measure to secure refinancing would cause a contraction of assets under management and a drop in dividends. Selling properties at cheap prices might cause a negative spiral as it places downward pressure on prices in the real estate market, which is in a recession, followed by lowered appraisal values of assets under management. Moreover, the first peak of redemption deadlines arriving for investment corporation bonds will come around September 2009 and after. This has made it necessary for J-REITs to secure cash on hand without selling their assets under management in a forced manner, to lower borrowing rates and to prepare for conducting refinances. Outside Japan, there are cases in which REITs endeavor to reinforce their financial standing; for example, some U.S. REITs work to prevent the outflow of cash on hand by partially paying dividends in treasury stocks instead of cash. In the British Commonwealth countries, REITs try to procure funds through rights issue at

issue prices far below market in spite of the market conditions in which general capital increases are hard to carry out; issue convertible bonds that can be exchanged into stocks when the stock prices recover; and conduct self-help efforts to sustain their stock prices by purchasing treasury stocks.

Strengthening the financial standing of individual REITs is also a critical issue in Japan. In this regard, the Forum conducted discussions, as presented below, concerning what can be devised to tackle this issue.

(1) Diversification of Financing Methods by J-REITs

J-REITs are by nature a collective investment scheme and represent a system that is based on investments by investors, and loans and other borrowings should be a complementary measure. In order for individual J-REITs to construct a stable financial foundation that allows them to avoid over-dependence on loans, etc., they may either sell their properties to repay loans, etc. and reduce asset size, or dynamically collect investment funds to lower borrowing ratios. Excessive sale of properties provokes concerns for negative impacts that include: investment units of J-REITs' losing their basic characteristic of being a stable income-gain product; decreases in dividends per unit; the shrinking J-REIT market; and the real estate prices triggered to drop. As for capital increases, on the other hand, the Investment Trust Law in Japan allows J-REITs to issue nothing but ordinary investment units (an equivalent of common stocks in stock-related vocabulary). As such, the only practical way to improve borrowing ratios within the market environment where capital increases through public offering are difficult due to stagnant stock prices is to implement capital increases through third-party allocation. In fact, there have actually been many cases using the third-party allocation method to increase capital. However, if capital increases are conducted through third-party allocation within a situation where investment unit prices are falling, the per-unit price for the allocated units will be significantly below per-unit investment funds. This is why investors have not necessarily welcomed the arrangement in all occasions.

Given such situations, the Forum has conducted the following studies as to how financing methods can be diversified in Japan, referring to cases in foreign countries where financing methods for REITs have been as diversified as those for general operating companies. Changes toward more diversified fund procurement by J-REITs have also already been seen in Japan, as a J-REIT issued subordinated investment corporation

bonds – the first among J-REITs – in February 2009 and an interpretation was indicated that capital increases by way of unitholder allocation at fair values are not banned under the Investment Trust Law. In order to allow respective J-REITs to implement the most effective financial policies for investors, we believe it necessary to investigate appropriate control methods, while prudently conducting examinations on introducing a wide variety of options, fully discerning if they have any disadvantages that harm investors' interests or if they fit J-REITs that embrace an externally-managed scheme. In doing so, references should also be made to the Company Law and the trends in overseas markets. This is also important for re-recognizing the essential nature of REITs as stable and income-gain-oriented financial products backed by real estate rental revenues.

a) Rights issue (capital increase through unitholder allocation)

Increasing capital through issuing investment units by way of shareholder allocation is used by foreign REITs particularly as a means to procure funds in times of recession. The amounts to be paid in these cases are usually set at a price significantly discounted compared with the market price, so that all shareholders are given opportunities to acquire the rights. In Japan, the Investment Trust Law does not specifically ban capital increases through unitholder allocation. Nevertheless, Japan has seen no case of capital increases through unitholder allocation by J-REITs because of such reasons as: the Investment Trust Law does not have provisions concerning capital increases through unitholder allocation while the Company Law has such provisions or applies to similar provisions; and Article 82-6 of the Investment Trust Law designates that “the paid amount for offered investment units must be a fair value in light of the content of assets owned by the investment corporation.” Meanwhile, there are issues to be examined from the viewpoint of protecting investors. Such issues include: investors who do not or cannot agree to additional investment will lose their rights and cannot enjoy benefits, possibly resulting in decreases in per-unit investor equity or dividend, or they may have an aversion to dilution and choose to sell their investment units, and; the amount of procured funds can vary in accordance with the proportion of investors losing their rights, so that care must be taken regarding how the funds are used. Therefore, related parties should prudently examine the preparation of systems that will make it possible to appropriately conduct capital increases through unitholder allocation, while grasping the needs of individual J-REITs and investors.

b) Convertible bonds (investment corporation bonds with subscription rights to new

investment units)

The Investment Trust Law neither has provisions equivalent to those in the Company Law concerning subscription rights to new stocks or corporate bonds with subscription rights to new stocks, nor applies to such provisions. As such, it is recognized that the issuance of convertible bonds by J-REITs is difficult under the current Investment Trust Law. By contrast, many countries including the U.S. and Australia allow REITs – not only company type but also trust type REITs – to issue such bonds. Indeed, there would be cases where investor trust could be improved if convertible bonds were issued as a means to procure funds at a time when investment unit prices remained stagnant, as it would help REITs implement policies including refinancing at low interests and improving capital structures. For example, REITs would be able to reduce borrowing ratios if conversion rights were executed through the process in which investment unit prices underestimated in the securities market due to refinancing risks should recover to the level of the NAVs (net asset values) of their assets under management. Moreover, capital sources such as strategic investors might be more inclined to buy convertible bonds in anticipation of the advantages that they could execute conversion rights in a process of rising investment unit prices; such capital sources would help decelerate the speed of dilution, caused by the conversion into investment units, throughout the lives of the convertible bonds. In fact, GPT Group, an Australian REIT, has combined rights issue and issuance of perpetual subordinated bonds with conversion rights to common stocks in an effort to reconstruct its financial structure, and has successfully improved its borrowing ratio by obtaining support from the Government of Singapore Investment Corporation.

However, there is also a possibility that, depending on how the conversion prices of the convertible bonds are set, a significant level of dilution would be caused through their conversion into a huge amount of investment units. Dilution might be further accelerated if the conversion prices were subject to some unlimited moving strike clauses. Moreover, downward pressure on investment unit prices may arise if trade practices are employed in which investment units are sold in the securities market while at the same time conversion rights are executed. On the other hand, no financial improvement – such as improvements in borrowing ratios – anticipated initially might be achieved if investment unit prices would not rise after issuance and the convertible bonds were not converted into common stocks (investment units) despite the arrival of conversion deadlines. Therefore, we believe that prudent investigations should be made as to the

product characteristics of convertible bonds and other factors, such as fully securing governance and the need for system design for investor protection, while considering the possibility of their introduction in Japan.

c) Classified stocks (classified investment units)

Issuance of classified investment units would be difficult as the Investment Trust Law neither has provisions equivalent to those in the Company Law concerning classified stocks, nor applies to such provisions. However, preferred stocks with conversion rights are generally used in the U.S. as a means to satisfy needs to procure funds over the long term. In the U.K. as well, a revision bill was announced in April 2009 that should allow REITs to issue preferred stocks with conversion rights. In Japan, approving the issuance of classified investment units so as to meet various types of investors' needs is expected to help investment corporations improve their financial standing and increase investor trust. However, the issuance of preferred investment units, for example, might also bring about a negative impact, as it would make all outstanding investment units subordinate to them and have a major impact on existing investors. Redemption of such preferred investment units would also become a big problem. Furthermore, there is a possibility that, if investors of investment units become relatively subordinated, such a situation would not fit the simple product characteristics of J-REIT investment units as financial products oriented to stable income gains. Because of this, we believe that prudent investigations should be made concerning such factors as to how classified investment units by investment corporations should be, while considering the possibility of their introduction in Japan as well as focusing on fully securing governance and protecting investors.

d) Acquisition of treasury stocks (acquisition of treasury investment units)

As a rule, the Investment Trust Law prohibits investment corporations from acquiring treasury investment units, except for such cases as succeeding them from investment corporations that cease to exist through mergers. The Law also does not have provisions corresponding to those in the Company Law concerning acquisition of treasury stocks by joint stock companies. Therefore, it should be difficult for investment corporations to acquire treasury investment units based on their own judgment. Meanwhile, the acquisition of treasury stocks (units) by REITs is permitted in such foreign markets as the U.S., Australia, Hong Kong and Canada, and is utilized for their capital and dividend policies as a means to counter stagnant stock prices or to improve dilution that occurs

after capital increases. It is also expected to possibly help improve investor trust. Nevertheless, care must be taken with regard to the relationship with existing creditors when using capital of the investment corporations as funds to acquire treasury investment units, and to fair and equal handling of all unitholders when using distributable profits to unitholders. Moreover, we believe it necessary to examine introducing regulations on insider trading, from the viewpoints of investor protection and securing fairness in securities trading including prevention of market maneuvering. Now that investment units are listed, pricing measures on investment units by investment corporations are important in order to enhance investor trust. In this regard, we believe that prudent investigations should be made as to how systems should be to take into account investor protection, while considering the possibility of approving the acquisition of treasury investment units in Japan.

e) Distributing stocks as dividends (distributing investment units as dividends)

Given the global credit crunch, it has become important for investment corporations to increase cash on hand to an adequate level. We believe that, in such an environment, giving more freedom to dividend policies in relation to conduit requirements should contribute to the improved financial standing of investment corporations, as it will allow them to internally retain cash on hand to a certain extent. In the U.S., for example, a measure was enforced in December 2008, in relation to the dividend requirement of distributing 90% or more of taxable income as a conduit requirement, in which REITs were permitted to distribute stock dividends according to investors' choices (although at least 10% of dividends must be done in cash and the measure shall be applied to dividends paid in the limited time frame of January 1, 2008 through December 31, 2009). It is pointed out that this measure has helped to control the outflow of cash on hand and reduce refinancing risks without violating the conduit requirements. In contrast, the Investment Trust Law of Japan is understood to prohibit investment corporations from using investment units as dividends in place of cash. In addition, the Special Taxation Measures Law stipulates in its provisions on recording paid dividends as losses that "distribution of monies paid by investment corporations" can be recorded as losses, and dividends in forms other than money cannot be recorded as losses and are subject to taxation. These show that issuing investment units in place of money for dividends is difficult. Investors may also have disadvantages when they want to liquidate investment unit dividends, since the market prices are low and selling them in the market will further lower the investment unit prices, although this leads to an easing of refinancing risks of

investment corporations. Accordingly, we believe it necessary to continue prudent examination concerning the distribution of investment units as dividends.

f) Establishment of provisions concerning capital decreases

If an investment corporation has its capital (unitholders' equity) decreased considerably due to impairment of the assets it owns, it may find it difficult to distribute profits as dividends over the long term. In this regard, there was an opinion in the Forum that such a REIT would be able to resume dividends as early as possible if provisions corresponding to capital decreases approved under the Company Law were introduced to the Investment Trust Law to allow it to cover losses due to capital decreases, and such an arrangement would also be effective in view of financing measures. Since the present system allows investment corporations to distribute dividends in excess of profits, we believe it necessary to clarify the position of such provisions on the system, and conduct an investigation on this issue while taking into account investor protection and other viewpoints.

(2) Necessity for Individual J-REITs to Reinforce Their Financial Strategy Functions

It is common practice globally for REITs to manage their assets by conducting a certain level of borrowing. Given the credit crunch currently prevailing, however, investors and lenders have started to pay attention to finance strategies of REITs, including borrowing ratios, lengths of loan periods, levels of loan interest and the status of collateral, as information directly relating to the management of the REITs. In Japan as well, it is pointed out that investment corporations noted to have dependence on securitization lenders and short-term debts, high borrowing ratios, etc. must improve their financial standing as a critical issue. As these show, what is important for heightening investor trust hereafter is not only on the asset side, where the key is the assets under management and how they are administrated, but also on the liability side, where appropriate financial strategies – taking loans and issuing investment corporation bonds on what conditions and to what degree, etc. – are essential. For example, such financial strategies would include diversifying repayment dates of respective loans so as to avoid duplication of maturity periods through a balanced combination of long-term and short-term debts – borrowing low-interest short-term loans as working capital over the short term, while securing stable long-term loans within a scope of rational judgment. Thus, we believe it important for individual J-REITs to work to reinforce their financial

strategy functions by such measures as securing staff that are highly capable in financial matters, in an effort to heighten investor trust.

The Investment Trust Law allows investment corporations to issue investment corporation bonds as a means to procure funds over the long term, and there have been many such bonds issued to date. Under the present credit crunch, however, it is understood that no investment corporations other than those with considerably high ratings can issue them. Nevertheless, there were events in February 2009 when subordinated investment corporation bonds were issued for the first time in J-REIT history, and the Bank of Japan newly included investment corporation bonds with a certain level of ratings in its list of eligible collateral. As these events suggest, it is hoped that the environment for issuing investment corporation bonds will recover as quickly as possible. In addition, with regard to short-term investment corporation bonds, investigations on the recovery of their issuance environment and the necessity to moderate issuance conditions are desirable from the viewpoint of expanding and enhancing fund procurement methods, as they represent a means to procure short-term funds speedily from sources other than financial institutions.

In relation to investment corporation bonds, some investment corporations have been pointed out to have problems in redeeming the investment corporation bonds they issued. In the case of borrowings from financial institutions, for example, investment corporations can ask the same financial institutions to refinance the loans again upon the arrival of maturity dates. In contrast, investment corporation bonds owned by institutional investors and other investors must be redeemed by the stipulated maturity dates. Because of this, investment corporations with upcoming maturity dates of investment corporation bonds must work to secure funds for redemption well in advance, through such measures as new borrowings from financial institutions, selling properties at appropriate prices, merging with other investment corporations or having sponsors with high credit participate in their operational management.

(3) Necessity of Loans Provided Appropriately by Financial Institutions

In acquiring and managing real estate properties, individual J-REITs use borrowed money and the like to partly fund the acquisitions. However, some financial institutions have found themselves unable to accept refinancing deals, partly because they have had difficulty in issuing loan obligation securitization products since the occurrence of

subprime loan problems. For other financial institutions, it is pointed out that, given the current credit crunch, they have made their refinance conditions too rigorous, such as shorter loan periods and higher interest rates and loan fees. However, J-REITs are a scheme in which they own high-occupancy, income-generating properties over the long term while enhancing the property values and returning the rent income to investors; they are not involved in risky business like that of real estate development. If financial institutions should refuse refinancing deals in spite of these characteristics of J-REITs, it may force the unreasonable sale of properties in the current real estate market that is said to have no buyers and, if properties cannot be sold in time for repayment dates, there might be bankruptcies and liquidations among J-REITs in worst case scenarios. The concern is, as a result, that the current drops in real estate prices will be accelerated and, through decreases in collateral values, there would be a significant impact on the financial system and real economy. Due to this concern, we expect financial institutions to be self-conscious that they are major players supporting the J-REIT market, and to appropriately respond to refinancing requests from investment corporations after fully reviewing their assets under management and how they are managed.

Moreover, since their establishment in 2001, J-REITs have enhanced their presence as major buyers of income-generating properties. In fiscal 2007, J-REITs acquired properties equivalent to approximately 1.5 trillion yen against approximately 3.3 trillion yen – the value of properties sold by listed real estate companies. Despite this, stagnant stock prices and the recent credit crunch have made it difficult for J-REITs to procure funds for newly acquiring income-generating properties. The reduction in property acquisitions by J-REITs, which sharply dropped to the level of 600 billion yen in fiscal 2008, is adding to the “no buyer” situation in the real estate market. In order to stabilize Japan’s real estate market and the entire economy, it is important to revive the function of J-REITs as property buyers, such as encouraging investment corporations with high credit to buy blue-chip properties featuring high yields and stabilizing management by expanding their size through mergers between investment corporations, etc. For these issues, we believe that financial institutions should agree to requests for new loans as much as possible by employing co-finance operations, etc. and contribute to the vitalization of the Japanese economy through supporting real estate buyers.

(4) Roles of the Government and Other Institutions

As stated above, it is needless to say that the financial operations of J-REITs must be

conducted appropriately with the initiative of the private sector, while continuing to disclose the content to investors in an appropriate manner. However, if some investment corporations should fail in securing funds and go bankrupt, not only would investors lose confidence in the entire J-REIT market, but J-REITs would likely cause a crash in the real estate market by dumping properties, contrary to their expected role as major buyers of properties.

To prevent such from happening, the Japanese government announced the “Emergency measures for activating housing and real estate markets” at the end of last year. The government has been providing financial support to residence/real estate operators and others (including J-REITs) that conduct sound operations by utilizing operations of smoothly responding to crises through the Japan Finance Corporation, and has immediately conducted system reforms to facilitate mergers between investment corporations. These measures clarify the government’s stance of supporting the J-REIT market, and are positively evaluated. In addition to these, the government stated in the “Countermeasures to Address the Economic Crisis” announced in April 2009 that it will implement the “provision of funds to J-REITs through a Fund to be jointly established by the government and the private sector, etc.”

This measure aims to stabilize the real estate market and prevent asset deflation by newly providing funds to J-REITs that are having trouble with fund procurement despite their stable cash flows and secured profits; forming a Fund in cooperation between the government and the private sector in order to recover the function of J-REITs as buyers; and working to recover the price formation functions in the market through the activities of J-REITs. The desire is that the measure will be implemented without delay. However, loans and other support by the Fund are nothing but a safety net. Individual J-REITs must not feel too secure to neglect voluntary efforts in improving their financial standing, reinforcing their governance, and so on. The measure should also not set back reorganization in the market.

In designing detailed systems for preventing moral hazards by the said Fund, it is expected that, if the Fund enables investment corporations to avoid bankruptcy, they must make further management efforts, including sponsor changes and mergers with other investment corporations, as conditions for obtaining support from the Fund.

5. Promoting Real Estate Investment by Retail Investors, Pension Funds and Other Investors

Given their primary characteristics, J-REITs should be able to produce stable dividends as they are backed by stable rental income, and their investment unit prices should also be fairly stable. Recently, however, it has been pointed out that their investment unit prices are strongly linked to stock prices and that, as the background of this linkage, owners of investment units are mostly foreign investors and financial institutions who are inclined to sell investment units to meet immediate needs for money or sell them at particular prices to avoid further losses. Considering the original characteristics of investment units, investors investing in REITs are supposed to be those who intend to own investment units for a long time – specifically, retail investors and pension funds, etc. Still, we can hardly say that investment units have sufficiently reached such investors. Accordingly, the Forum held the following discussions concerning how to encourage the holding of investment units by retail investors who have a strong inclination for saving and pension funds that expect stable income over the long term.

(1) Promoting Diffusion to Retail Investors

According to the survey conducted by The Association For Real Estate Securitization (ARES) in December 2008, the recognition rate by retail investors of J-REITs remains at around one-third that of stocks, and there were opinions that the product characteristics of J-REITs are not well understood. Although the industry held the “J-REIT Fair 2009 for Retail Investors” (sponsored by ARES) in March 2009 – the first such event – to facilitate recognition of J-REIT product characteristics, it is important that operators, related groups and other players first cooperate and endeavor to conduct promotion activities and investor education for retail investors.

Moreover, it is necessary for securities companies to further strengthen their sales activities, as they are the sole direct contact for selling investment units. We expect that they will take the initiative and make efforts to construct an environment that should facilitate investment by retail investors – such as raising the priority of J-REITs in their marketing strategies and enhancing recognition of their sales staff on J-REITs, and such.

Next, banks are expected to play certain roles, as they have strengthened their sales activities for life insurance and investment trusts (mutual funds) in recent years. At present, banks sell investment trusts that cover J-REITs. They are an extremely

important sales channel for expanding the retail investor base, and banks are expected to further reinforce their sales frameworks. J-REITs are an important part of investment products based on laws, and represent a major public interest as their investment funds lead to urban development through acquisition of income-generating properties and increasing the value of such properties. Banks are also expected to share this perspective and implement proactive measures to promote sales.

In addition, ETFs (Exchange Traded Funds, or listed investment trusts) were listed on the Tokyo Stock Exchange last year. They are a type of investment trust, and are linked to the TSE REIT index. By utilizing these ETFs, investors can make diversified investment with a small amount of money in each of the 40 issues of J-REITs listed on the Tokyo Stock Exchange. These products are also expected to contribute to the diffusion J-REITs to retail investors.

(2) Promoting Diffusion to Pension Funds

Pension funds abroad invest more funds in real estate compared to pension funds in Japan, motivated by the diversification of management subjects, pursuing high cash returns, securing inflation hedge effects, and other benefits. In contrast, only a limited number of pension funds conduct real estate investment, and many public pensions make no investment in real estate.

As far as the J-REIT market is concerned, there are opinions that the market is still too small for pension funds to invest. In this regard, we believe that reorganization and further growth of the market is needed through such measures as mergers between investment corporations. Meanwhile, the entire real estate market in Japan is huge at approximately 2,300 trillion yen and has the potential to produce significant added value. As such, we expect pension funds, which conduct stable investment over the long term, to more proactively investigate the effectiveness of real estate investment.

On the other hand, pension funds have expressed their expectations over years for large-sized privately-placed funds with low borrowing ratios that are specialized in managing stable assets in line with their demand for stable investment subjects over the long term. However, we cannot say that there has been a sufficient supply of products that respond to this requirement. Developing products that satisfy the needs of pension funds is also important from the viewpoint of executing social missions to meet the

national challenge of managing pension funds in the aging society.

To encourage pension funds to invest in real estate, it is also important to investigate the use of advisory and other services by real estate investment advisors with abundant knowledge and experience in real estate investment, and to study the necessity of organizations for investment education and enlightenment such as the Pension Real Estate Association (PREA) in the U.S., which was established in 1979 for providing communication opportunities for investors (including public pensions), management institutions and real estate service operators, and to provide opportunities for cross-industry dialogue specifically for real estate investment.

Furthermore, major institutional investors in the West have prepared Principles for Responsible Investment, which are the principles for socially responsible investment (SRI), under the guidance of the United Nations, and are proactively conducting socially responsible investments. Stable real estate investment by such pension funds and other investors may be more readily introduced into Japan if Japanese real estate operators are encouraged to further endeavor to develop and manage blue-chip properties that could be the subject of socially responsible investment.

6. Investigations on Real Estate Appraisals

Appraisals play a major role in real estate securitization, as the Investment Trust Law requires that price surveys be conducted based on appraisals by real estate appraisers, and the importance of appraisals is growing throughout the real estate securitization business. This is primarily because the appraisal system is recognized as a useful referential index for justifying the reasonability of trade prices of individual real estate transactions to investors. The background of this recognition is that real estate in general is an asset with high particularity, where prices are determined in negotiated contracts, and there is no price formed in a permanent and open transaction market – in contrast to general products traded in markets.

The real estate appraisal system has been revised in line with the expanded use of appraisals and other factors. The appraisal standards were amended in April 2007 to include items concerning appraisal of properties subject to securitization, and the report announced in April 2001 by the Real Estate Appraisal Subcommittee of the Land Policy Division at the National Land Council indicated directions that included reinforcing internal control systems in order

to enhance the credibility of appraisals.

Under the appraisals currently employed for properties subject to securitization, focus is put on the income capitalization approach that applies the discount cash flow (DCF) method as a rule. When calculated with the method, the appraisal values vary in accordance with variations in the discount rate and other yield factors. As such, it is pointed out that appraisal values vary significantly as a result of changes in yields in accordance with economic trends, although investment corporations usually intend to own assets under management for a long time instead of trading them, and enjoy stable rental income over the long term. Appraisal values of individual J-REITs are disclosed at the end of each fiscal term and, through comparisons with their book values and other measures, have a major impact on the investment behavior of investors.

Because of this, real estate appraisers are expected to fully examine the grounds of the appraisal values and the discount rates and other yield factors they employ in appraising, and to describe the grounds in the appraisal statements in an easy to understand way. In addition, it is desirable that individual J-REITs disclose the essential parts of appraisal statements to investors in a more enhanced way to provide explanations to investors as to the appraisal values and the yields used in the appraisals. Such disclosures are also expected to bring about such effects as improved appraisal quality and shared views on appraisal values and yields. Thus, it is desirable to conduct investigations concerning how to disclose the content of appraisal statements in a way that is easy to understand for investors.

Moreover, arrangements would also be effective for continuous evaluation of properties owned by J-REITs, such as the handling of negotiable securities for an accounting purpose that is treated differently according to the purposes of “owning them through maturity” and “owning for trade,” and such. On the other hand, however, there may also be many issues to tackle, including consistency with international accounting standards and other rules, as well as whether or not a problem arises from the viewpoint of investor protection in that continuous appraisal values are highly likely to differ significantly from appraisal values or actual trade values upon the acquisition or sale of properties. For this reason, further investigations are required concerning the continuous appraisal of properties and their disclosure on the assumption of continuous ownership such as J-REITs, with consideration given to opinions of investors, operators, financial institutions, real estate appraisers, certified public accountants, etc.

7. Information Disclosure by J-REITs

As products listed and traded on stock exchanges, J-REITs have contributed to the improvement in the transparency of the real estate market through timely disclosure by stock exchanges. The emergence of J-REITs has greatly enhanced the transparency of the real estate market in Japan. On the other hand, there were opinions that further improvement is required from the viewpoint of investors, and the Forum held the following discussions concerning disclosure by J-REITs.

(1) Information Disclosure by J-REITs

Individual J-REITs are endeavoring to provide information through timely disclosure on stock exchanges and on their respective websites, but it is pointed out that the content of disclosure is not consistent among J-REITs. In particular, there were opinions that call for more unified disclosure among J-REITs including information in English for overseas investors, which hold approximately half of the share in investment unit trading, or disclosure of such items as NOI (net operating income) and cap rates under the direct capitalization method that serve as assumptions for conducting appraisals, and repair and maintenance costs over the long term calculated upon the acquisition of properties. Of course, providing information is accompanied with such problems as related costs and the duty of confidentiality. However, in order to activate the market, constant efforts to provide information useful for investment judgment in a way that is easy to understand for investors are indispensable. Thus, it is desirable that individual J-REITs will continue to discuss with market-related parties including stock exchanges in efforts to make improvements.

(2) Housing Price Indices

In the U.S., housing indices based on actual selling prices are publicly available to make it possible to grasp housing price trends over a wide range of areas, and serve as important information for investors and other parties. Among such indices is the S&P/Case-Shiller Home Price Indices. There is no counterpart to these indices in Japan, and some people point out that the lack is one reason why the housing values perceived in the market are lower than what they are supposed to be. Therefore, we believe it is necessary for Japan to develop housing price indices based on actual selling prices and to make them widely available.

8. Other Issues for Activating the Real Estate Investment Market

(1) Development of Diversified Business Methods

The Forum discussed that investigations should be made into development of new business methods to allow the realization of a variety of businesses that meet market demands. Such methods might include those for joint entities solely comprising developers and real estate investment professionals to receive non-recourse loans and conduct development-type real estate investment businesses.

(2) Privately-Placed Real Estate Funds, Etc.

In comparison to the asset size of J-REITs totaling approximately 8 trillion yen, the asset size of privately-placed funds is approximately 3 trillion yen. Privately-placed funds also account for a large proportion in the real estate investment market. Generally, privately-placed funds are formed by such professional investors as institutional investors, and tend to have higher borrowing ratios compared to J-REITs. There are a variety of funds with different characteristics that have an extensive scope of assets under management, ranging from development-type assets to small-sized rental condominiums.

Presently, the credit crunch makes it difficult for new privately-placed funds to be formed, and many privately-placed funds are faced with the problem of redeeming their CMBSs (commercial mortgage backed securities) due to the drop in property prices. If the “no buyer” situation in the market does not improve, privately-placed funds may be forced to put their properties on the market. As these show, the trends of privately-placed funds have a major impact on the real estate market. On the other hand, there have been cases in which new privately-placed funds are formed with an aim to acquire income-generating properties that are currently priced lower than their value. It may be possible to expect them to serve as new buyers of properties.

While the trends and other events surrounding privately-placed funds must be watched carefully, it is necessary for operators, experts, government agencies and other parties involved in the real estate investment market to unite and study how to activate the real estate investment market in areas other than J-REITs, as well.

9. Closing

The J-REIT market is the basic foundation of the real estate investment market in Japan. The J-REIT market must be reactivated as early as possible, and a good circulation of funds around real estate must be reconstructed so that rehabilitation of cities and local communities is promoted.

Since October 2008, in an effort to establish the real estate investment market that is trusted by investors, the Forum repeatedly conducted discussions on a variety of measures that should help activate that market, with a focus on the J-REIT market, and future challenges to tackle.

Endeavors made by related parties to date have generated certain results, as the system concerning mergers between investment corporations has been enhanced and directions have been demonstrated for a variety of measures to activate the market. In the future, while implementation of such measures must be assured, profound discussions must be conducted sufficiently concerning how Japan's systems should be, and market participants including relevant business operators and government agencies must continue their efforts from their respective positions in order to overcome the challenges. Moreover, in promoting these endeavors, it is extremely important to conduct activities in which each market participant cooperates and works to obtain the general public's heightened trust of J-REITs – such as reinforcing governance capabilities.

IV. Reference

(Reference 1)

Forum for Building Up the Real Estate Investment Market
that is Trusted by Investors:
Meetings of the forum Held to Date

2008

October 28	Third meeting of the Forum Real Estate Securitization in Japan and Subject: Reorganizing J-REITs through Mergers and Other Measures (1)
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2009

January 30	Fifth meeting of the Working Group Subject: Financing by J-REITs (2)
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March 4	Sixth meeting of the Working Group Subject: Financing by J-REITs (3)
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(Reference 2)

Forum for Building Up the Real Estate Investment Market
that is Trusted by Investors:
Meetings of the Working Group Held to Date

2008

- | | |
|-------------|--|
| November 11 | First meeting of the Working Group
Subject: Reorganizing J-REITs through Mergers and Other Measures (1) |
| November 26 | Second meeting of the Working Group
Subject: Reorganizing J-REITs through Mergers and Other Measures (2) |
| December 9 | Third meeting of the Working Group
Subjects: Reorganizing J-REITs through Mergers and Other Measures (3)
Corporate Governance of J-REITs (1) |
| December 24 | Fourth meeting of the Working Group
Subjects: Corporate Governance of J-REITs (2)
Financing by J-REITs (1) |

2009

- | | |
|------------|---|
| January 30 | Fifth meeting of the Working Group
Subject: Financing by J-REITs (2) |
| March 4 | Sixth meeting of the Working Group
Subject: Financing by J-REITs (3) |
| March 31 | Seventh meeting of the Working Group
Subject: Promoting real estate investment by retail investors,
pension funds and other investors |

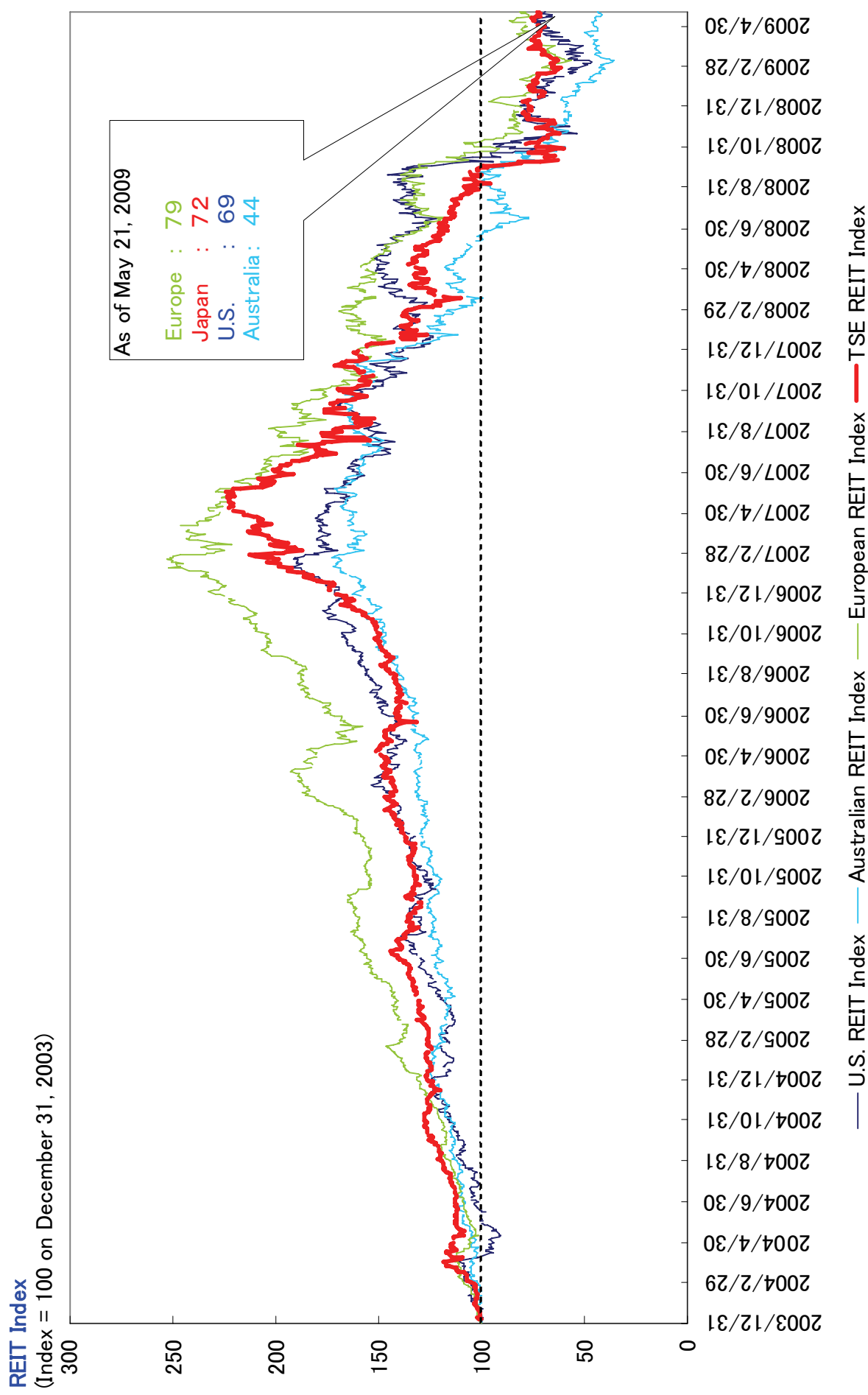
- April 20 Eighth meeting of the Working Group
Subject: Real estate appraisal, information disclosure and
 housing price indexes
- May 25 Ninth meeting of the Working Group
Subject: Other challenges concerning the real estate investment market

V. Reference Material

Reference Materials

1. Introduction

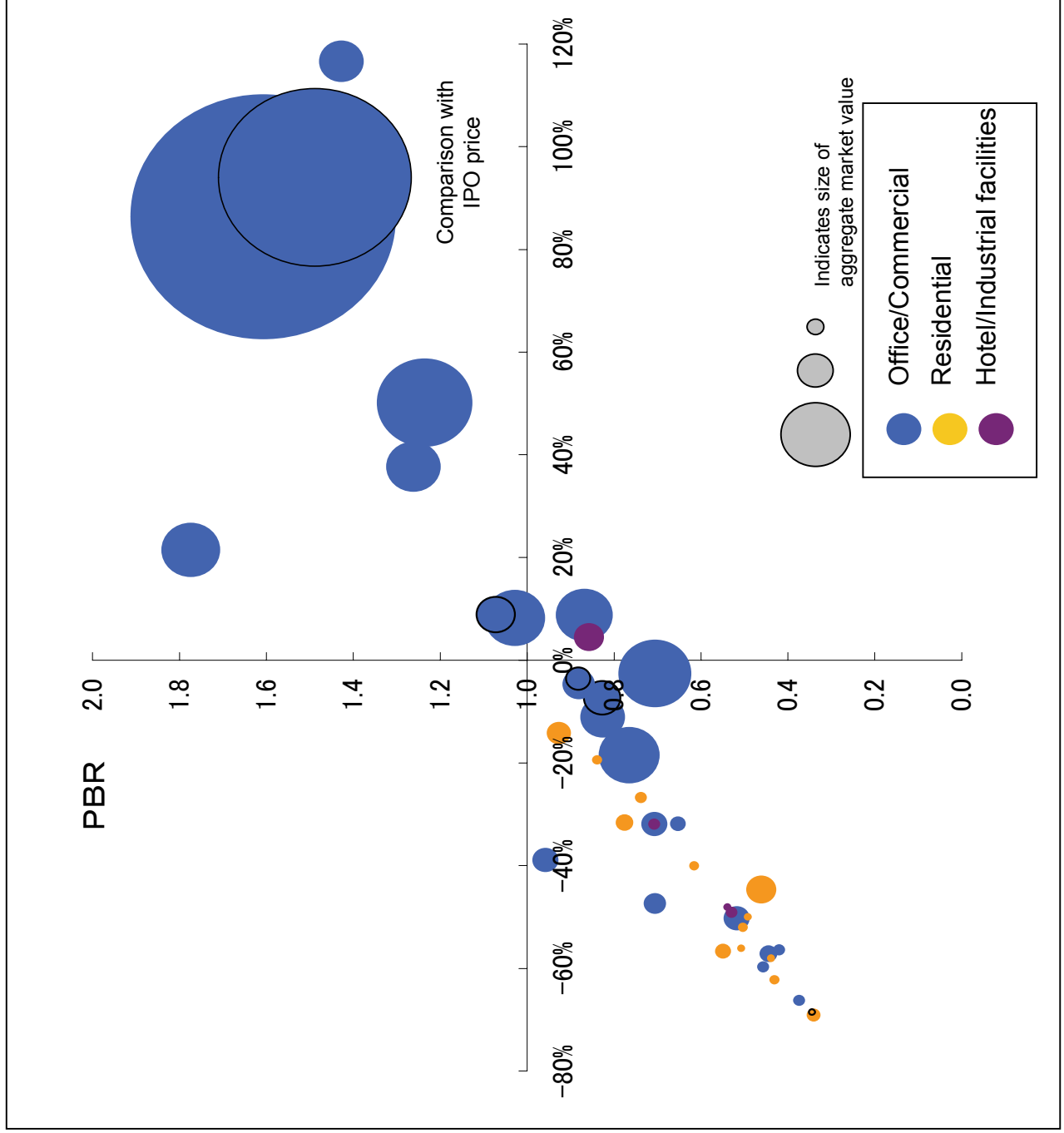
Trends in the Global REIT Market



Data: Prepared by ARES based on data provided by Bloomberg

2. Need to Restructure J-REITs, Including Mergers

Various REITs Exist



*PBR (Price-to-Book Ratio) = Aggregate market value ÷ (Net asset – Dividend)

Source: Prepared by Ministry of Land, Infrastructure, Transport and Tourism based on published data (as of August 22, 2008)

Clauses Concerning Mergers

Investment Trust and Investment Corporations Act

(Conclusion of Merger Agreement)

Article 145 Investment corporations may merge with other investment corporations. In this case, the merging investment corporations must conclude a merger agreement.

(Agreement for Absorption-type Merger)

Article 147 When investment corporations merge by absorption (when an investment corporation merges with another investment corporation, and all rights and obligations of the dissolving investment corporation are succeeded by the surviving investment corporation; hereafter, the same), the following items shall be stipulated in the agreement for an absorption-type merger:

- (i) The trade name and address of the surviving investment corporation (hereafter, the “surviving corporation of an absorption-type merger”) and the dissolving investment corporation (hereafter, the “dissolving corporation of an absorption-type merger”) of the merger by absorption
 - (ii) Matters concerning the number of investment units in the surviving corporation of an absorption-type merger that will be issued to investors of the dissolving corporation of an absorption-type merger in accordance with the merger by absorption, the method of calculating the number of investment units, and the total contribution by the surviving corporation of the absorption-type merger
 - (iii) Matters concerning the allocation of investment units in the previous item to investors of the dissolving corporation of an absorption-type merger (excludes the dissolving corporation of an absorption-type merger and the surviving corporation of an absorption-type merger; the same applies for the next item)
 - (iv) The date that the absorption-type merger takes effect (“effective date” in the next article and Provision 4)
- 2 In cases stipulated by the previous section, with regard to matters raised in (iii) of the previous section, investment units of the surviving corporation of an absorption-type merger shall be issued in accordance with the number of investment units owned by the investors of the dissolving corporation of an absorption-type merger.

(Agreement for Consolidation of Corporations)

Article 148 When two or more investment corporations consolidate (when two or more investment corporations merge, and all rights and obligations of the dissolving investment corporations are succeeded by the investment corporation established through the merger; hereafter, the same), the following items shall be stipulated in the agreement for consolidation of the corporations:

- (i) The trade name and address of the investment corporations dissolving through the consolidation of the corporations (hereafter, the “dissolving corporations after consolidation of the corporations”)
 - (ii) The purpose, trade name, address of headquarters, and total number of authorized investment units of the investment corporation to be established through consolidation of the corporations (hereafter, the “corporation established through consolidation of the corporations”)
 - (iii) Matters other than those raised in the previous item stipulated by the rules of the corporation established through consolidation of the corporations at the time of establishment
 - (iv) Name of the executive officer, supervisory officer, and accounting auditor of the corporation established through consolidation of the corporations as a replacement for the investors of the dissolving corporations after consolidation of the corporations in accordance with the consolidation of the corporations, the method of calculating the number of investment units, and the total contribution by the corporation established through consolidation of the corporations
 - (vi) Matters concerning the allocation of investment units in the previous item to investors of the dissolving corporations after consolidation of the corporations (excludes dissolving corporations after consolidation of corporations; the same applies for the next section)
- 2 In cases stipulated by the previous section, with regard to matters raised in (vi) of the previous section, investment units of the corporation established through consolidation of the corporations shall be distributed in accordance with the number of investment units owned by the investors of the dissolving corporations after consolidation of the corporations.

Systemic Revisions, etc. to Promote Mergers of J-REITs

① Improvement of conduit formula determining dividend requirement

① – 1 “Revision of the formula determining the dividend requirement”

The distributed dividends of J-REITs are included in expenses upon fulfilling various requirements (conduit nature), but the current formula determining the dividend requirement, which is one of the requirements, compares accounting income to taxable income as follows. When there is a large gap between accounting and tax (e.g. treatment of repair costs), a risk arises in that the conduit status cannot satisfy the formula. The latest revision is expected to allow judgment through accounting income alone.

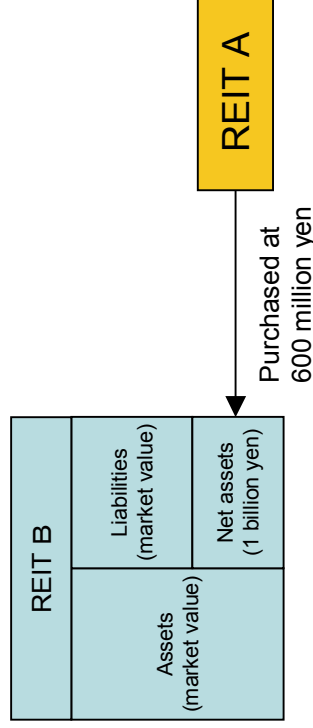
(Before revision)

Dividend from **accounting income** > **Taxable income** × 90%

(After revision)

Dividend from **accounting income** > **Accounting income** × 90%

① – 2 “Measure for negative goodwill”



In the case where REIT A merges with REIT B with net assets of one billion yen by absorbing REIT B at a price of 600 million yen, the “negative goodwill” of 400 million yen will be booked as REIT A’s liabilities after the merger. In terms of accounting, the 400 million yen will be recognized as profit*, but since REIT A did not actually attain 400 million in cash, it cannot fulfill the post-revision formula indicated on the left unless it procures over 360 million yen (400 million yen × 90%) in cash by newly selling property, etc. The measure exempts the amount equivalent to “negative goodwill” for this case from the post-revision formula for the business year that the “negative goodwill” occurs.

* With regard to the treatment of negative goodwill, the “Financial Accounting Standard for Business Combinations (published by the Accounting Standards Board of Japan on December 26, 2008)” revised equal amortization within 20 years to recording as one-time profit within the applicable business year (Timing of application: Applied from business combinations executed on or after April 1, 2010; however, it can be applied from the first business combination executed in business years commencing on or after April 1, 2009).

System Revisions, etc. to Promote Mergers of J-REITs

② Clarification of possibility of utilizing delivered money due to merger

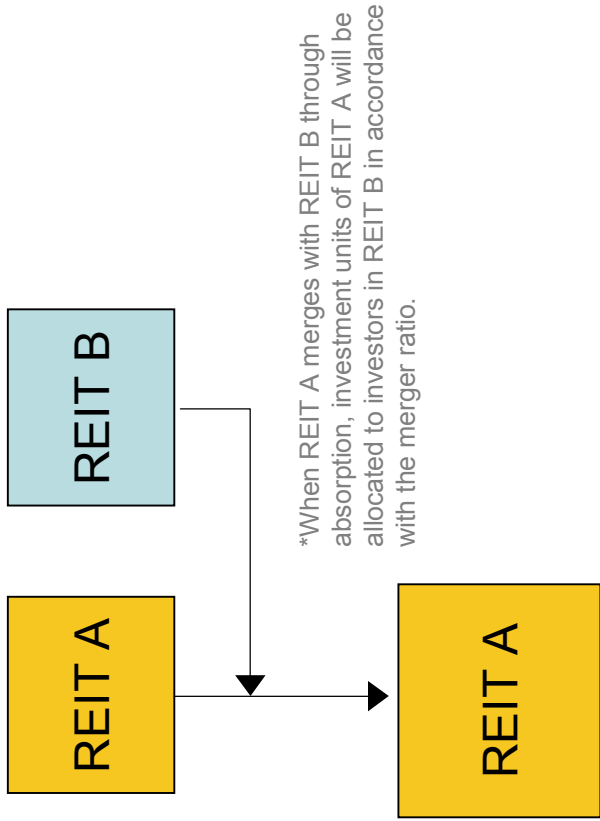
It has been clarified (revisions to cabinet ordinance and regulatory guidelines) that when REIT A merges with REIT B through absorption, cash can be paid to adjust fractions in the merger ratio and to adjust the profit dividend when the settlement periods of the merging parties differ (“delivered money due to merger”).

(Specific example of adjusting fractions in the merger ratio)

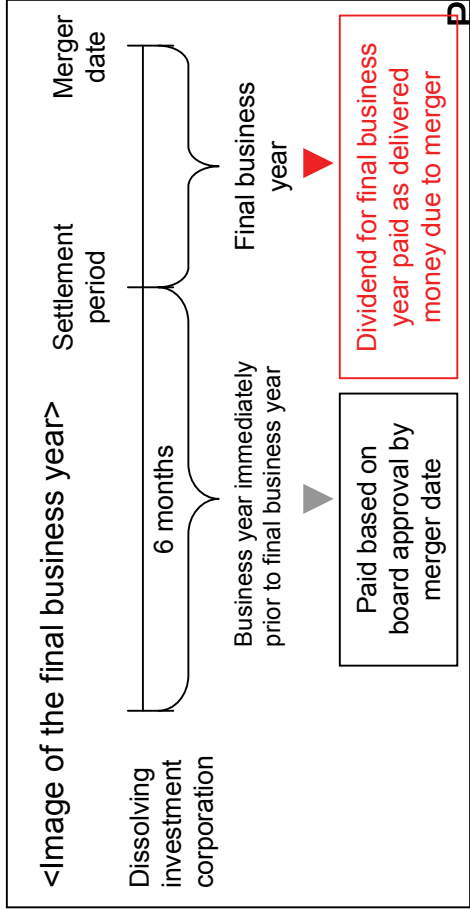
Investment units of REIT A will be allocated to the investors in REIT B, but if, for instance, the merger ratio of “REIT A : REIT B = 1 : 2.222” was to be ultimately adjusted to “REIT A : REIT B = 1 : 2,” the 0.222 portion will be paid to investors in REIT B as delivered money due to the merger.

(Specific example of adjusting profit dividend)

The dividend for the dissolving investment corporation for the final business year cannot be paid since a board meeting of the dissolving investment corporation cannot be held. Therefore, the dividend for the final business year will be paid as delivered money due to the merger.



*When REIT A merges with REIT B through absorption, investment units of REIT A will be allocated to investors in REIT B in accordance with the merger ratio.



Outline of Fiscal Year 2009 Tax Reform

Outline of Fiscal Year 2009 Tax Reform (Ruling party decision on December 12, 2008)

XI Other Tax Policies

25 Special exception on taxation of SPCs, etc. shall be reviewed as follows:

(1) (omitted)

(2) Requirement that paid dividends exceed an amount equivalent to 90% of distributable income shall be changed to a requirement that paid dividends exceed an amount equivalent to 90% of distributable profit. When there is negative goodwill, necessary adjustment measures shall be taken, such as a deduction from distributable profit in the year that the negative goodwill arises.

(3) Stipulations in laws and regulations concerning investment corporations have clarified the treatment of delivered money due to the merger of investment corporations. In accordance with this, it shall be clarified that delivered money due to a merger, which is comparable to a dividend, be included in paid dividends that are subject to inclusion in expenses.

Outline of Fiscal Year 2009 Tax Reform (Cabinet decision on January 23, 2009)

IX Other

15 Special exception on taxation of SPCs, etc. shall be reviewed as follows:

(1) (omitted)

(2) Requirement that paid dividends exceed an amount equivalent to 90/100 of distributable income shall be changed to a requirement that paid dividends exceed an amount equivalent to 90/100 of distributable profit. When there is negative goodwill, necessary adjustment measures shall be taken, such as a deduction from distributable profit in the year the negative goodwill arises.

(3) Stipulations in laws and regulations concerning investment corporations have clarified the treatment of delivered money due to the merger of investment corporations. In accordance with this, it shall be clarified that delivered money due to a merger, which is comparable to a dividend, be included in paid dividends that are subject to inclusion in expenses.

P9

Revision of the Ordinance for Enforcement of the Investment Trust and Investment Corporations Act (promulgated on January 23, 2009 and enforced on the same day)

(Advance Disclosure Items for Dissolving Corporation of Absorption-type Merger)

Article 193

(omitted)

- 2 In this article, a “merger consideration” refers to the investment units of the surviving corporation of an absorption-type merger **or cash** delivered to investors in the dissolving corporation of an absorption-type merger upon the absorption as a replacement for the investment units of the dissolving corporation.
- 3 “Matters concerning the reasonableness of a merger consideration” stipulated in Section 1, Item 1 refers to matters concerning the reasonableness of the stipulation (when there is no applicable stipulation, the absence of such stipulation) pertaining to the following items and other items raised in Article 147, Section 1, Items 2 and 3.
 - (i) Matters concerning the reasonableness of the **total** merger consideration (**refers to the total number of investment units and the total amount of cash**)
 - (ii) (omitted)
 - (iii) If cash is selected as a merger consideration, the reason for such**
- 4 “Matters that should serve as reference for a merger consideration” stipulated in Section 1, Item 2 refers to the following items and other pursuant items (when there is general consent from investors in the dissolving corporation of an absorption-type merger not to indicate or record all or part of these items in written or electromagnetic record, the items subject to such consent shall be excluded).
 - (i) (omitted)
 - (ii) The following items and other items concerning the method of converting into cash the **investment units to be delivered as a** merger consideration
 - a. Market where **applicable investment units** will be traded
 - b. Party to serve as an intermediary, agent, or proxy for the trading of **applicable investment units**
 - (iii) When there is a market price of the **investment units to be delivered as a** merger consideration, matters concerning the price
- 5 (omitted)

*Red font = Latest revision

P10

Comprehensive Guidelines for Supervision of Financial Instruments Operators, etc.
(revised on January 30, 2009 and applied on the same day)

VI – 2 – 7 Other Considerations

VI – 2 – 7 – 3 Considerations Concerning Mergers of Investment Corporations

When calculating investment units to be delivered to investors of the dissolving corporation in the case of a merger by absorption, if the merger ratio adjustment money or dividend substitutions (hereafter, “delivered money due to merger”) are delivered to adjust the merger ratio, etc., it must be noted that the items raised in Article 147, Section 1, Item 2 of the Investment Trust and Investment Corporations Act include the amount of delivered money due to merger, the calculating method, and matters concerning the amount of delivered money due to merger allocated according to the number of investor units owned by the investors in the dissolving corporation.

Investment Trust and Investment Corporations Act

(Treatment of Fractions Less Than One)

Article 149-17 In a case where the investment units of the applicable investment corporation are delivered to the party stipulated in each of the following items in the events raised in each item, if there are fractions of less than one investment unit of the applicable investment corporation, the number of investment units equivalent to the total of those fractions (fractions of less than one for the total shall be omitted) shall be **red in a manner stipulated by the cabinet ordinance**, which is the appropriate method to realize sale at a fair value, and distribute the money obtained from the sale to the applicable party.

(i) **Absorption-type merger** (limited to cases where the applicable investment corporation survives the absorption-type merger)
Investors in the dissolving corporation of an absorption-type merger

(ii) **Investors in the dissolving corporations after consolidation of corporations that issue investment units at the time of establishment of the new investment corporation based on the agreement for the consolidation of corporations**

2 Stipulations in Article 88, Sections 2 and 3 shall apply correspondingly in the cases of the previous section.

Ordinance for Enforcement of Investment Trust and Investment Corporations Act

(Method of Handling Fractions of Investment Units)

Article 199 The method established in the cabinet ordinance stipulated in Article 149-17, Section 1 shall be the method stipulated in each item below according to the classification of investment unit

(i) **Sale through trading on the financial instruments market** where the investment units of the investment security are listed on the financial market exchange

(ii) Sale through trading on the over-the-counter market where the investment units of the investment security comprise an over-the-counter security

(iii) Sale at a fair and rational price in light of the net asset amount of the investment corporation that issues investment units other than the investment units mentioned in the above two items

What is ToSTNeT Trading?

Can REITs be traded through ToSTNeT? (excerpt from the Tokyo Stock Exchange website, “Q&A for Investors on REITs”)

Q: Can REITs be traded through ToSTNeT?

A: REITs can be traded and the trading rules are exactly the same as stocks.

What is ToSTNeT trading? (excerpt from the Tokyo Stock Exchange website)

ToSTNeT trading is the buying and selling of securities and listed derivatives trading on the ToSTNeT market. ToSTNeT trading of cash commodities comprises Single Issue Trading, Basket Trading, Trading on Closing Price and Off-auction Repurchase of a company's own shares. Also, ToSTNeT trading of futures and options allows Cross-trading by the same participant and trading by different participants.

What is the ToSTNet market?

The ToSTNeT market refers to the off-auction market of the Tokyo Stock Exchange. Transactions executed on the ToSTNeT market through the electronic trading network system ToSTNeT (Tokyo Stock Exchange Trading Network system) are referred to as off-auction trading.

In response to the sophistication and diversification of off-auction trading, the Tokyo Stock Exchange revised its off-auction market system and established the “ToSTNeT Market” on January 15, 2008.

Domestic stocks, foreign stocks, and convertible bonds (CB) listed on the auction market are all listed on the ToSTNeT market and are available for off-auction trading. The main types of trading are Single Issue Trading, Basket Trading, Trading on Closing Price and Off-auction Repurchase of a company's own shares.

Q Thinking on Merger Ratio Calculation Method

Various methods can be conceived of in calculating the valuation of a firm, which is required when calculating the merger ratio. The following are examples:

① Market Price

Market value of investment corporation

② NAV (Net Asset Value)

Definition of NAV (from ARES "Real Estate Securitization Handbook 2008-2009")

"Appraised value of real estate, etc. incorporated in investment corporation less liabilities such as loans"

Appraised value represents the valuation of assets at the current market price and is not an appraisal. However, it is difficult to grasp the current market price in actuality. There are various methods for calculating NAV, but a simplified method for calculating NAV using an appraisal, for example, is as follows:

Simplified NAV = Net assets [post dividend] + (Total appraised value - Total book value)

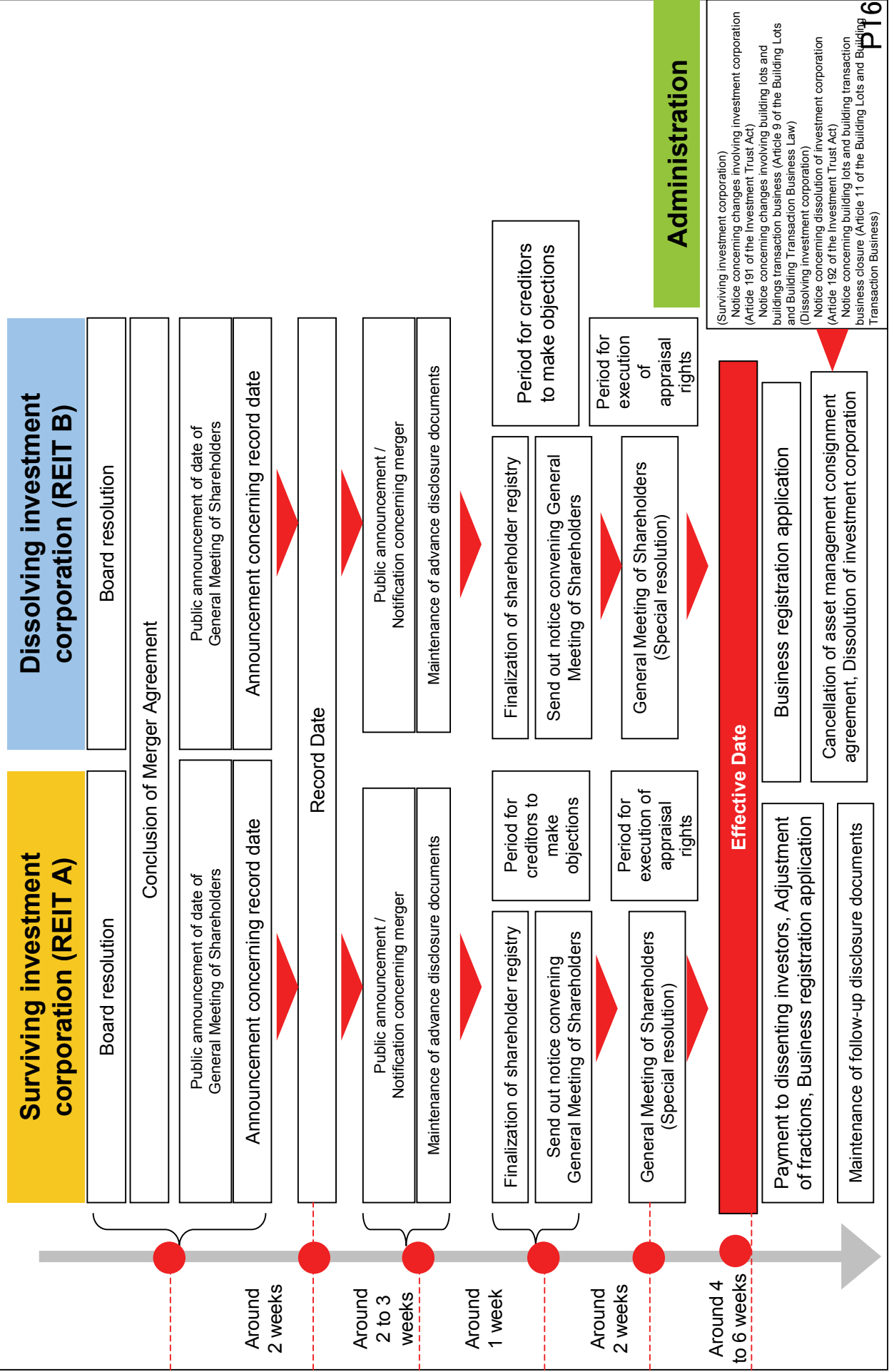
*Net assets [post dividend] = Net assets - Total distribution
(from Masters Training Program Textbook 203 [ARES])

Merger Simulation Model

Flow of merger (in the case of absorption-type merger)	Considerations debated by WG
The diagram illustrates the flow of merger in an absorption-type merger, showing the transition from a status quo to a post-merger state. Status quo: REIT A (yellow) and REIT B (blue) are separate entities. REIT A has a Lender, Investors A, and Asset Management Company A. REIT B has a Lender, Investors B, and Asset Management Company B. Arrows indicate the flow of funds and management. Absorption-type merger: A red arrow labeled "Absorption-type merger" points from the Status quo to the Merger stage. Merger: REIT A is being absorbed into REIT B. The Lender and Investors A are shown, but the Asset Management Company A is being transferred to REIT B's management company. A red arrow labeled "Transfer business, etc." points from the Merger stage to the Post-merger stage. Post-merger: REIT A is fully integrated into REIT B. The Lender, Investors A, and Investors B are shown, but the Asset Management Company A is now part of Asset Management Company B. The final state is labeled "Post-merger".	•Calculation of merger ratio.....Must be fair merger ratio, full explanation to investors essential •Fraction adjustment for merger ratio••Utilize delivered money due to merger (possibility of utilizing clarified by revision of Cabinet Office ordinance, etc.) •Debt finance.....coordination with lenders, etc. required •Fraction adjustment at time of delivery of investment units••Sell using ToSTNet trading •Dividends from dissolved investment corporation••Dividends for the final business year paid by using delivered money due to merger (possibility of utilizing clarified by revision of Cabinet Office ordinance, etc.) •Treatment of negative goodwill.....Expected to be deducted from conduit formula for the year in which it arises

Merger Simulation Model

Schedule



Changes in Major Shareholders (Sponsors) at Asset Management Companies

For J-REITs, there are neither case examples of mergers of investment corporations nor changes in asset management companies. There are examples of changes in major shareholders (sponsors) at asset management companies.

Date	Asset Management Company	Description
Dec. 2008	Creed REIT Advisors (Japan Office Advisors) *Trade name change as of December 22, 2008	<u>CREED Corporation → Ichigo Asset Trust</u> *All of the shares owned by main sponsor CREED Corporation and other shareholders were transferred to Ichigo Asset Trust.
Nov. 2008	Morimoto Asset Management	<u>Morimoto → Daiwa House Industry</u> *Daiwa House Industry acquired shares owned by main sponsor Morimoto and CapitalLand Japan, raising its stake from 10.0% to 73.5%. Morimoto's stake declined from 50.1% to 20.0%.
Oct. 2008	re-plus REIT Management (Mi-Casa Asset Management) *Trade name change as of October 24, 2008	<u>re-plus → AppleRingo Holdings (Oaktree)</u> *AppleRingo Holdings (Oaktree) launched a TOB for the investment corporation while simultaneously acquiring 35% of the shares in the asset management company from re-plus. After the bankruptcy of re-plus, Oaktree additionally acquired a 55% stake, and ultimately a 90% stake.
March 2008	Frontier REIT Management	<u>Japan Tobacco → Mitsui Fudosan</u> *Japan Tobacco transferred its 100% stake to Mitsui Fudosan.
Nov. 2007	LaSalle Investment Advisors	<u>Asset Managers → LaSalle Investment Management</u> *Asset Managers purchased all shares owned by other shareholders and transferred them entirely to LaSalle Investment Management. The investment corporation's trade name was changed from eASSET Investment Corporation to LaSalle Japan REIT Inc.

Example of Concern Regarding Protection of Dissenting Investors When Delisting Investment Corporation

- With regard to making a J-REIT open-ended, which allows redemption of investment units at the investor's request (converting to an open-ended structure violates the Tokyo Stock Exchange's delisting rules, resulting in delisting), a special resolution by the general meeting of stakeholders is required. Although an investor protection process exists, will the reason for converting to an open-ended structure, various procedures and other information disclosure sensitive to investor protection be implemented as items recognized as a reference for investors executing voting rights on reference material at the general meeting of stakeholders?
- When redeeming investment units to dissenting investors, redemption at a "fair price in light of assets owned" (Article 125, Section 1 of the Investment Trust and Investment Corporations Act) is required. How do you explain the grounds for such an amount to investors?

<Violates the criteria for delisting in Article 1218-2-11 of the security listing regulations of the Tokyo Stock Exchange>

Listing regulations (criteria for delisting)

Article 1218 (omitted)

2 A REIT will be delisted if any of the following items apply. The handling of each item shall be stipulated by the enforcement rules.

(omitted)

(1) With regard to a listed REIT, in the case where redemption of investment units at an investor's request or cancellation during the trust agreement period at beneficiary request is made possible by a change in the investment corporation's rules or the investment trust contract

(omitted)

3. J-REIT Governance

J-REITs Incur Administrative Penalties Due to Conflicts of Interest or Inadequate Internal Control

● J-REITs incur administrative penalties due to conflicts of interest or inadequate internal control

Company A (December 2008) 【Punishment: Business improvement order (Management company only)】

When a management company **acquired property from an interested party**, with regard to one property, **it failed to take measures** to satisfy standards specified in the investment policy, etc. concerning the acquisition of property using asbestos stipulated by the management company and caused **the investment corporation to incur unnecessary expenses**.

Also, for another property, the management company had the investment corporation acquire the property without considering that there would not be rental revenues during the period of renovations and additions to the structure.

Company B (October 2008) 【Punishment: Business improvement order (Regarding petition for commencement of civil rehabilitation proceedings: Investment corporation and management company; Regarding advisory from Securities and Exchange Surveillance Commission (November 2008): Management company only)】

With regard to the investment corporation filing a petition for commencement of civil rehabilitation proceedings, it became necessary to have the investment corporation and management company take all possible measures from the perspectives of preservation of the investment corporation's assets, prohibition of unreasonable expenditures, and investor protection.

Also, when the management company conducted capital increases through issuing investment units by way of third-party allocation, **despite the fact that one outside director opposed** at a meeting of the investment committee, which requires approval from all outside directors with voting rights, the management company processed this as having reached a decision by a majority vote and **took measures such as writing minutes that ran counter to the truth**.

Company C (September 2008) 【Punishment: Business improvement order (Management company only)】

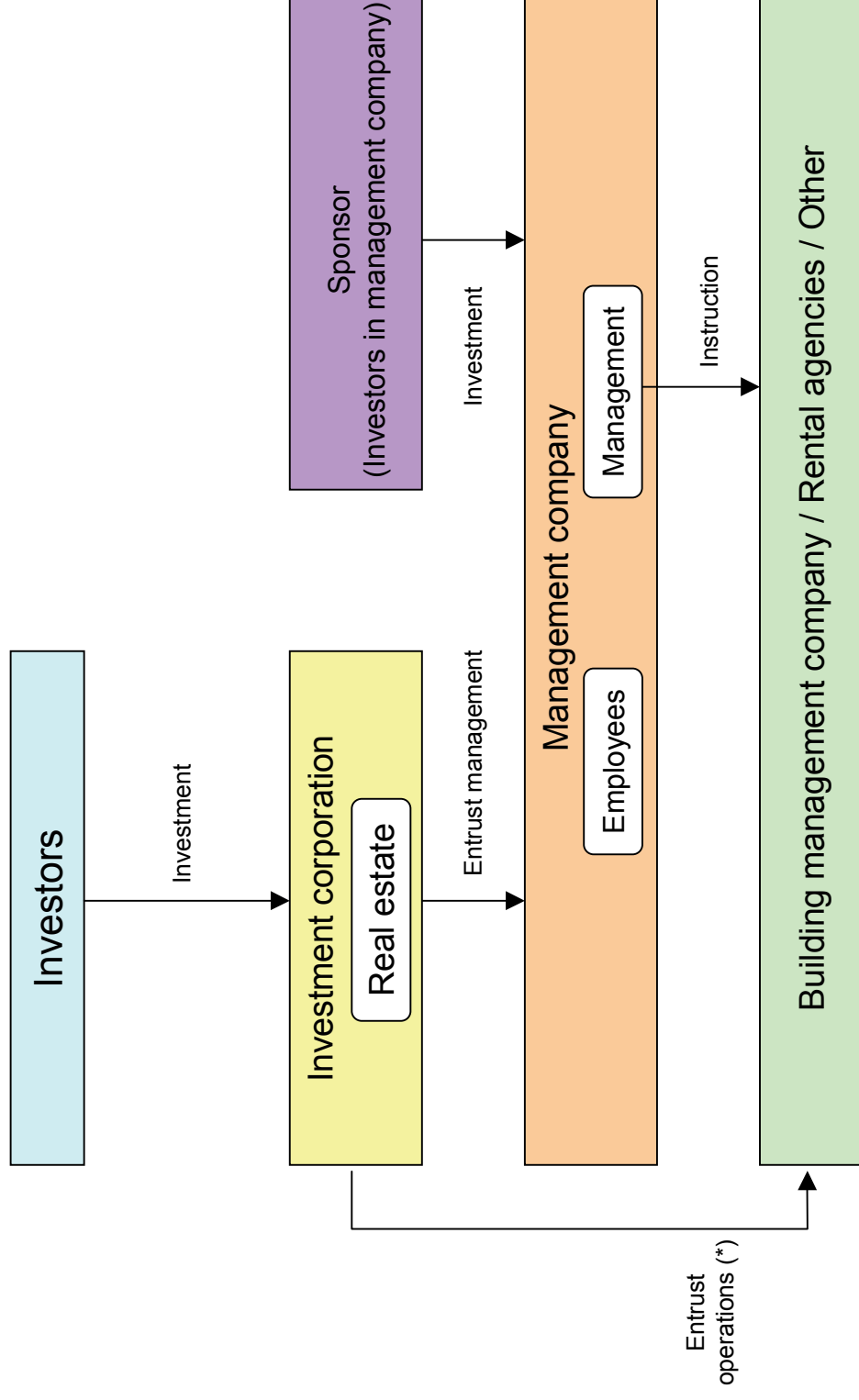
With regard to obtaining an appraisal at the time of acquiring an asset, the company took inappropriate actions that impaired the appraiser's independence, such as **asking the appraiser for an appraisal that was equal to or more than the asking price of the seller (an interested party of the management company)**. Furthermore, the company was engaged in **inappropriate processes in selecting appraisers**, such as asking for estimates from multiple appraisers until obtaining a price that was close to the asking price and selecting the appraiser that presented the highest price.

Company D (March 2008) 【Punishment: Business improvement order (both the investment corporation and management company)】

At the time of acquiring an asset, **the investment corporation shouldered costs that should have been born by the seller (an interested party of the management company) exceeding the appropriate price of the asset**. Also, the management company, which is supposed to adequately control the investment corporation's sales contracts, failed to do so in this case.

REIT Schemes in Different Countries

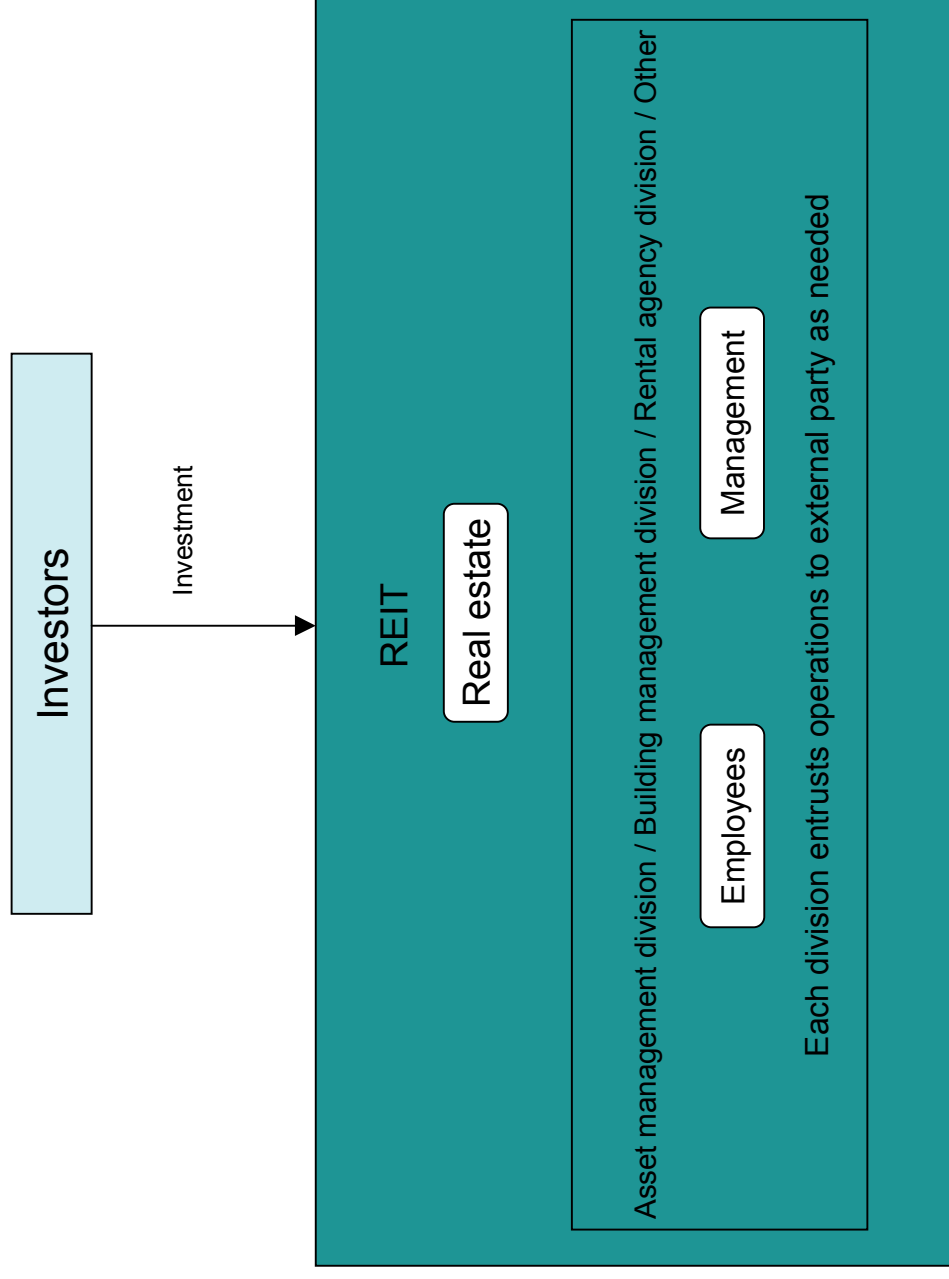
1. Japan (J-REITs) ~External management structure~



(*) However, there are cases where operations are re-commissioned via management companies.

REIT Schemes in Different Countries

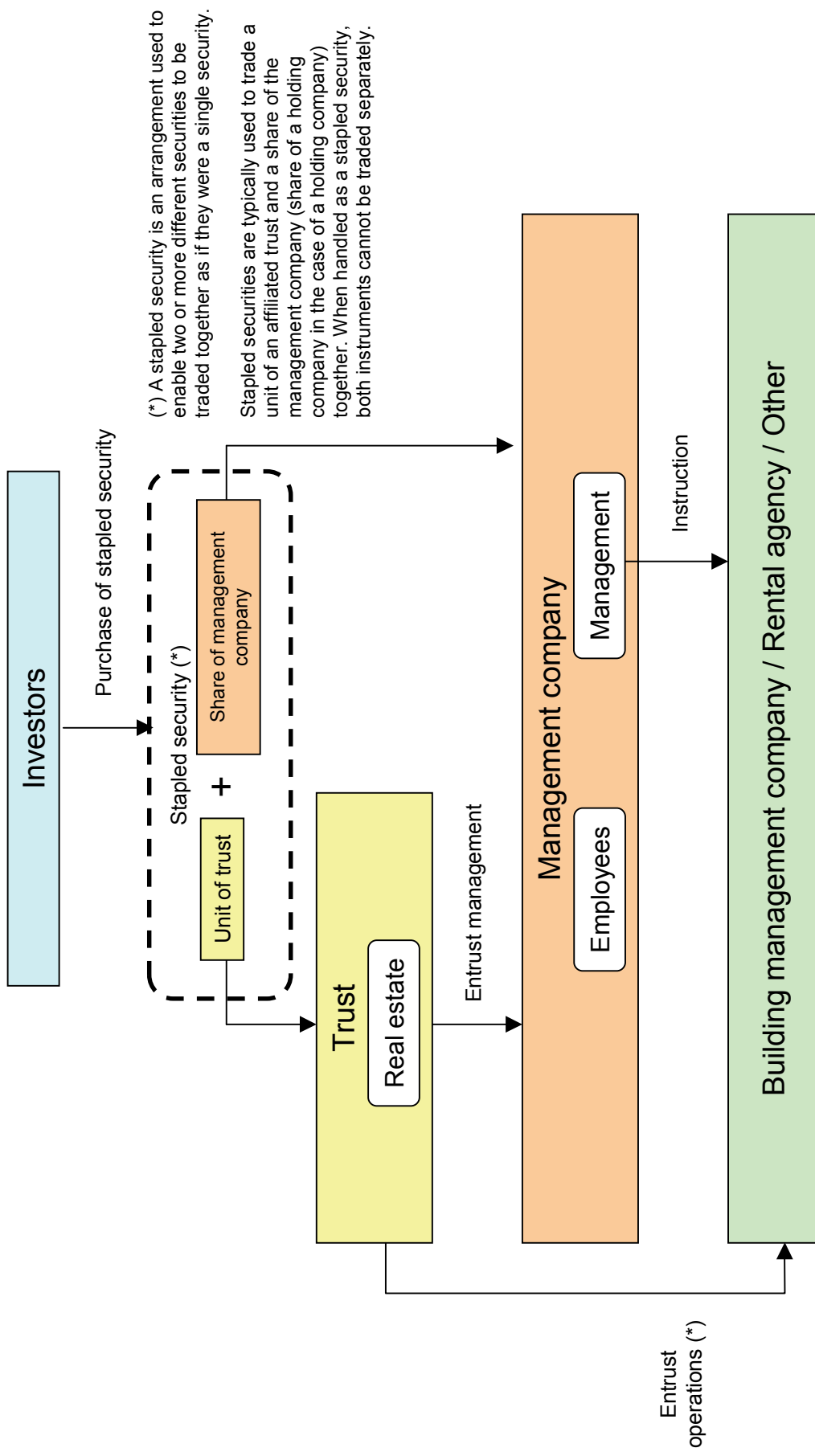
2. U.S. (U.S. REITs) ~Internal management structure~



Major Advantages and Disadvantages of Internal and External Management

	Advantages	Disadvantages
External Management	•Easier to gain cooperation from the sponsor since the management company is a subsidiary of the sponsor. (e.g., operation management capability, securing human resources, property supply function, credit capability, etc.) •Tax benefits (possible to include dividends in expenses because it is deemed as a conduit since it does not manage assets on its own)	•Possibility of conduct conflicting with investor interests since asset management is entrusted to an external management company •Since asset management is entrusted to an external management company, costs for establishing the investment corporation and ensuring the management company acts in accordance with investor interests (e.g., costs to monitor management company operations, incentive remuneration to management company) tend to lead to higher costs compared to internal management
Internal Management	•Conduct conflicting with investor interests less likely to occur since asset management is handled internally •Since asset management is handled internally, costs tend to be lower due to the absence of costs needed in the case of external management to ensure the management company takes action in accordance with investor interests	•Since asset management is handled internally and there is no external management company that is a subsidiary of the sponsor, it is hard to gain sponsor cooperation •Since asset management is handled on its own, there is risk that its attribute as conduit is lost and tax benefits cannot be obtained

3. Australia ~Stapled structure~



(*) However, there are cases where operations are re-commissioned via management companies.

Investor's Guide

“Australian Real Estate - A Legal Guide for Foreign Investors”

Blake Dawson, together with Jones Lang LaSalle, have published Australian Real Estate - A Legal Guide for Foreign Investors to assist investors in understanding the Australian commercial real estate market and the legal and taxation aspects of Australian real estate transactions (May 30, 2008).

http://www.blakedawson.com/Templates/Publications/x_publication_content_page.aspx?id=51705

Major Australian law firm Blake Dawson introduces laws and tax practices pertaining to the Australian real estate market to foreign investors.



Section that introduces stapled securities (P37)

External management and stapled securities

The idea of an external manager is deeply rooted in the legal structures used for real estate funds in Australia. In the classic structure, the real estate is held on trust for the investors by a trustee, and the business of managing the fund is carried on by a separate manager. More recently, for REITs and for some unlisted real estate funds such as wholesale real estate funds, the roles of the trustee and manager have been combined into a single responsible entity. This is still external management. The ownership and control of the manager is separate from ownership and control over the real estate assets.

In the classic structure, the trustee's role is passive. It holds the assets for unitholders and distributes the net income of the fund to them. The manager makes all the decisions concerning the operation of the fund and undertakes all negotiations, reporting and other activities to implement those decisions.

In the new structures using responsible entities, the responsible entity performs both the passive trustee role and also provides (as part of its own business, not the business of the trust) fund management services for the benefit of the unitholders. Its function is therefore still to act as an external manager.

However, the principle of external management has recently become qualified by the market practice of stapling securities. The shares in the manager and the units in the REIT are both listed and they are quoted and traded on the ASX as if they were a single security. They cannot be traded separately.

The stapled structure effectively converts the REIT into an internal management structure for investor purposes. This has developed in the market in recent years partly in response to investor demand for returns to the manager to be more closely aligned with investor interests and partly due to the vulnerability of managers in REIT takeovers.

The stapled structure is preferred in Australia to a simple corporate structure where a listed company holds the assets. This is because of the tax advantages where the assets are passively held in trust for unitholders and the active management is undertaken by a separate vehicle.

(Japanese translation of the underlined portion)

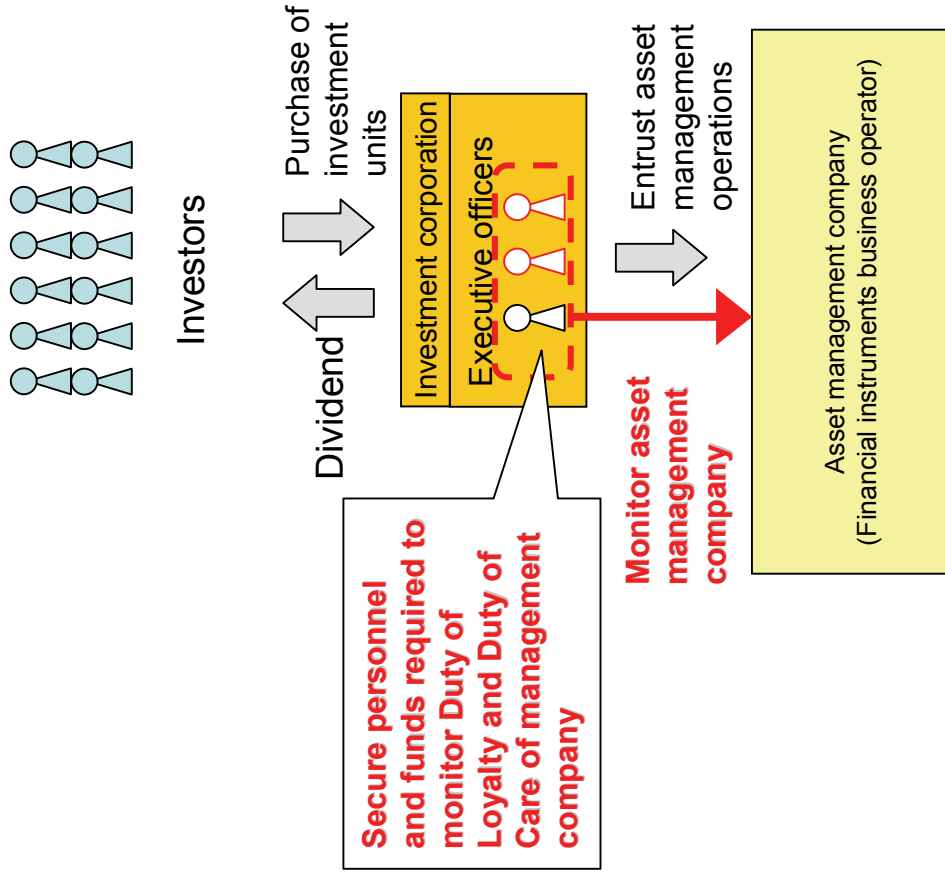
ステープルド型は、投資家にとりREITを実質的に内部運用体制へと変えるものである。このステープルド型は近年市場で発展してきたものであるが、資産運用会社の収益と投資家利益をより一致させるべきであるという投資家のニーズへ対応するとともに、REITの買収に際して資産運用会社の脆弱性に対処することが発展の理由として挙げられる。

Example of Strengthening Governance ①

○ Strengthening Investment Corporations' Monitoring of Duty of Loyalty, etc. of Management Companies

The major task of executive officers of investment corporations as representative of investors is to monitor whether management companies' handling of asset management based on their consignment contracts with investment corporations are fully performing their Duty of Loyalty, Duty of Care, etc. to the investment corporations.

Investment corporations may as well secure the personnel and funds required to monitor the Duty of Loyalty, Duty of Care, etc. of management companies so that their executive officers can fully and proactively perform their duties (increase board members, partial outsourcing of monitoring function as necessary, etc.).



Duty of Loyalty and Duty of Care of Asset Management Companies

• Financial Instruments and Exchange Act

(Duties to Right Holders)

Article 42 A Financial Instruments Business Operator, etc. **shall engage in Investment Management Business with loyalty** to Right Holders (meaning the persons prescribed in the following items for the Categories of Business listed in the respective items; hereafter, the same shall apply in this Subsection):

(i) Business of conducting the act specified in Article 2(8)(xii): the other party of the contract set forth in (a) or (b) of said item;

(ii) Business of conducting the act specified in Article 2(8)(xiv): the person who holds rights indicated on Securities listed in said item or other rights designated by a Cabinet Order; and

(iii) Business of conducting the act specified in Article 2(8)(xv): the person who holds rights listed in (a) to (c) of said item or other rights designated by a Cabinet Order as prescribed in said item.

2 A Financial Instruments Business Operator, etc. **shall engage in Investment Management Business with the due care of a prudent manager** for Right Holders.

Executive Officers of Investment Corporations

Q How many executive officers must an investment corporation have?

Stipulated by the Investment Trust and Investment Corporations Act, with the number stipulated by respective investment corporations in their bylaws
(Change to investment corporation bylaws (general meeting of shareholders resolution) is required when increasing the number to exceed the number of executive officers stipulated by the bylaws)

Investment Trust and Investment Corporations Act

Article 95 Investment corporations shall establish the following organizations:

- (i) One, two or more executive officers
- (ii) Supervisory officers totaling at least one more than the number of executive officers
- (ii) Board
- (iv) Accounting auditor

Example of investment corporation bylaw

(Number of executive officers and supervisory officers)

Article O **The number of executive officers shall be two or less**, and the number of supervisory officers shall be three or less. However, the number of supervisory officers must be at least one more than the number of executive officers.

Q Is it possible for investment corporations to outsource operations?

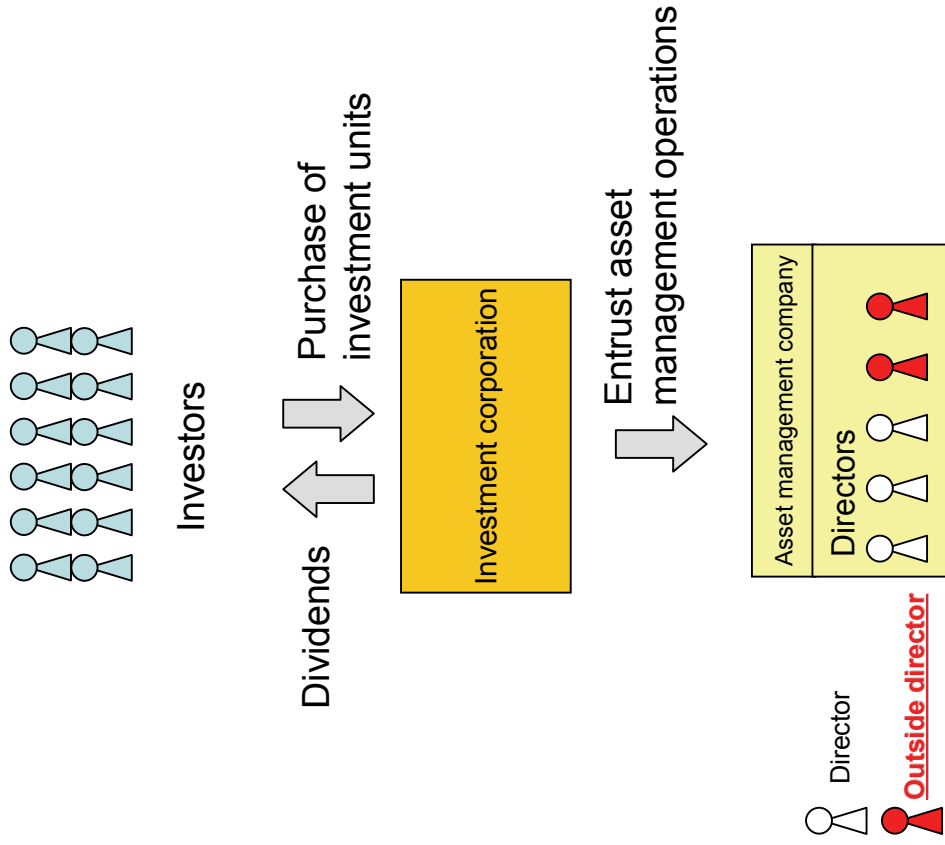
The Investment Trust and Investment Corporations Act requires outsourcing of the following operations. There are also cases where investment corporations entrust real estate management to real estate management companies.

- ① Outsourcing administrative matters (e.g., reparation and maintenance of the register of unitholders)
.....Article 117 of the Investment Trust and Investment Corporations Act
- ② Outsourcing asset management of its assets (e.g., acquisition or transfer of real estate)
..... Article 198 of the Investment Trust and Investment Corporations Act
- ③ Outsourcing custody of its assets (e.g., custody of vital documents such as registration certificates of real estate)
... Article 208 of the Investment Trust and Investment Corporations Act

Example of Strengthening Governance ②

○ Selection of Outside Directors at Management Companies

From the perspective of strengthening governance at a management company and heightening investor confidence, the investment corporation can consider selection of highly independent outside directors that can be expected to monitor execution of operations at a management company from the perspective of securing investor profit.



What is an outside director?

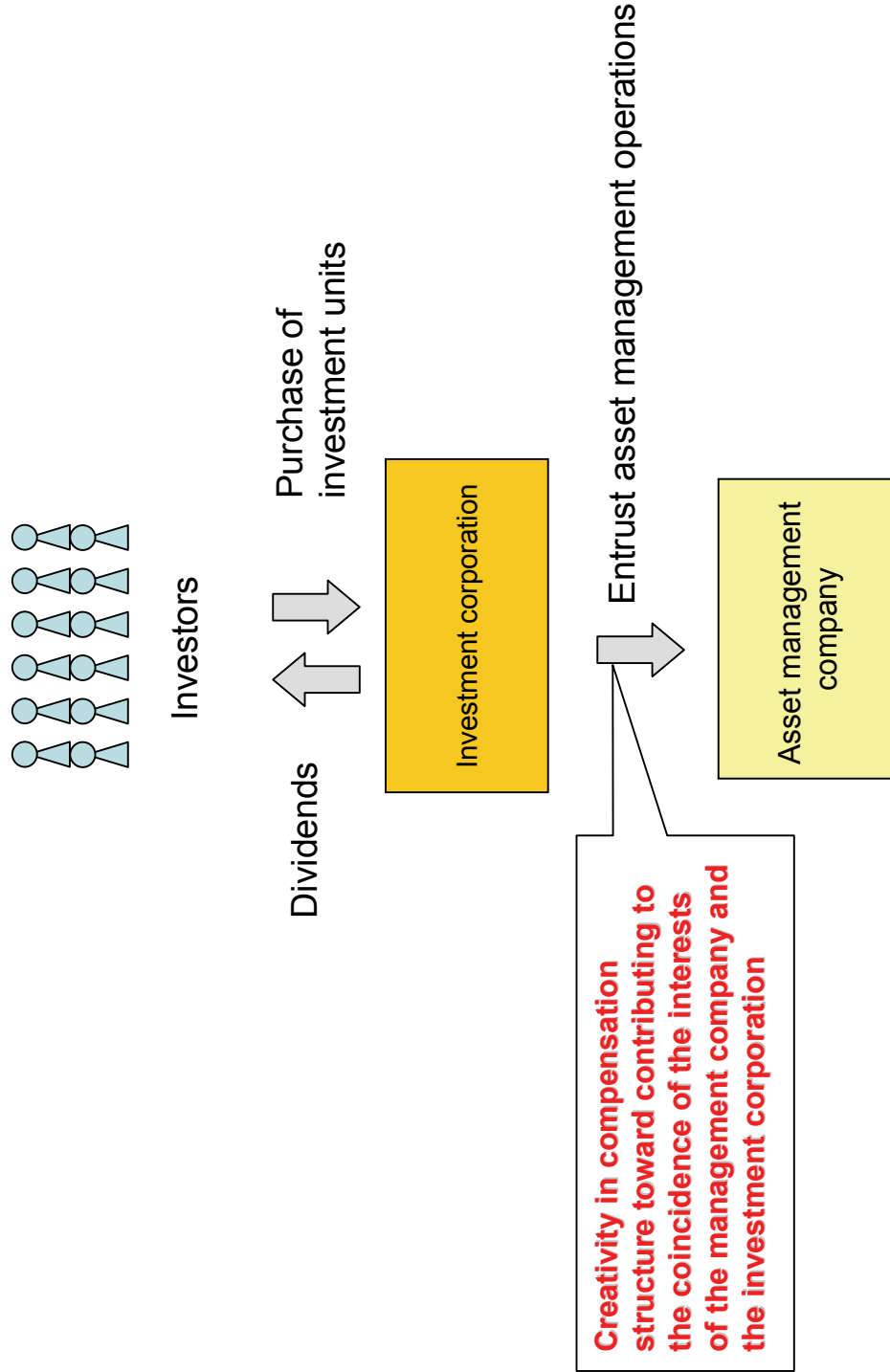
The Companies Act Article 2 (xv) defines the outside director as “a director of any Stock Company who is neither an Executive Director nor an executive officer, nor an employee, including a manager, of such Stock Company or any of its Subsidiaries, and who has neither served in the past as an executive director nor executive officer, nor as an employee, including a manager, of such Stock Company or any of its Subsidiaries,” thus demanding the role of making management decisions from an objective standpoint of not executing operations.

Outside directors are often introduced for the purpose of strengthening supervisory activities of the Board of Directors amid calls for companies to strengthen the separation of the execution and supervision of management.

Example of Strengthening Governance ③

○ Further Creativity in Compensation Structure of Management Companies

Even more creativity can be considered regarding the compensation structure at a management company toward contributing to the coincidence of the interests of the management company and the investment corporation.



Example of Management Fee ①

Management Fee Case Example 1

Management fee = Basic Fee 1 + Basic Fee 2

Type of Fee	Calculation Method and Timing of Payment
Basic Fee 1	Total assets multiplied by 0.15% (fractions of less than one yen omitted) shall be the Basic Fee 1. "Total assets" refers to the total assets indicated on the Balance Sheet (limited to that approved by Article 131 Section 1 of the Investment Trust and Investment Corporations Act) for the investment corporation's fiscal term immediately prior to the first day of the applicable business period. The payment date of the Basic Fee 1 shall be within the applicable business period.
Basic Fee 2	Distributable amount multiplied by 3.0% (fractions of less than one yen omitted) calculated each fiscal term shall be the Basic Fee 2. When there is a loss carried forward in the net income before taxes before the Basic Fee 2 is deducted in accordance with GAAP, "distributable amount" refers to the amount after such loss carried forward is covered. The payment date of the Basic Fee 2 shall be within a month after board approval of financial documents, etc. (refers to financial documents, etc. stipulated by Article 129 of the Investment Trust and Investment Corporations Act) concerning the applicable business period.

Management Fee Case Example 2

Management fee = Basic Fee 1 + Basic Fee 2

Type of Fee	Calculation Method and Timing of Payment
Basic Fee 1	Amount equivalent to 2.5% (fractions of less than one yen omitted) of rent, common expenses, parking fees, auxiliary income, facility rental fees, facility installation fees, delay damages, cancellation fees or similar charges in accordance with the cancellation of rental agreements and other profit arising out of the rental of the real estate under management (including beneficiary interests in trust acquired by the investment corporation and other assets backed by real estate; hereafter, "real estate" in this article) calculated every settlement date (however, this excludes profit from the sale of real estate and other assets under management; hereafter, "rent revenue" in this section). Based on the fiscal management plan the company entrusted with asset management submits to the investment corporation at the beginning of every year in line with the asset management consentment contract, the amount equivalent to 2.5% of rent revenue for the preceding three months will be paid on the last day of March, June, September, and December each year (the business day immediately prior when such date is a bank holiday) and the excess and deficiency will be balanced upon approval of accounts without delay.
Basic Fee 2	Amount equivalent to 3% (fractions of less than one yen omitted; however, negative values deemed as 0 yen) of net income before taxes before the Basic Fee 2 calculated every settlement date is deducted (however, when there is a loss carried forward, the amount after covering all such) and shall be paid upon approval of accounts without delay. If the pay corresponds to a period short of an accounting period, the pay shall be adjusted per diem.

*Management fees are indicated on "investment corporation rules" posted on each investment corporation's website.

Example of Management Fee ②

Management Fee Case Example 3

Management fee = Basic Fee 1 + Basic Fee 2 + Incentive fee

Type of Fee	Calculation Method and Timing of Payment
Basic Fee 1	Total of amounts obtained by the following calculation formula according to the total appraised value of managed assets as of the end of the previous business period. Here, the total appraised value of managed assets refers to the total of the appraised values of respective real estate properties (real estate that is the trust asset in the case of beneficiary interest in real estate). 【Calculation Formula】 • Portion whose total appraised value of managed assets of 200 billion yen or less multiplied by 0.150% • Portion whose total appraised value of managed assets exceeds 200 billion yen multiplied by 0.125% Fee for the applicable period shall be paid by the settlement period of the applicable business period.
Basic Fee 2	Total of amounts obtained by the following calculation formula according to recurring cash flow during the applicable business period. Here, recurring cash flow refers to depreciation costs and the amortization of deferred assets added to the recurring profits / losses and excluding profits / losses on sales and appraisal of specified assets (excluding those booked under extraordinary income and expenses) (hereafter "CF"). When calculating the Basic Fee 2, the CF before deduction of the Basic Fee 1, the Basic Fee 2 and the Incentive fee stipulated below shall serve as the criteria. 【Calculation Formula】 • Portion whose CF is 5 billion yen or less multiplied by 6.0% • Portion whose CF exceeds 5 billion yen multiplied by 5.0% Fee shall be paid within two months of the settlement period pertaining to the applicable business period.
Incentive fee	Amount obtained by the following calculation formula according to the investment unit price (closing price) on the Tokyo Stock Exchange during the applicable business period. However, the following calculation formula shall be promptly reviewed if the investment corporation merges or splits investment units. 【Calculation Formula】 • (Average closing price of investment unit during applicable business period — Highest price among the average closing prices of respective business periods up until the previous business period) X Number of outstanding investment units as of the end of the previous business period X 0.4% The average closing price of investment unit shall be calculated by totaling the investment unit price (closing price) on each business day of the applicable business period and dividing it by the number of business days. Business days without closing prices shall be excluded from the calculation. If the average closing price of the investment unit during the applicable business period does not exceed the highest price among the average closing prices of respective business periods up until the previous business period, the fee shall be 0 yen. Fee shall be paid within two months of the settlement period pertaining to the applicable business period.

*Management fees are indicated on "investment corporation rules" posted on each investment corporation's website

4. Financing for J-REITs

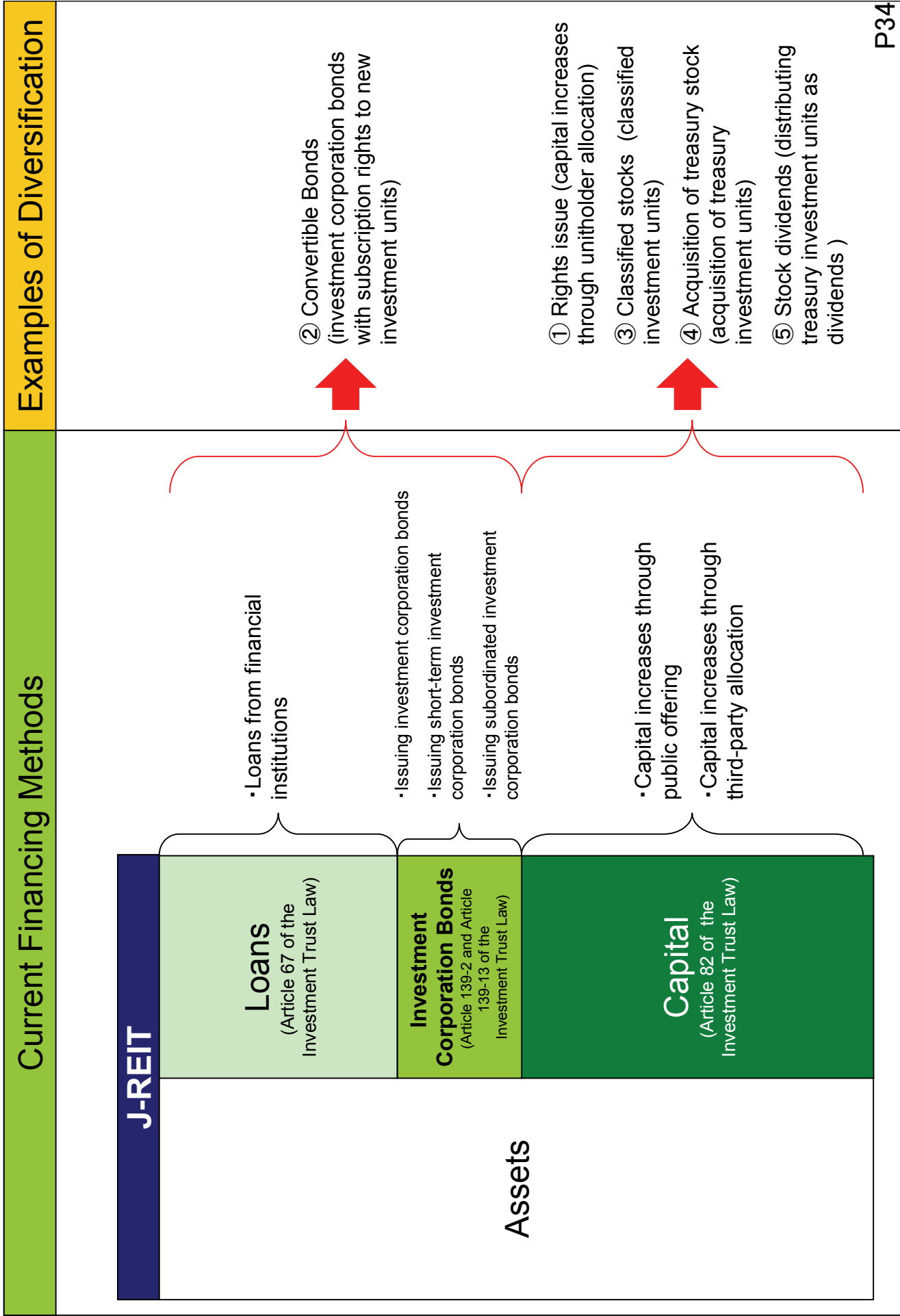
Gearing Regulations for REITs in Major Countries

Gearing Regulations for REITs in Major Countries

U.S.A.	None
Australia	None (only undercapitalization rules)
Hong Kong	45% of asset value
Singapore	35% of real estate asset value (possible up to 60% by acquisition of ratings and disclosure)
France	None (only undercapitalization rules)
U.K.	Interest coverage test (taxable income before interest and financial expense deductions / interest paid > 1.25)
Germany	45% of value of fixed assets (IAS40)
Belgium	65% of total assets

*By Baker and McKenzie GJB/Tokyo Aoyama Aoki Koma Law Office

Diversification of Financing Methods



Capital Increases through Third-party Allocation

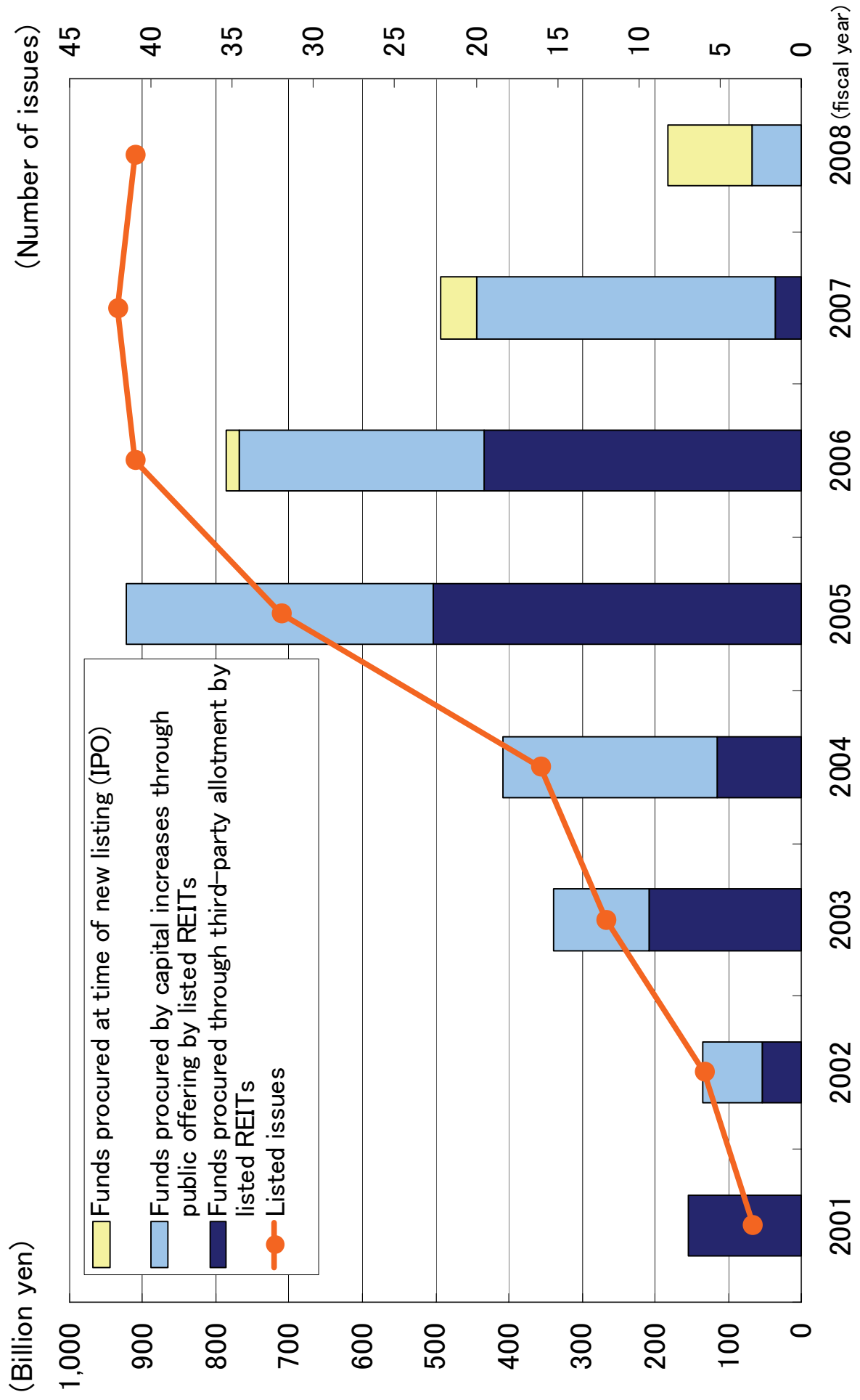
○ Capital Increases through Third-party Allocation in the Past Year

With regard to capital increases through third-party allocation that were undertaken in the past year, there were some cases where dividends decreased by 30% to 40%.

Press Release	Investment Corporation Name	Dividend Forecasts		Volatility	Procured Amount	Use of Funds
		Before Capital Increase	After Capital Increase			
April 2008	Company A	14,954yen →	10,050yen	▲ 32.8%	5.1bn yen	Loan repayment, property acquisition
May 2008	Company B	14,706yen →	14,232yen	▲ 3.2%	60.0bn yen	Loan repayment, redemption of investment corporation bonds
Aug. 2008	Company C	10,321yen →	5,766yen	▲ 44.1%	12.3bn yen	Loan repayment, property acquisition
Sep. 2008	Company D	14,117yen →	13,500yen	▲ 4.4%	14.7bn yen	Property acquisition
Sep. 2008	Company E	20,334yen →	20,500yen	0.8%	17.6bn yen	Loan repayment (However, dividend forecasts increased since the revenue from property recently acquired is reflected.)
Jan. 2009	Company F	22,027yen →	18,862yen	▲ 14.4%	1.5bn yen	Loan repayment
Mar. 2009	Company G	5,200yen →	4,200yen	▲ 19.2%	2.0bn yen	Loan repayment

*Compiled based on press releases of companies.

Equity Procurement by J-REITs



* As of March 31, 2009 (by Daiwa Institute of Research Ltd. based on public data from investment corporations)

① Rights Issue (Capital Increases through Unitholder Allocation)

○ What is rights issue?

• Issuance of new investment units conducted by investment corporations through the granting of rights to receive investment units to all unitholders listed in the register of unitholders on a certain record date.
(Unitholders decide whether to respond to the offer. Therefore, the fund procurement amount varies according to the proportion of unitholders who respond to the offer. Unitholders who do not respond to the offer lose these rights.)

<Interpretation of capital increases through unitholder allocation>

The answer by the FSA regarding how to interpret capital increases through unitholder allocation in the regulatory reform requests (Cabinet Office) received on October 2008:
"It is not necessarily against the law for an investment corporation to allocate investment units to existing unitholders at a **fair value**."

○ Advantages

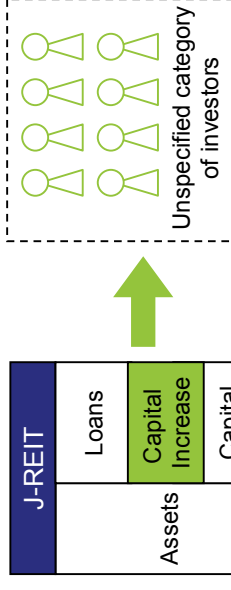
- Since all unitholders are able to acquire rights, it is different from a capital increase through third-party allocation in that there is no discrimination, etc. and all unitholders receive the opportunity to participate.
- Since this offer made to all unitholders is cheaper compared to market prices, unitholders find it easier to respond and therefore, it becomes possible to procure equity during periods when investment unit prices are low.

○ Points of caution from the viewpoint of protecting investors

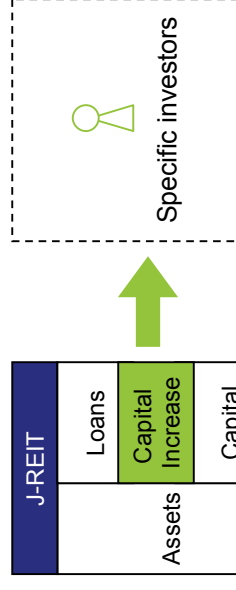
- Since capital increases through unitholder allocation represent a request for capital to existing unitholders who had not originally wished to increase their purchase, REITs generally increase capital by issuing at discounted prices compared to market prices, in order to motivate existing unitholders to invest, etc. There may be unitholders who lack the funds and do not agree to additional investment and who end up losing the rights, thereby choosing to sell their investment units in order to avoid a decrease in distribution per investment unit (dilution). In addition, the amount of procured funds can vary in accordance with the proportion of investors losing their rights, so that care must be taken regarding how the funds are used.

Diagram

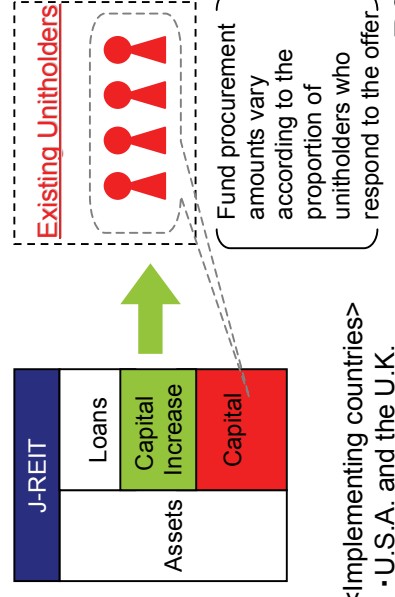
<Capital increases through public offering>



<Capital increases through third-party allocation>



<Capital increases through unitholder allocation>



<Implementing countries>
• U.S.A. and the U.K.

① Rights Issue (Capital Increases through Unitholder Allocation)

○ Major Cases of Implementation in Foreign Countries (Rights issue)

Nation	REIT	Period	Amount	Discount Rate of Issue Price
Australia	GPT Group	Announced 2008/10/23	About 79.3 bn yen	-48% (compared to closing price on Oct. 21)
	Goodman Group	Announced 2008/10/29	About 44.3 bn yen	-29.7% (compared to closing price on Oct. 28)
	Mirvac Group	Announced 2008/11/5	About 26.1 bn yen	-37.5% (compared to closing price on Nov. 4)
	ING Office Fund	Announced 2008/12/8	About 15.3 bn yen	-22% (compared to closing price on Dec. 2)
U. K.	Workspace Group	Announced 2009/1/27	About 13.1 bn yen	-69.2% (compared to closing price on Jan. 26)
	Hammerson	Announced 2009/2/9	About 87.6 bn yen	-62.2% (compared to closing price on Feb. 6)
	British Land	Announced 2009/2/12	About 110.0 bn yen	-53% (compared to closing price on Feb. 11)
	Land Securities	Announced 2009/2/19	About 113.4 bn yen	-51% (compared to closing price on Feb. 18)

*Compiled based on press releases, etc. of REITs. Based on the assumption that 1 GBP = 150 yen and 1 AUD = 61 yen.

② Convertible Bonds (Investment Corporation Bonds with Subscription Rights to New Investment Units)

○ What are investment corporation bonds with subscription rights to new investment units?

• Investment Corporation Bonds with Subscription Rights to New Investment Units
They are first issued as investment corporation bonds, and if the buyer makes a request within a certain set period, then he/she can convert those bonds into investment units of the investment corporation at a price (conversion price) agreed upon at the time those bonds were issued.

○ Advantages

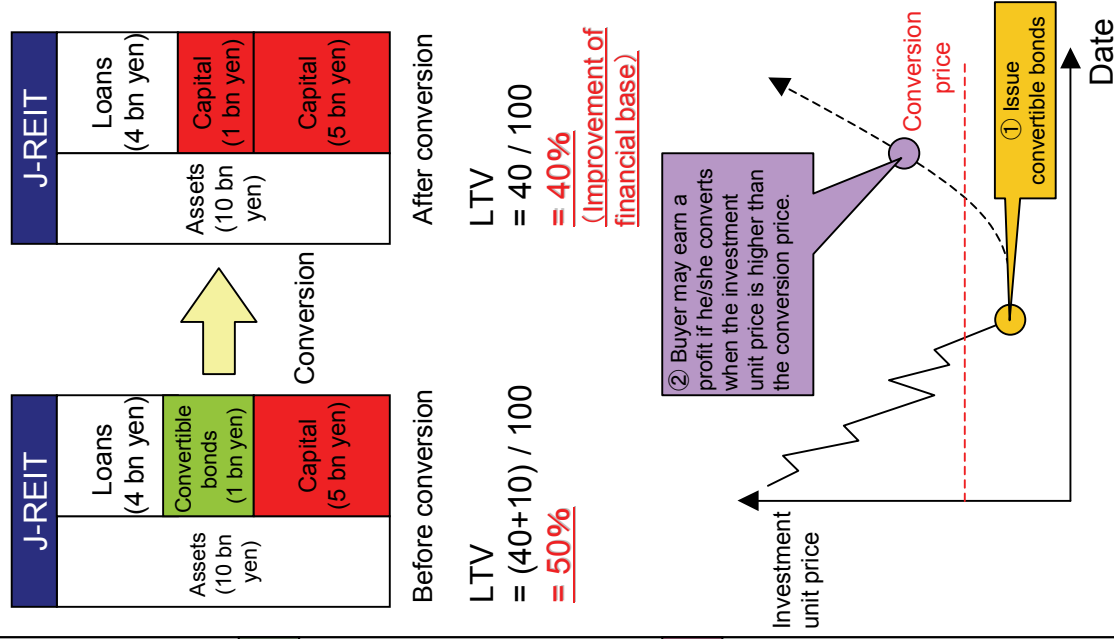
<In the case where convertible bonds are issued when investment unit prices are low>

- When prices of investment units underestimated in the market are recovering to their net asset values and the conversion rights are exercised, then LTV can be reduced.
- Capital sources such as strategic investors might be more inclined to buy convertible bonds in anticipation of the advantages that they could execute conversion rights in a process of rising investment unit prices
- Such capital sources would help decelerate the speed of dilution, caused by the conversion into investment units, throughout the lives of the convertible bonds.

○ Points of caution from the viewpoint of protecting investors

- There is a possibility that, depending on how the conversion prices of the convertible bonds are set, a significant level of dilution would be caused through their conversion into a huge amount of investment units. Dilution might be further accelerated if the conversion prices were subject to some unlimited moving strike clauses.
- Furthermore, downward pressure on investment unit prices may arise if trade practices are employed in which investment units are sold while at the same time conversion rights are executed (a decrease of market prices as a result of short-selling large volumes, etc. and conversion prices are then corrected according to market prices; after the price correction the conversion right is exercised, only to be followed by another round of selling.)
- On the other hand, no financial improvement – such as improvements in LTV – anticipated initially might be achieved if investment unit prices would not rise after the issuance and the convertible bonds were not converted into common stocks (investment units) despite the arrival of conversion deadlines.
- Therefore, we believe that prudent investigations should be made as to the product characteristics of convertible bonds and other factors, such as fully securing governance and the need for system design for investor protection.

Diagram

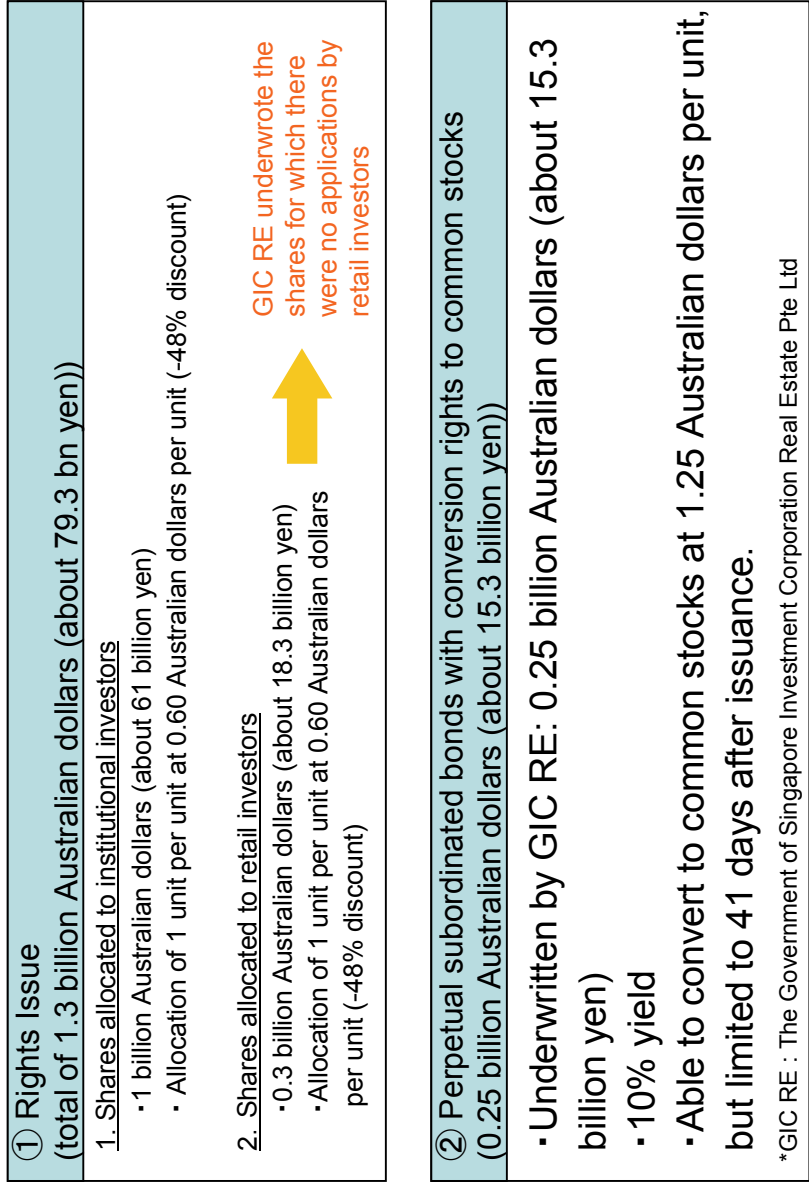


<Implementing countries>
 • U.S.A. and Australia

○ Cases of Implementation in Foreign Countries (Convertible bonds)

<Australia: The GPT Group> completed on Nov. 28, 2008

- The convertible bonds were used to repay existing debts. Furthermore, the company combined capital increases by way of a shareholder allocation of stocks and an issuance of perpetual subordinated bonds with conversion rights to common stocks in an effort to reconstruct its financial structure, and was thus able to procure funds that totaled 1.55 billion Australian dollars (about 94.6 billion yen).
- As a result, **its LTV decreased from about 47% to about 42%**.



③ Classified Stocks (Classified Investment Units)

What are classified investment units?

• Investment units whose content varies from that of common investment units in terms of dividend rights. (Preferred investment units: a type of classified investment unit and an investment unit for which a right to receive dividends and distribution of residual assets is granted at a higher priority than unitholders of common investment units.)

For example, the Corporate Law stipulates classified stocks as the following:

- ① Distribution of retained earnings
- ② Distribution of residual assets
- ③ Resolution rights
- ④ Restriction on transfers
- ⑤ Put options for shareholders
- ⑥ Shares subject to call by the company
- ⑦ Class share subject to class-wide call
- ⑧ Vetoes
- ⑨ Right to appoint executives

<Reference> For many of the preferred shares of ordinary companies, shareholders of common stocks may receive dividends and distributions of residual assets on a priority basis in place of not receiving resolution rights in shareholders' meetings (After distributing dividends to preferred shareholders at a dividend price higher than that decided at the time of issuance, and there still remains some retained earnings, those are distributed to common shareholders. After distributing residual assets to preferred shareholders at a price decided on at the time of issuance, and there still remains residual assets, those are distributed to common shareholders.). Furthermore, after a certain period of time, there are certain conditions attached. For example, investors can convert them into common stocks or demand buybacks from companies, or companies can repurchase them.

○ Advantages

• Even in the face of a difficult environment in obtaining financing, leaving the option open for various issuances of classified investment units to respond to various investor needs allows investment corporations to improve their finances, which in turn may lead to an increase in investor trust. For example, although there are no resolution rights attached, if unitholders of preferred investment units can receive dividends at a higher priority than unitholders of common investment units, this would make it easier for companies to obtain financing.

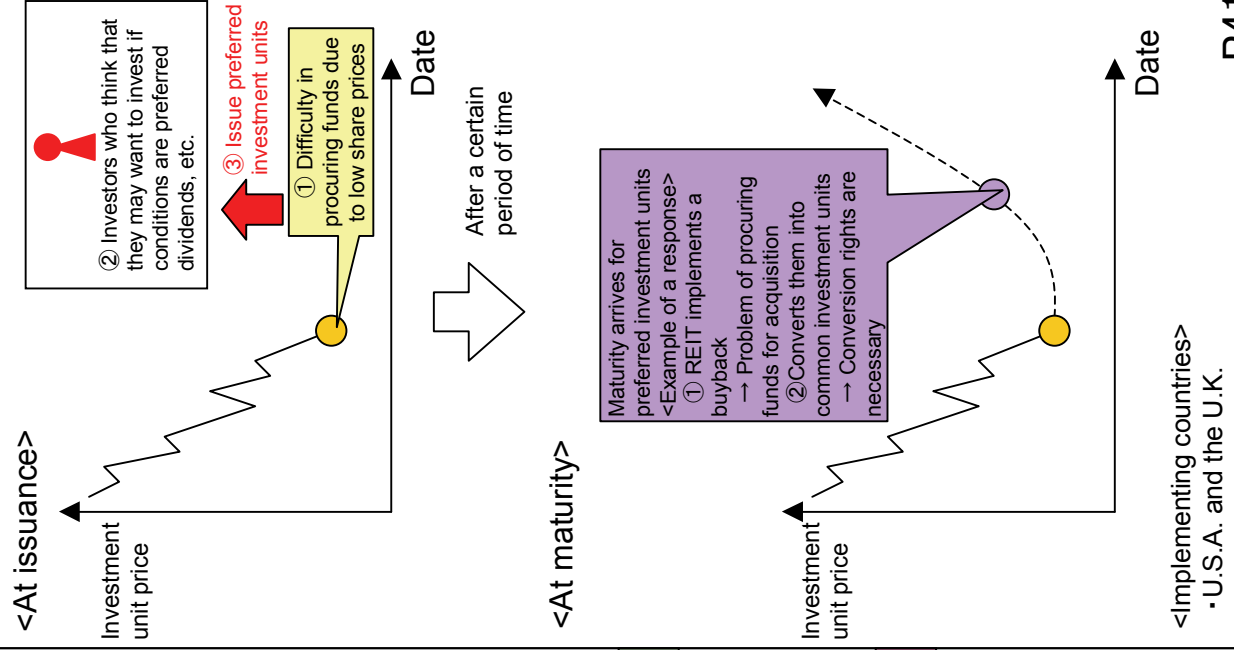
○ Points of caution from the viewpoint of protecting investors

• However, issuing preferred investment units, for example, might also bring about a negative impact, as they would make all outstanding investment units subordinate to them and have a major impact on existing investors. Redemption of such preferred investment units would also become a big problem.

• Furthermore, there is a possibility that, if existing investors of investment units become relatively subordinated, such a situation would not fit the simple product characteristics of J-REITs' investment units that they are financial products oriented to stable income gains.

• Therefore, it is necessary that discussions be made regarding the ideal classified stocks while considering factors securing governance and protecting investors.

Diagram



③ Classified Stocks (Classified Investment Units)

○ Cases of Implementation in Foreign Countries (Classified stocks)

<Past Capital Increases of U.S.-Listed REITs>

Year	Common Stocks		Preferred Stocks	
	Cases	Amount	Cases	Amount
2000	11	1.2 bn USD	31	1.7 bn USD
2001	58	4.2 bn USD	21	1.9 bn USD
2002	85	5.8 bn USD	25	2.0 bn USD
2003	82	5.5 bn USD	64	5.2 bn USD
2004	79	7.3 bn USD	61	5.9 bn USD
2005	71	8.5 bn USD	36	3.1 bn USD
2006	75	15.7 bn USD	39	4.2 bn USD
2007	56	11.9 bn USD	26	4.2 bn USD
2008	60	11.1 bn USD	9	1.2 bn USD

*Compiled using NAREIT's "Industry Capital Offerings – Summary Historical Offerings: April 2009"

<Examples>

REIT	Announced	Amount	Details
Alexandria Real Estate Equities	2008/3/18	0.25 bn USD	Preferred stocks with conversion rights (7.0% interest rate)
Entertainment Properties Trust	2008/3/26	0.09 bn USD	Preferred stocks with conversion rights (9.0% interest rate)

*Compiled based on press releases, etc. of REITs.

④ Acquisition of treasury stock (Acquisition of Treasury Investment Units)

○ What is an acquisition of treasury investment units?

- The acquisition of a investment corporation's own outstanding investment units.

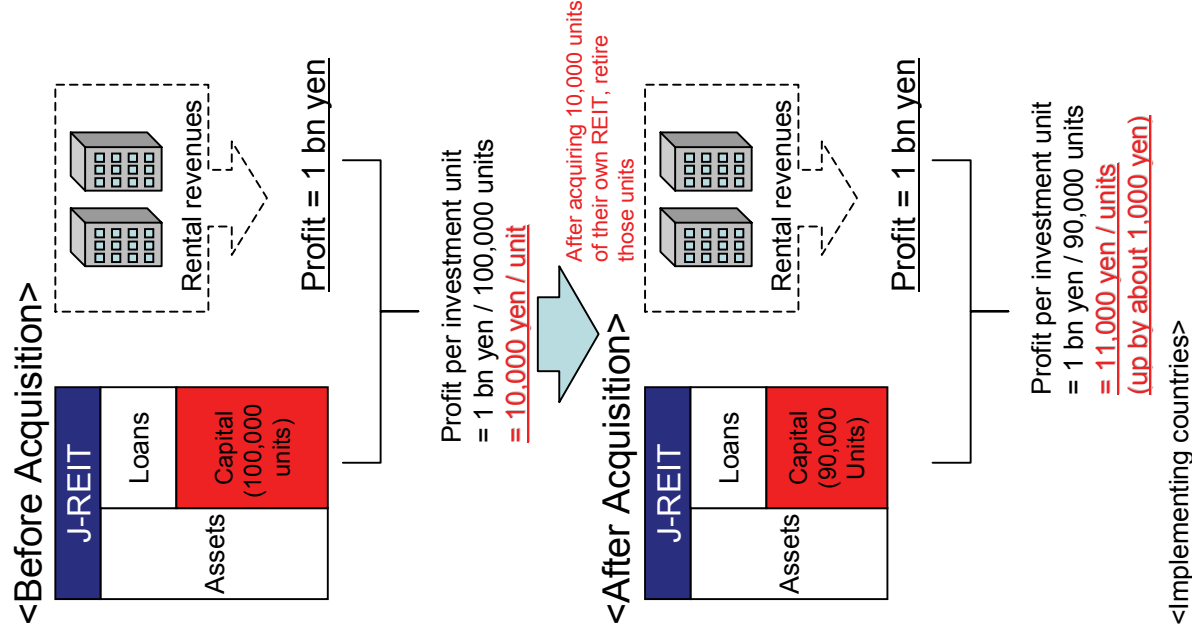
○ Advantages

- If a REIT acquires its own outstanding investment units, the number of investment units traded in the market will decrease. Therefore, the above would enable the effect of maintaining investment unit prices.
- Furthermore, in the case of acquiring its own outstanding investment units and retiring them (in the case of decreasing the number of outstanding investment units) and if the profit is the same, then implementing the above would have the effect of increasing profit per investment unit.
- Due to this, companies in countries implementing the above like the U.S. utilize this for their capital and dividend policies as a means to counter stagnant stock prices or to improve dilution that occurs after capital increases. It is also expected to possibly help improve investor trust.

○ Points of caution from the viewpoint of protecting investors

- Care must be taken with regard to the relationship with existing creditors when using the capital of the investment corporations as funds to acquire treasury investment units, and to fair and equal handling of all investors when using distributable profits to investors, since this would involve the repayment of capital invested.
- Since it is possible that the executives, employees, etc. of the same REIT may obtain internal information and sell or purchase the REIT's investment units before said information is announced, regulations on insider trading may need to be introduced.

Diagram



④ Acquisition of treasury stock (Acquisition of Treasury Investment Units)

O Cases of Implementation in Foreign Countries (Acquisition of treasury investment units)

<U.S.A.: Plum Creek>

- Plum Creek purchased about 3.3 million shares or about 2% of their outstanding shares, which totaled about 166 million shares at about 87 million dollars during the applicable fiscal term (Jan. 2009 ~ Mar. 2009). Rather than retiring them, it kept them as is (treasury stocks). As a result, Plum Creek's treasury stocks increased from 773 million dollars to 860 million dollars.

<U.S.A.: SL GREEN>

- On March 2007, SL Green announced that it would buy about 300 million dollars of its treasury stocks (equivalent to about 3.4% of its outstanding shares) by December 2008.
- Following this, it periodically acquired treasury stocks which resulted in a purchase of about 300 million dollars of its treasury stocks by December 2008. It is currently keeping them as treasury stocks.

⑤ Distributing Treasury Stocks as Dividends (Investment Unit Dividends)

○ What are investment unit dividends?

- The act of distributing investment units as dividends, rather than in cash.

<Example in the U.S.>

In the U.S., a new rule was enforced in December 2008 in relation to the dividend requirement of distributing 90% or more of taxable income as a conduit requirement in which REITs were permitted to distribute stock dividends according to investors' choices (although at least 10% of dividends must be conducted in cash).

(*A temporary legislation which shall be applied to dividends paid in the limited time frame of January 1, 2008 through December 31, 2009)

○ Advantages

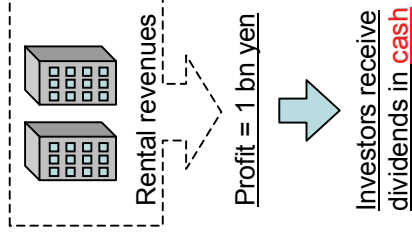
- In the U.S., even major blue-chip REITs paid out share dividends and it is pointed out that this measure has helped to control the outflow of cash on hand and to reduce refinancing risks without violating the conduit requirements.

○ Points of caution from the viewpoint of protecting investors

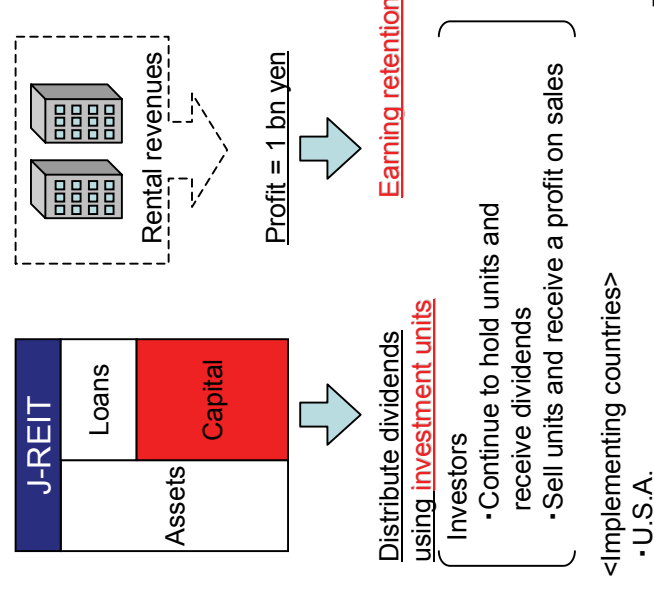
- Investment unit dividends are usually implemented during periods when investment unit prices are low as a result of refinancing risk, etc. Thus investors may be at a disadvantage when they want to liquidate stock dividends, since the market prices are low and selling them in the market would further lower the stock prices.

Diagram

<Ordinary Dividends>



<Investment Unit Dividends>



⑤ Distributing Treasury Stocks as Dividends (Investment Unit Dividends)

○ Cases of Implementation in Foreign Countries (Stock dividends)

<U.S.A.>

• In the U.S., a Guidance was officially released from the IRS (Internal Revenue Service) last December saying that a maximum of 90% of dividends can be paid using shares. Major REITs are now paying out part of their dividends in shares rather than in cash.

Vornado Realty Trust (Announced on January 14, 2009)

• Vornado paid share dividends in order to reduce its refinancing risk, etc.

In 2009, if it is able to maintain this policy, its plan is to raise retained earnings of 390 million dollars (about 39 billion yen).

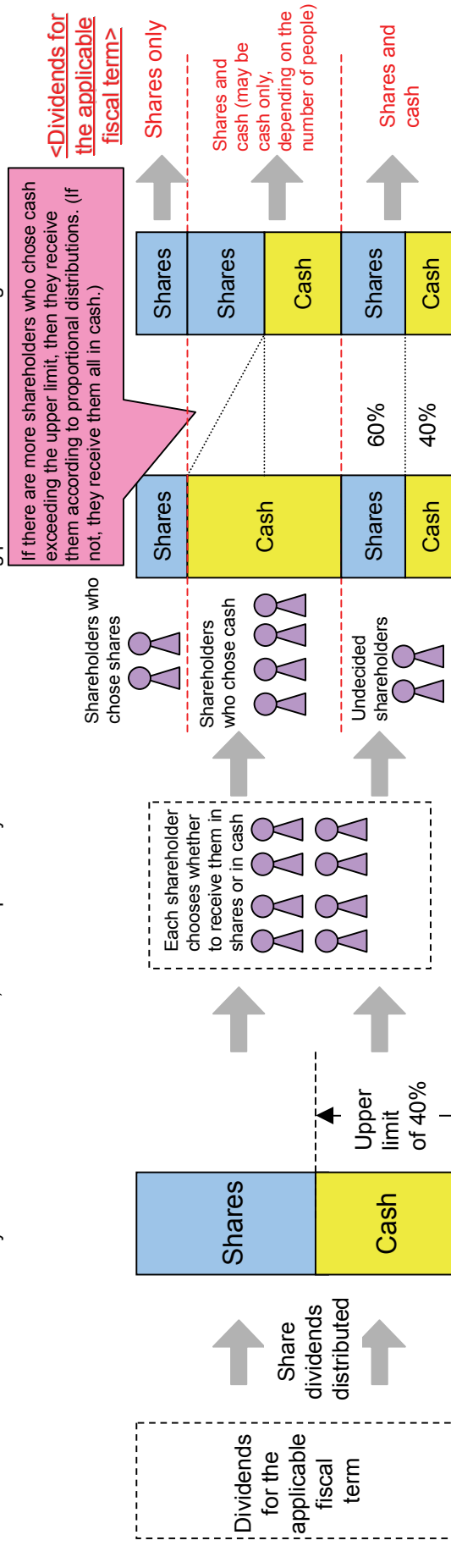
*Based on the assumption that 1 USD = 100 yen.

— Shareholders can choose between shares and cash when receiving dividends. However, the system allows a payout in cash of no more than 40% of dividends for the applicable fiscal term.

- ① Firstly, shareholders choose whether they would like to receive all of their dividends in cash or all of their dividends in common stocks.
- ② Shareholders who did not make a choice can receive 60% of their dividends in shares and 40% in cash.
- ③ For shareholders who chose to receive all their dividends in shares, they may receive all of their dividends for the applicable fiscal term in shares.
- ④ For shareholders who chose to receive all of their dividends in cash, the amount of cash they receive varies depending on the proportion of shareholders who chose to do likewise.

If there are many shareholders who chose likewise, then they receive cash in proportional distributions and the rest are paid in shares since the payment of dividends in cash is limited by up to 40% of the dividends for the applicable fiscal term.

If there are only a few who chose likewise, then the possibility of all of their dividends being paid out in cash becomes higher.



⑥ Establishment of Provisions Concerning Capital Decreases

○ What is a capital decrease?

- A capital decrease is when a company decreases its capital.
- If a company produces a loss in their financial results of a fiscal term, it can post it as a loss carried forward in the balance sheet and then cover the loss carried forward using the profit from the next fiscal term. However, if the profit from the next fiscal term is not sufficient to cover it, then the loss carried forwards remains until the fiscal term following the next, and so forth. If this is the case, there arises the concern that it would face difficulty in distributing profits until it is able to produce profits. In order to solve this problem, the method called capital decrease may be used to reverse capital and dispose the loss carried forward at once.
- There are cases when an ordinary company that conducts a capital decrease conducts a capital increase immediately afterwards since shareholders' equity also decreases.

○ Advantages

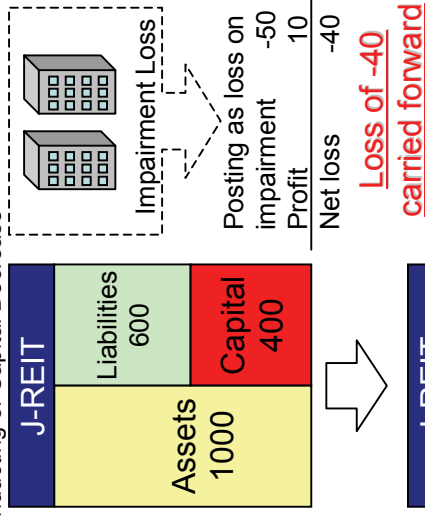
- Take for example a investment corporation whose assets amount to 100 billion yen and whose net income every fiscal term is 1 billion yen. If, due to the large drop in the prices of real estate owned, an impairment loss of 5 billion yen is incurred and the company produces a net loss of 4 billion yen, then 4 billion yen would be posted as loss carried forward. Three billion yen would then be posted as loss carried forward during the next fiscal term and the loss would be carried forward until after the fiscal term following the next.
- If a investment corporation has a loss carried forward, it may find it difficult to distribute profits as dividends. Furthermore, financial institutions who are lending to the investment corporation would be faced with the situation of having to review lending to a company with losses and may find difficulty in making the loan. In this regard, there was an opinion that a capital decrease was conducted to allow it to cover losses, and such an arrangement would also be effective in view of financing measures.

○ Points of caution from the viewpoint of protecting investors

- Since conducting a capital decrease would have a significant impact on investors as a result of a decrease in shareholders' equity and increase in LTV, etc., it is advisable that careful discussions are made regarding the decision-making process for conducting capital decreases (a resolution at a shareholders' meeting is necessary for joint stock companies).

Diagram

<Flow from the Incurring of Losses until the Conducting of Capital Decrease>



The loss carried forward is reduced by using profits from each fiscal term. However, excess profits are not produced until it disappears and so dividend payouts are made difficult.

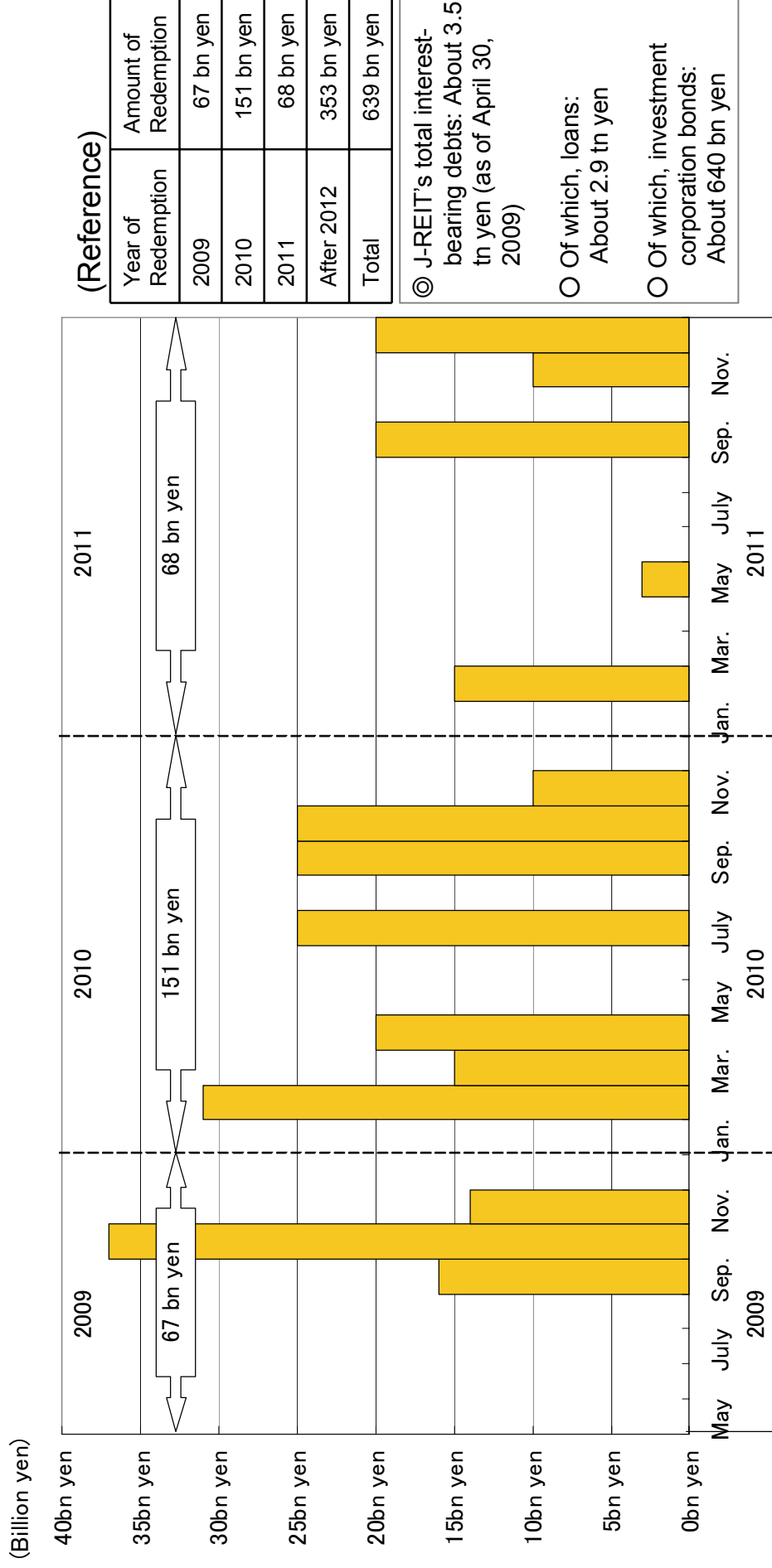
Implement a capital decrease of -40

If the loss carried forward disappears as a result of the capital decrease, then dividend payouts can be restarted earlier.

<Implementing countries>
• U.S.A. and the U.K.

Redemption of Investment Corporation Bonds by J-REITs

○ Redemption of Investment Corporation Bonds



*As of April 30, 2009 (by Daiwa Institute of Research Ltd. based on public data from investment corporations)

Subordinated Investment Corporation Bonds

O Subordinated Investment Corporation Bonds

Investment Corporation	Industrial & Infrastructure Fund Investment Corporation
Name of Issue	Industrial & Infrastructure Fund Investment Corporation First Unsecured Corporate Bonds (Subordinated corporate bonds exclusively for qualified institutional investors)
Recipient of Allotment	Mitsubishi Corporation
Total Issuing Amount	8,000 million yen
Date of Issuance	February 27, 2009

<Subordinated Investment Corporation Bonds>

- In the case that an investment corporation goes into liquidation or bankruptcy, the assets of the investment corporation are distributed to general creditors, but their repayment is normally lower in priority than that of ordinary investment corporation bonds. Firstly, repayment to general creditors is given priority, and if residual assets still remain, they are distributed to the holders of subordinated investment corporation bonds.
- Therefore, an ordinary company sets the interest rate for subordinated corporate bonds, whose risk is higher than that of ordinary corporate bonds, at a higher rate.
- Furthermore, repayment for loans made to the investment corporation by banks is given higher priority than to holders of subordinated investment corporation bonds. Some banks thus view subordinated investment corporation bonds as capital rather than as liabilities when conducting loan examinations. In that case, subordinated investment corporation bonds are not treated as interest-bearing debt when calculating the LTV (= Interest-bearing debt / Total assets). Some have pointed out that investment corporations are then able to suppress the LTV in comparison to the case of issuing normal investment corporation bonds, and as a result may receive loans more easily.

Qualification of Investment Corporation Bonds as Eligible Collateral

○ Qualified as Eligible Collateral by the Bank of Japan

- To be selected by the Bank of Japan (BOJ) as a collateral asset when the BOJ provides funds to a financial institution.
- The BOJ selects qualified collateral assets by placing priority on their trustworthiness and marketability.

<Press Release (Jan. 22, 2009)> Amendments to “Guidelines on Eligible Collateral” (excerpts):

“At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan decided, with a view to further facilitating the Bank’s money market operations, to accept **bonds issued by real estate investment corporations**, dematerialized commercial paper issued by real estate investment corporations, bills drawn by real estate investment corporations, commercial paper issued by real estate investment corporations, and loans on deeds to real estate investment corporations as eligible collateral for the Bank’s provision of credit and to add dematerialized commercial paper issued by real estate investment corporations and commercial paper issued by real estate investment corporations to the list of CP purchased with repurchase agreements.”

Collateral Category	Eligibility Standard
Bonds Issued by Real Estate Investment Corporations	Bonds issued by real estate investment corporations satisfying the following requirements: (1) Publicly-offered bonds issued by investment corporations (as defined in Article 2, Paragraph 12 of the Investment Trust and Investment Corporations Act, Act No. 198, 1951) which are deemed eligible in light of creditworthiness and other relevant factors, such as being rated AA or higher by an eligible rating agency. (When bonds are guaranteed by other companies, factors regarding the creditworthiness of the companies such as being rated A or higher would also be taken into account. The same criteria will be applied to all debt of real estate investment corporations.) (2) Principal investment objects of debtor investment corporations should be real estate, a leasehold of real estate, superficies of real estate, asset-backed securities backed by these assets or real estate-related assets which are deemed corresponding to these assets.
Dematerialized Commercial Paper Issued by Real Estate Investment Corporations Bills Drawn by Real Estate Investment Corporations Commercial Paper Issued by Real Estate Investment Corporations	Dematerialized commercial paper issued by real estate investment corporations, bills drawn by real estate investment corporations, and commercial paper issued by real estate investment corporations satisfying the following requirements: (1) Those deemed appropriate in light of creditworthiness of debtor investment corporations and other relevant factors. (2) Principal investment objects of debtor investment corporations should be real estate, a leasehold of real estate, superficies of real estate, asset-backed securities backed by these assets or real estate-related assets which are deemed corresponding to these assets. (3) Those with an original maturity of up to 1 year.

Outstanding collateral accepted by the BOJ: Real estate investment bonds = 4.3 billion yen (principal) as of April 30, 2009

Short-term Investment Corporation Bonds

○ Past Issuances of Short-term Investment Corporation Bonds

Investment Corporation	Period	Amount	Use of Funds
Nomura Real Estate Office Fund, Inc.	April 24, 2008 to June 6, 2008	20 bn yen	Property acquisition
	June 24, 2008 to Sep. 24, 2008	15 bn yen	Property acquisition
Japan Retail Fund Investment Corporation	Dec. 25, 2007 to Mar. 23, 2008	25 bn yen	Property acquisition
	Mar. 24, 2008 to June 23, 2008	25 bn yen	Redemption of existing short-term investment corporation bonds
	June 24, 2008 to Sep. 23, 2008	25 bn yen	Redemption of existing short-term investment corporation bonds
	Sep. 24, 2008 to Dec. 24, 2008	25 bn yen	Redemption of existing short-term investment corporation bonds

○ Investment Trust and Investment Corporations Act (Special Provisions Concerning Short-term Investment Corporation Bonds)

Article 139-12: Notwithstanding the provisions of Article 681 of the Corporate Law which is applied mutatis mutandis to Article 139-7, an investment corporation that has issued investment corporation bonds that meet any of the following conditions need not make an investment corporation bond register.

- (i) The amount of an investment corporation bond is no less than 100 million yen.
- (ii) A set period of **less than one year** is designated from the day that the total amount of the investment corporation bond is paid until the principal redemption date and there are no specifications on dividend payments.
- (iii) There are provisions that stipulate the payment date of interest as being the same date as the redemption date set forth in the previous item.
- (iv) Collateral is not posted pursuant to provisions under the Secured Bonds Trust Law.
- (2) Provisions under Articles 139-8 to 139-10 shall not apply to short-term investment corporation bonds.

(Issuance of Short-term Investment Corporation Bonds)

Article 139-13: Investment corporations shall not issue short-term investment corporation bonds except in the following cases:

- (i) When they meet all of the following conditions:
 - (a) **The purpose of the issuance is the procurement of funds necessary to acquire specified assets (limited to real estate and assets prescribed other Cabinet Orders) and other purposes set out under Cabinet Office Ordinance.**
 - (b) A limit is set as to the issuing amount in the bylaws.
 - (c) Other than those set out under (a) and (b), conditions that are stipulated by the Cabinet Office Ordinance in order to protect unitholders.
- (ii) In the case of procuring funds to redeem short-term investment corporation bonds (limited to cases prescribed by the Cabinet Office Ordinance).

○ Enforcement Order for the Investment Trust and Investment Corporations Act

(Conditions of Issuance of Short-term Investment Corporation Bonds)

Article 98-2: Assets set forth under Article 139-13, item (i) (a) of the Act and prescribed by Cabinet Order are the following:

- (i) Assets set forth under Article 3, items (iii) to (v).
- (ii) Trust beneficiary rights which only entrust assets set forth under the preceding item.
- (iii) If one party makes an investment in the other party so that it may conduct management of assets set forth under the preceding two items, and the other party manages the invested assets only for the purpose of investing in said assets, then the interests of investment in relation to an agreement that stipulates that profit arising from said management will be distributed.
- (iv) Preferred investment securities set forth under Article 2, paragraph 9 of the Law on Securitization of Assets issued by a special purpose company prescribed under Article 2, paragraph 3 of the Law on Securitization of Assets (limited to specified assets set forth under Article 2, paragraph 1 and that are set forth under items (i) and (ii)).

Short-term Investment Corporation Bonds

O Enforcement Ordinance of Investment Trust and Investment Corporations Act (Conditions of Issuance of Short-term Investment Corporation Bonds)

Article 192: Purposes prescribed by the Cabinet Office Ordinance stipulated under Article 139-13, item (i) (a) of the Act are the following:

- (i) **Procurement of funds necessary to acquire specified assets** (limited to assets set forth under all items in Article 98-2 of the Ordinance. The same shall apply for the next paragraph, item (ii).)
- (ii) **Procurement of funds necessary to repair the following real estate (limited to those that need urgent repairs as a result of accidents, natural disasters, etc.).**
 - A. Real estate owned by an investment corporation.
 - B. Real estate that are trust assets for trust beneficiary rights stipulated under provisions in Article 98-2, item (ii) of the Ordinance that are owned by the investment corporation
- (iii) **Procurement of funds necessary to refund deposits or guarantees to tenants of real estate set forth under (a) and (b) in the preceding item.**
- (iv) **Procurement of funds necessary for the issuance of investment securities or investment corporation bonds in the case of procuring funds until the time of issuance.**

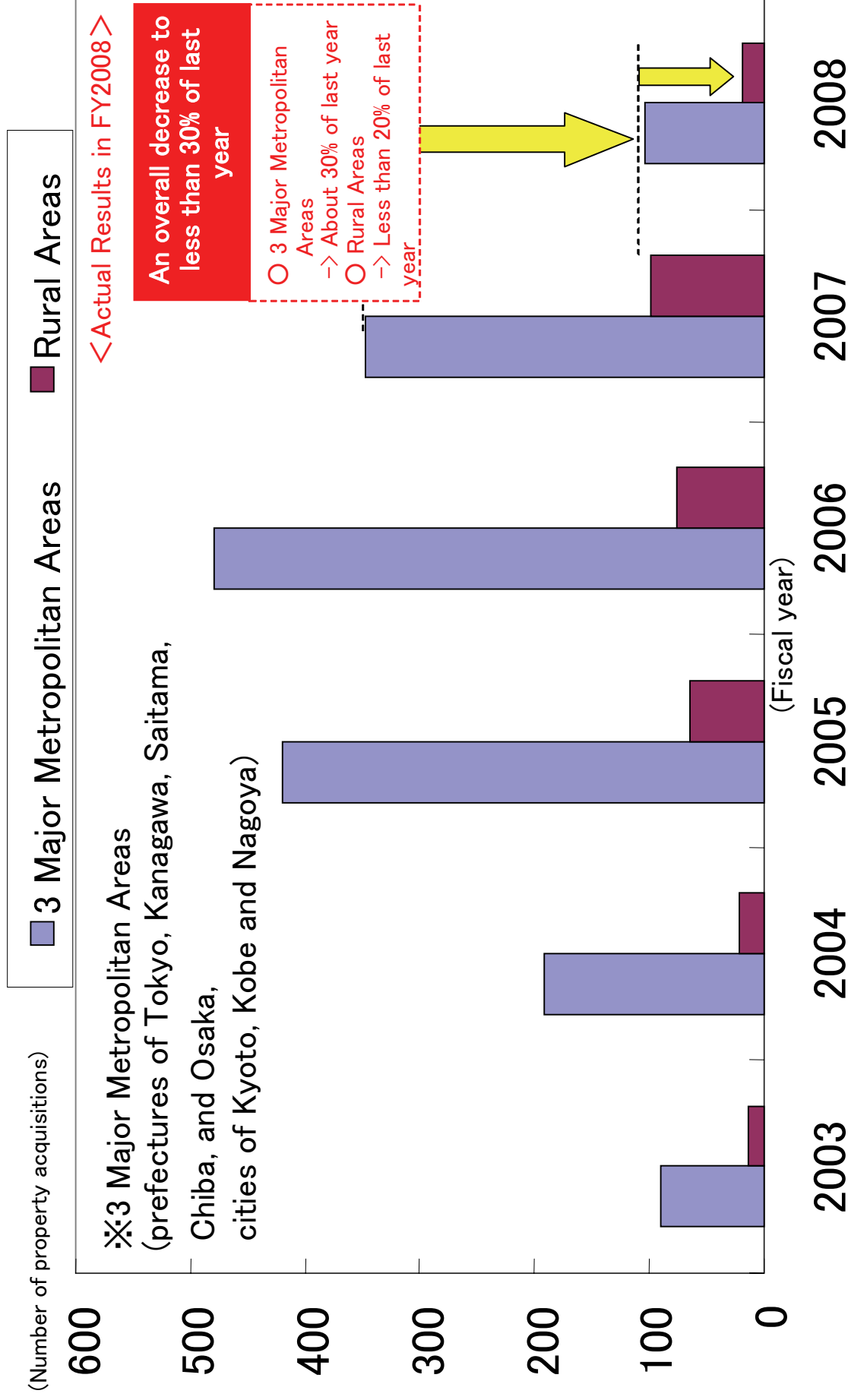
Limitations on Use of Funds (the above items (i) to (iv))

- (2) Conditions stipulated by Cabinet Office Ordinance stipulated under Article 139-13, item (i) (c) of the Act are the following:
 - (i) A short-term investment corporation bond scheduled for issuance has received a credit rating stipulated under provisions of Article 9-5 of the Cabinet Office Ordinance on the Disclosure of Corporate Information, etc. by a designated credit rating agency. (This refers to a designated credit rating agency stipulated under provisions of Article 1, item (xiii) (b) of the Ordinance. The same shall apply for the next paragraph, item (i).)
 - (ii) In the case of issuing short-term investment corporation bonds for the purpose stipulated under the preceding paragraph, item (i), an agreement for acquiring specified assets set forth in the same item shall either have been concluded, or it is certain that it will be concluded.
 - (iii) In the case of issuing short-term investment corporation bonds for the purpose stipulated under the preceding paragraph, item (ii), an agreement for repairing real estate set forth in the same item must either have been concluded, or it is certain that it will be concluded.
 - (iv) In the case of issuing short-term investment corporation bonds for the purpose stipulated under the preceding paragraph, item (iii), it is certain that the lease agreement will be terminated.
 - (v) In the case of issuing short-term investment corporation bonds for the purpose stipulated under the preceding paragraph, item (iv), there are provisions saying that the period until the principal redemption date is less than 6 months from the time the total amount of said short-term investment corporation bonds were paid.
- (3) In the case that the provisions under the Cabinet Office Ordinance set forth under provisions of Article 139-13, item (ii) of the Act, all of the following conditions shall be met.
 - (i) A credit rating stipulated under provisions of Article 9-5 of the Cabinet Office Ordinance on the Disclosure of Corporate Information, etc. is granted by a designated credit rating agency for the short-term investment corporation bond scheduled for issuance.
 - (ii) If either one of the following applies:
 - (a) In the case that any specified short-term investment corporation bonds (This refers to short-term investment corporation bonds whose funds for repayment will be acquired by issuing the short-term investment corporation bonds scheduled for issuance. The same shall apply to (b) below and the next paragraph.) are issued for the purposes set forth under paragraph 1, items (i) to (iii), there are provisions saying that the period until the principal redemption date is less than one year from the time the total amount of said specified short-term investment corporation bonds were paid.
 - (b) In the case that any specified short-term investment corporation bonds are issued for the purposes set forth under paragraph 1, item (iv), there are provisions saying that the period until the principal redemption date is less than six months from the time the total amount of said specified short-term investment corporation bonds were paid.
- (4) The short-term investment corporation bonds set forth under the preceding paragraph, items (ii) (a) and (b) whose funds for repayment will be acquired by issuing specified short-term investment corporation bonds (including short-term investment corporation bonds that are deemed as specified short-term investment corporation bonds as set forth under provisions of this paragraph) will be deemed as specified short-term investment corporation bonds.

*Since the use of funds is limited to property acquisitions or repairs, refunds of deposits, or stopgap funds required until the issuance of investment corporation bonds, short-term investment corporation bonds cannot be used as short-term funds, etc. until the acquisition of new loans.

Results of Property Acquisition by J-REITs

Property acquisitions by J-REITs fell significantly last year, which is greatly affecting the real estate market.

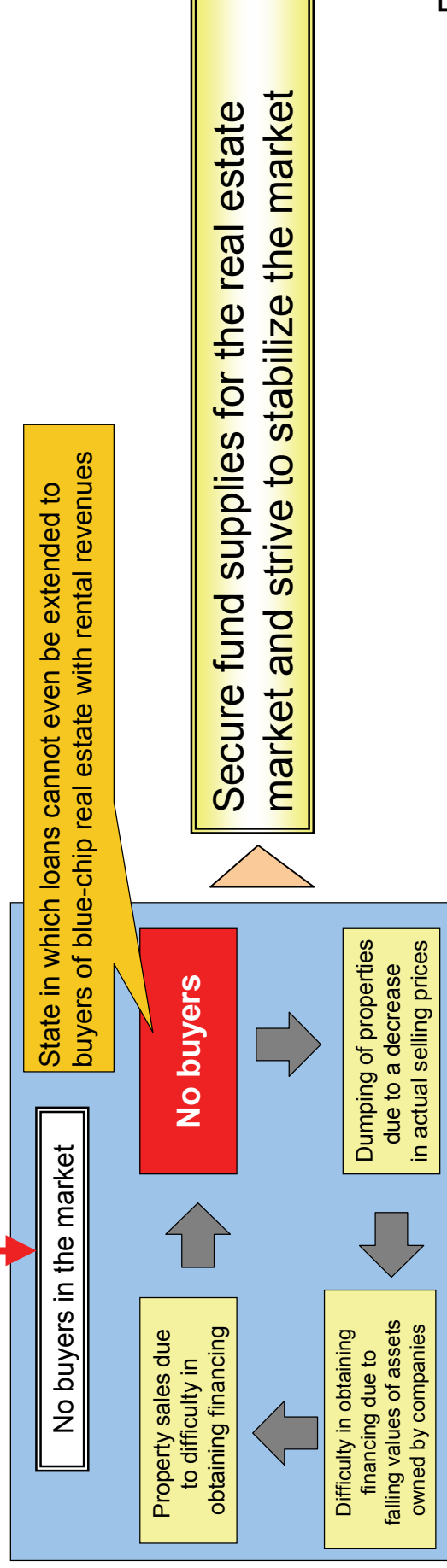


Need for Stability in the Real Estate Market

- In the current real estate market, fund supplies provided to buyers has gone down significantly. Furthermore, due to the dumping of properties in order to procure funds, there is concern about the significant decrease of actual selling prices.
 - Even J-REITs that have been major buyers are having problems making further property acquisitions due to the recent slumping share prices, credit crunch, etc., resulting in a shortage of financial institutions in the market willing to provide funds.
- *In fiscal 2007, J-REITs acquired about 1.5 trillion yen out of the total real estate sales amount for listed companies, etc., which was about 3.3 trillion yen.
- Therefore, we will discuss acquisition methods using a wide variety of funds for J-REITs, etc. and thereby strive to stabilize the real estate market by increasing funds for the acquisition of real estate.

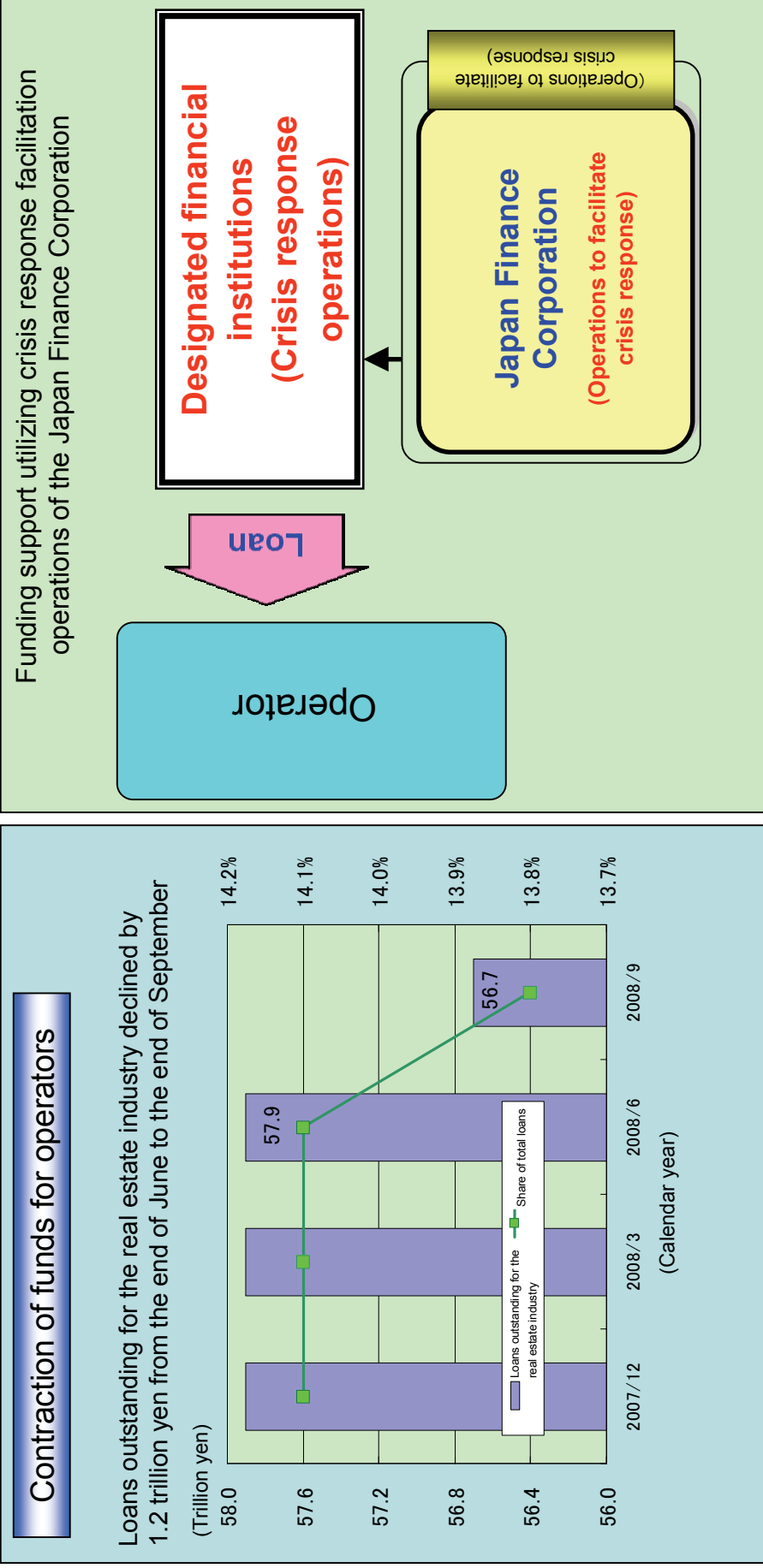
<Current Issues That the Real Estate Market Is Facing>

- In the current financial environment, most real estate market players are sellers and there are not enough buyers. If this situation is left to stand, then the real estate market may fall into a “negative spiral,” which is the condition of a lack of appropriate price formation in the market.



Funding Support Utilizing Crisis Response Facilitation Operations of the Japan Finance Corporation

Due to the impact of the turmoil in the global financial market triggered by the subprime loan problem, domestic financial institutions are tightening their lending stance toward the real estate industry. In response to the rapid credit crunch, we will provide funding support to housing and real estate operators with sound businesses by utilizing the crisis response facilitation operations of the Japan Finance Corporation. (Announcement by the Ministry of Land, Infrastructure, Transport and Tourism, December 15, 2008)



【Purpose for Establishing the Fund】

Due to the sudden credit crunch which occurred as a result of confusion in the international financial markets, J-REITs are having trouble with fund procurement despite their stable cash flows and secured profits. This shows that the real estate market has fallen into a “negative spiral,” where there is a lack of appropriate price formation.

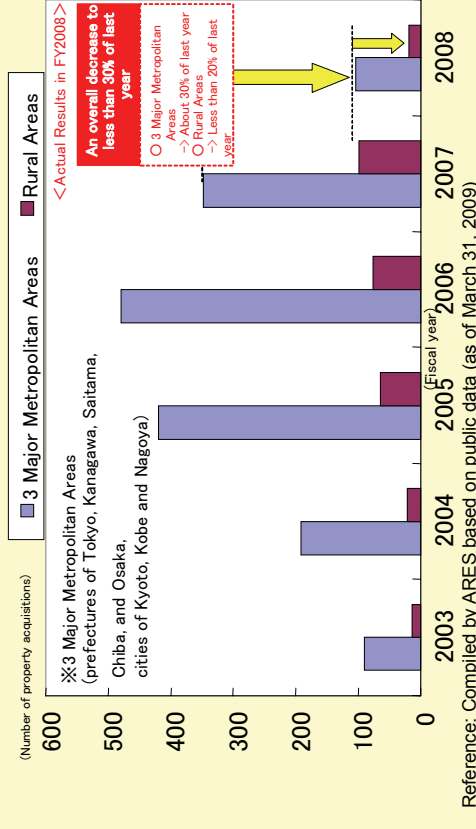
This measure aims to stabilize the real estate market and prevent asset deflation by working to recover the price formation functions in the market through the activities of J-REITs. In order to do so, the measure aims to form a Fund through cooperation between the government and the private sector in order to recover the function of J-REITs as buyers by newly providing funds to them.

【J-REITs That Are Major Buyers】

*The total amount of real estate sales for listed companies, etc., in fiscal 2007: → J-REITs acquired about 1.5 trillion yen out of a total of about 3.3 trillion yen.

*Source: ARES Handbook 2008-2009

【Property acquisitions by J-REITs fell significantly】



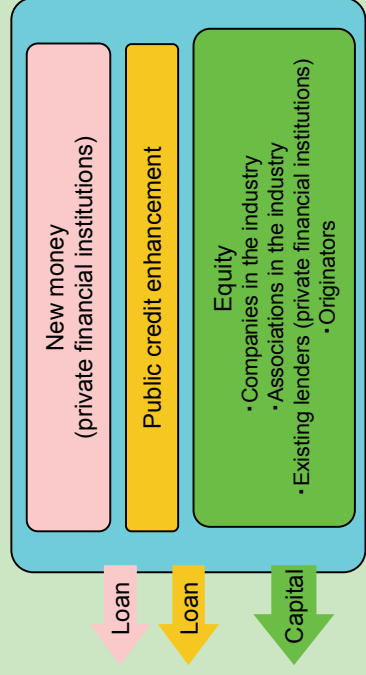
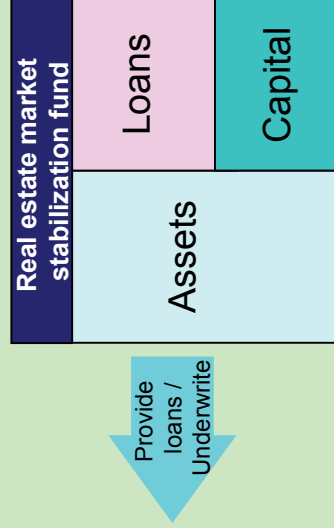
【Establishing the Fund】

○ In order to establish a fund through cooperation between the government and the private sector for the purpose of supplying funds to J-REITs, rules concerning incorporation need to be clarified, such as investment, loans, etc. upon consultation with related industries (the real estate industry, REITs, financial institutions), government authorities, experts, practitioners, etc.

J-REITs

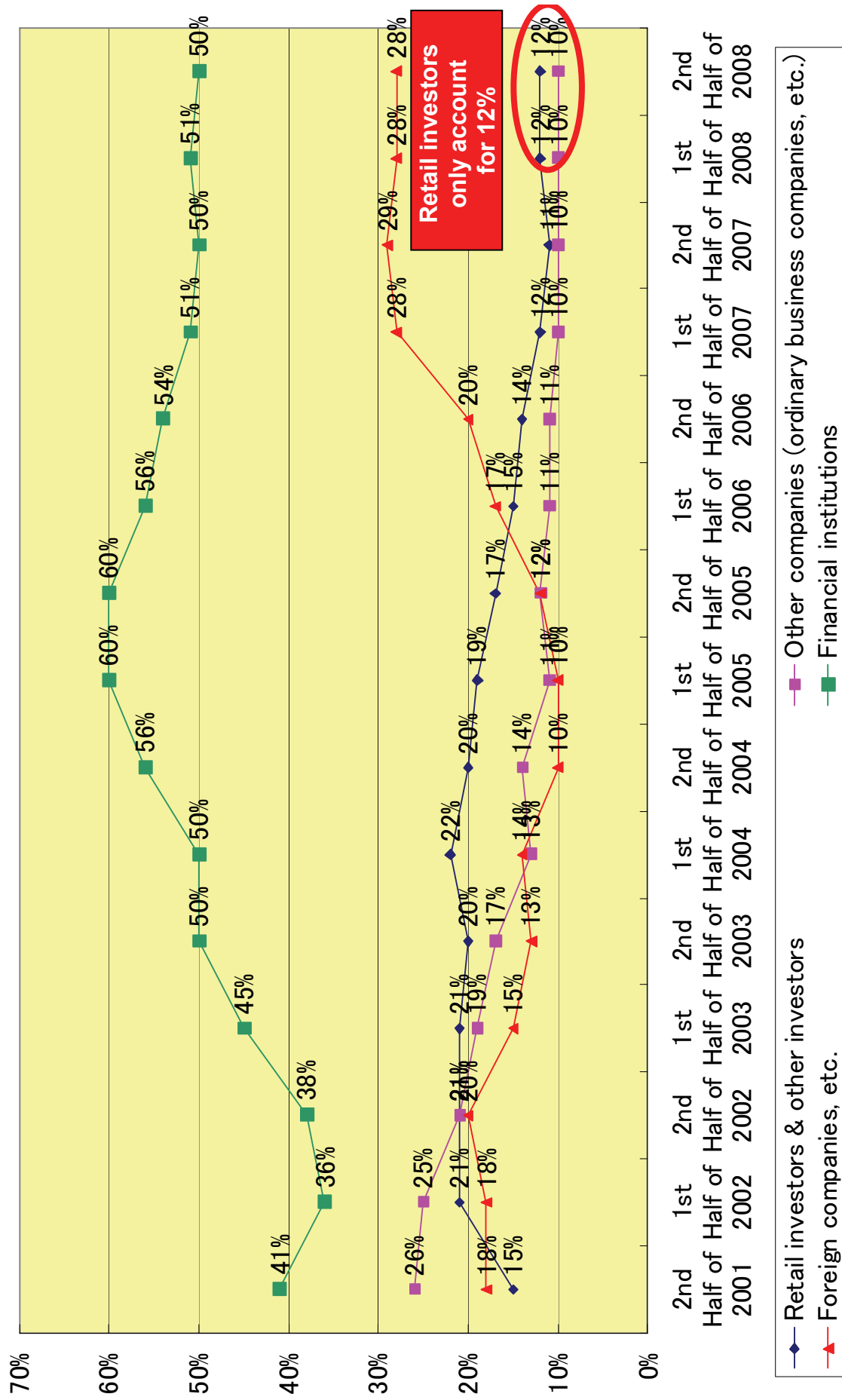
【Examples that would involve loans, etc.】

- New property acquisitions by J-REITs
- Funds necessary for reconstruction related to mergers, etc.
- Refinancing investment corporation bonds, etc.



Ratio of Retail Investors

Investment in J-REITs by Unitholder Type (based on amount)

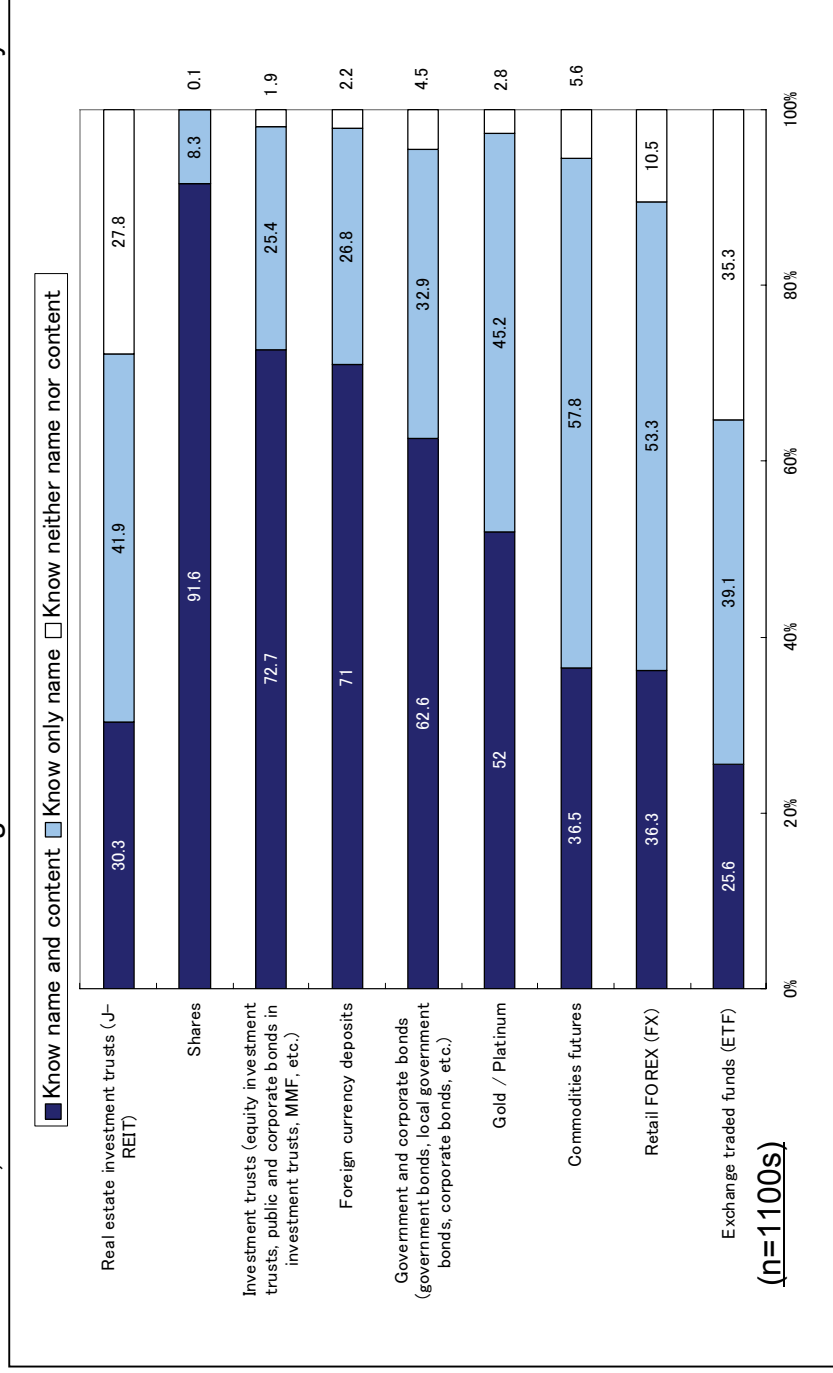


*Reference: ARES

Awareness Level of J-REITs by Retail Investors

O Awareness Level

The awareness of J-REITs by retail investors is about one-third of that of shares, and is lower than that of commodities futures and retail FOREX, etc. There is also a large number of retail investors who do not even know they exist.



Overview of "J-REIT Awareness Survey"

- ◇ Investigation period: December 2008
- ◇ Investigation method: Internet
- ◇ Sampling: Internet monitors from Nikkei Research, Inc.
- ◇ Target area: Nationwide
- ◇ Targets: Retail investors (Owners of financial products, excluding savings and insurance)
- ◇ Responses: 1,100

*Reference: ARES

Sale, etc. of Investment Trusts, Including J-REITs, at Bank Tellers

○ Investment Trusts Targeting J-REITs as an Investment Target Sold at Bank Tellers of Major Banks

Name of Bank	Products Sold at Bank Tellers
The Bank of Tokyo-Mitsubishi UFJ, Ltd.	NISSAY J-REIT Fund (2 months, settlement type)
	World REIT Open (every month, settlement type)
Mizuho Bank, Ltd.	Mizuho J-REIT Fund
Sumitomo Mitsui Banking Corporation	J-REIT Open
The Sumitomo Trust and Banking Co., Ltd.	Sumishin J-REIT Research Open (every month, settlement type)
Mitsubishi UFJ Trust and Banking Corporation	Mitsubishi UFJ J-REIT Open (3 months, settlement type)
	NISSAY J-REIT Fund (2 months, settlement type)
	Nomura Japan-US REIT Fund (monthly, dividend payment type)
	World REIT Open (every month, settlement type)
The Chuo Mitsui Trust and Banking Company, Limited	Chou Mitsui J-REIT Fund
Japan Post Bank Co., Ltd.	Nomura World Six Assets Distribution Investment Trust
	Nomura Asset Design Fund
	DIAM World REIT Index Fund (monthly, dividend payment type)

*Posted on each bank's website (as of May 20, 2009).

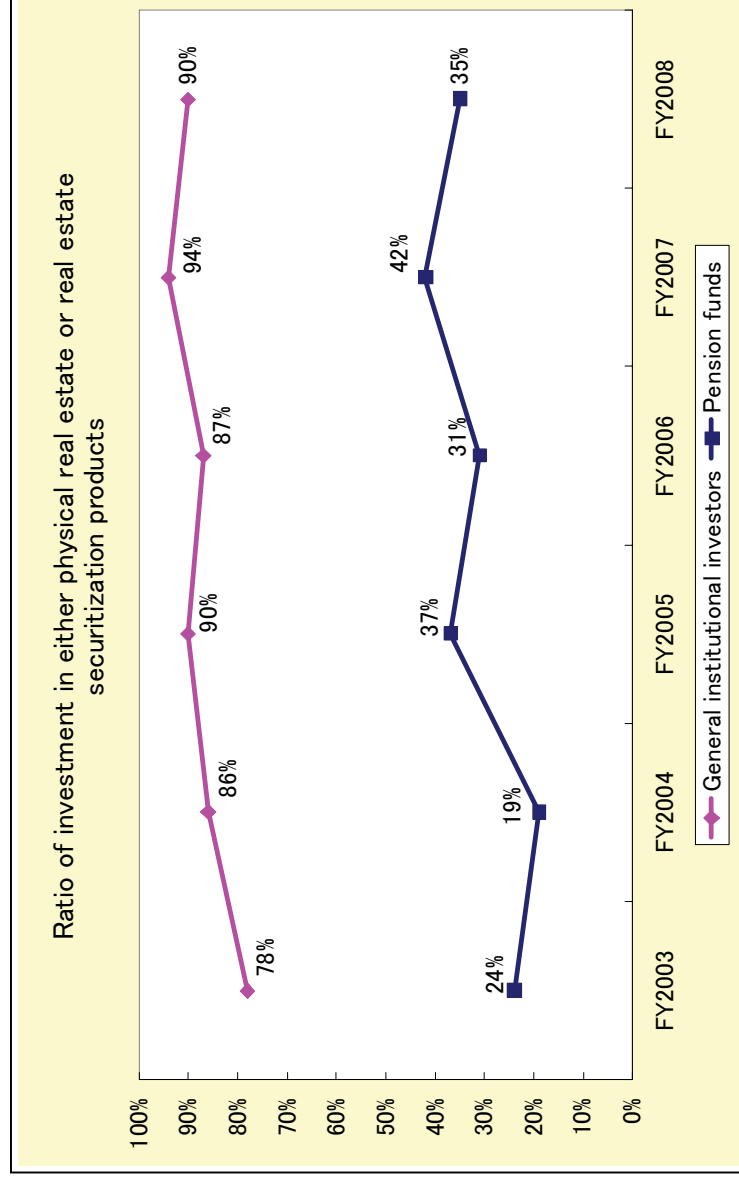
○ ETFs which are listed on the TSE market and designed to correspond to the TSE REIT index

Name	Fund Administrator
NEXT FUNDS REIT INDEX ETF	Nomura Asset Management
Listed Index Fund J-REIT (Tokyo Stock Exchange REIT Index) Bi-Monthly Dividend Payment Type	Nikko Asset Management

Real Estate Investment by Pension Funds

O Changes in the Ratio of Pension Funds Conducting Investment in Real Estate

The ratio of pension funds investing in real estate is on the rise. However, in comparison with general institutional investors (life insurance companies, non-life insurance companies, banks, trust banks, etc.), the ratio is low.



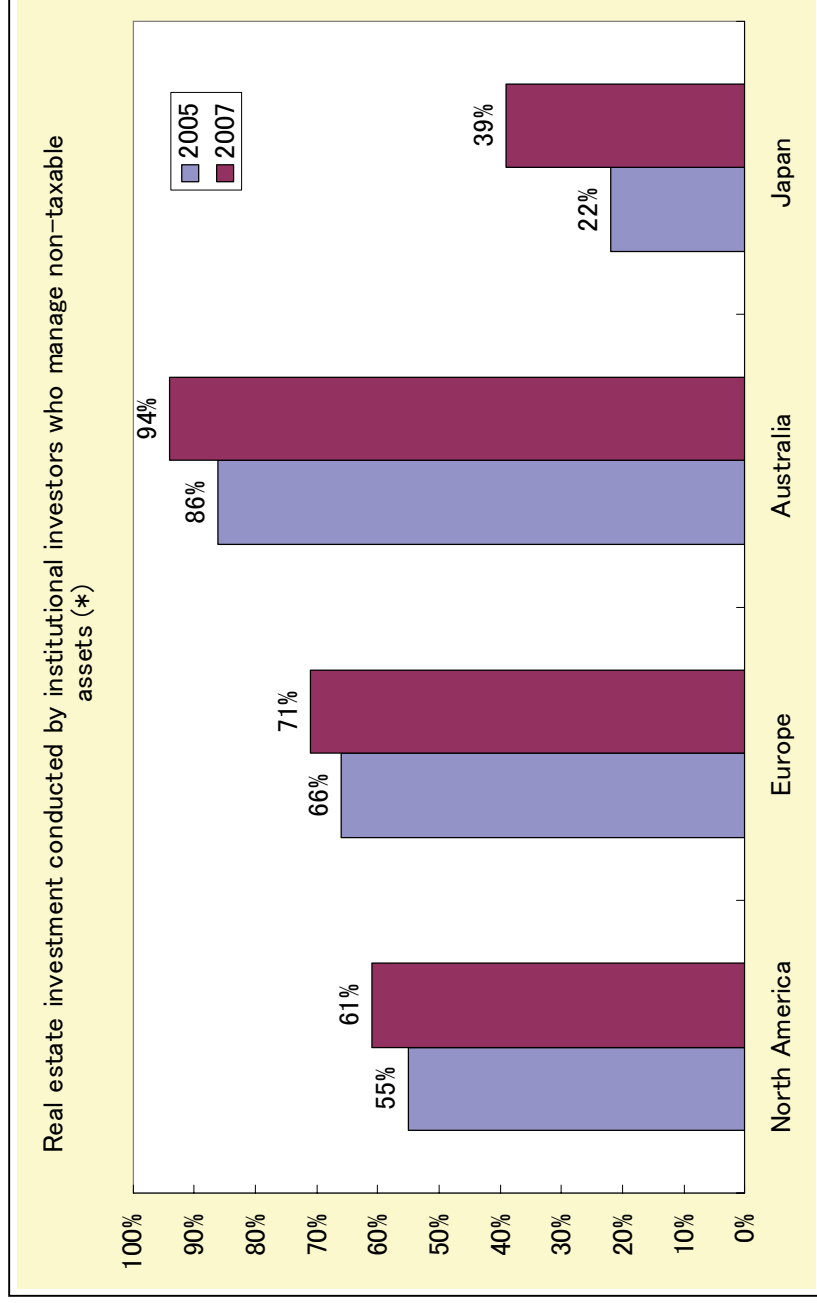
*Reference: "The 8th Questionnaire Survey on Real Estate Investment by Institutional Investors" by The Association for Real Estate Securitization (July 2008)

*Moreover, a point to note is that the possibility that respondents of the questionnaire conducted by ARES (The 8th Questionnaire Survey on Real Estate Investment by Institutional Investors) having a high interest in real estate investment is high due to the nature of the questions. For example, according to the questionnaire conducted by Daiwa Fund Consulting Co., Ltd., the ratios of pension funds actually investing in real estate are as follows: 2005: 16.8%; 2006: 17.0%; 2007: 20.1%

Real Estate Investment by Pension Funds

Real Estate Investment by Pension Funds in Various Countries

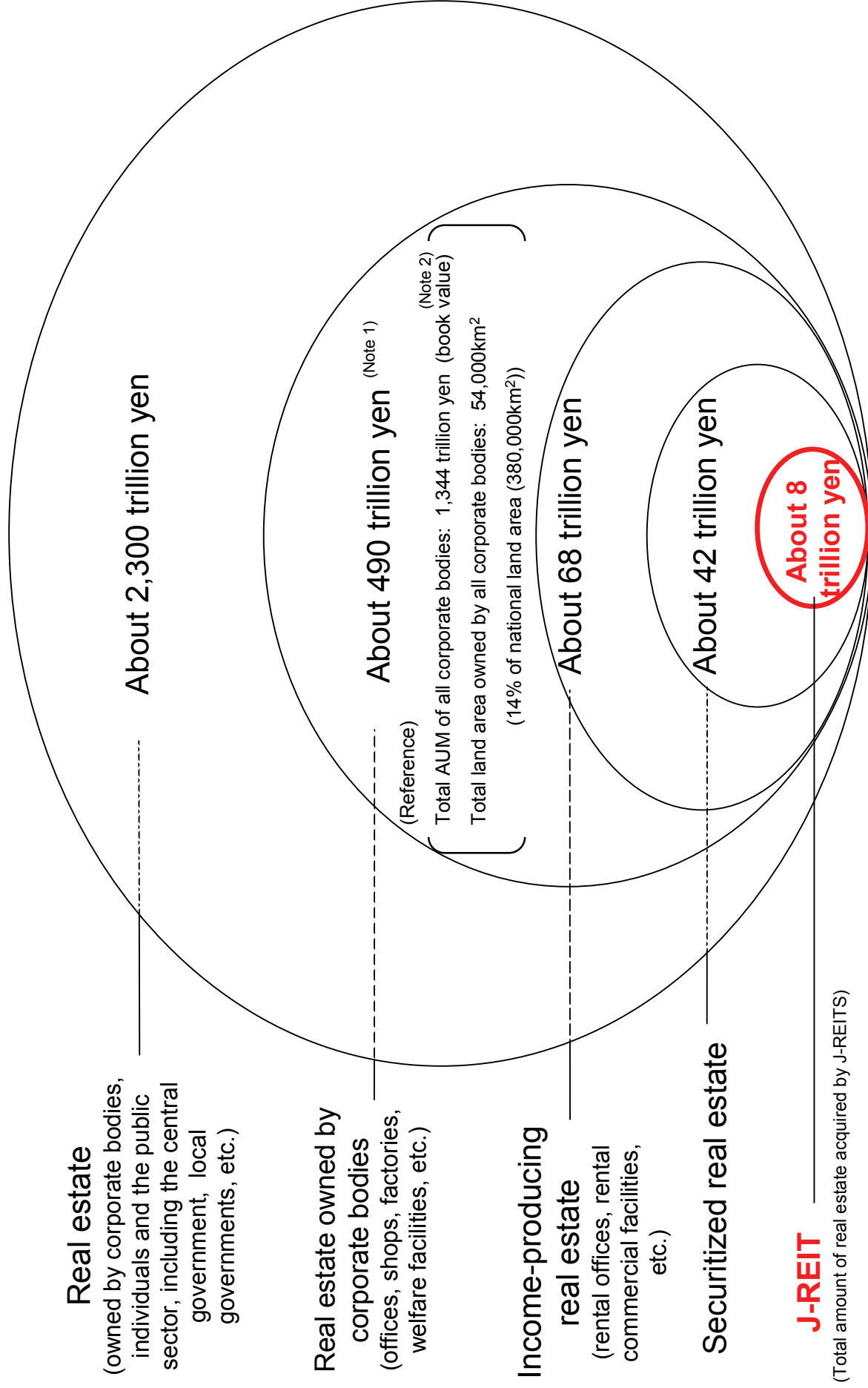
We compare the state of real estate investment conducted by non-taxable institutional investors, starting with pension funds in North America, Europe and Australia with those in Japan. You can see that although there is an increase in Japan, there is still a large gap between the former three and Japan in terms of level.



*The ratio of respondents in the questionnaire who responded that they conducted real estate investment.

*Reference: Compiled by ARES based on the public data of Russell Investments,
"The 2007-2008 Russell Investments Survey on Alternative Investing"

Asset Size of Japanese Real Estate

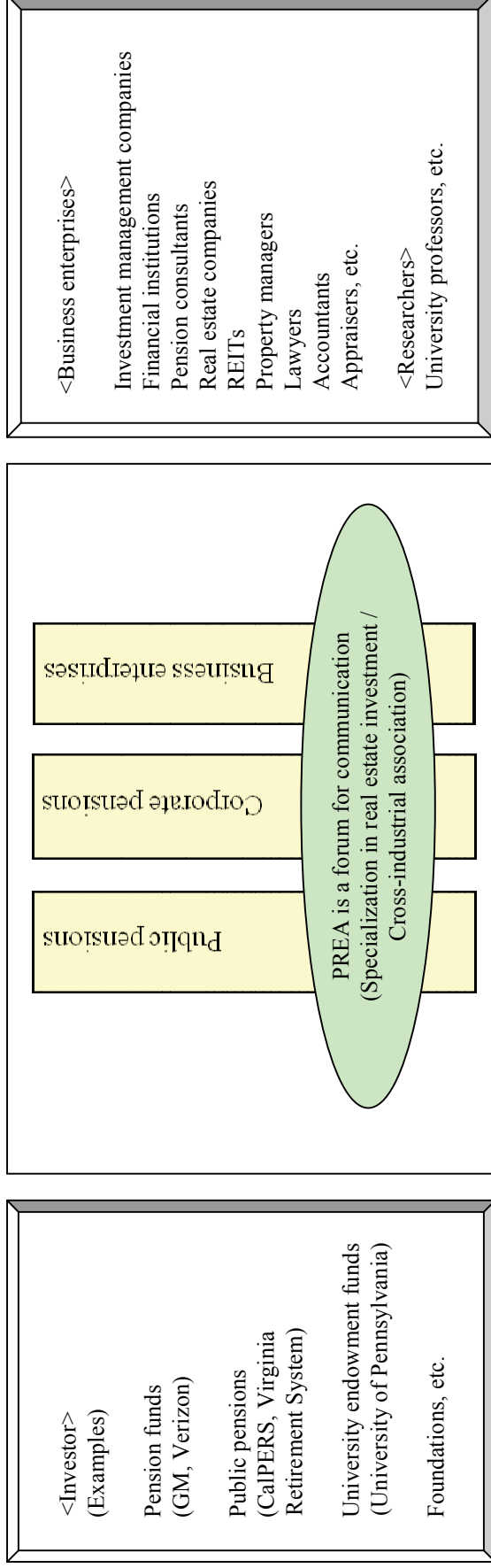


Reference: "National Accounts for 2005" (annual report), General Report of "Basic Survey on Land" (2006), "Real Estate Securitization Survey" (2007); (The AUM for "real estate," "real estate owned by corporate bodies" and "income-producing real estate" is based on January 1, 2003 data; the AUM for "securitized real estate" and "J-REIT" is based on end of FY2007 data)

(Note 1) Market value is based on the "Basic Survey on Land" (as of January 1, 2003); (Note 2) Book value is based on the "Financial Statements Statistics of Corporations by Industry" (as of the end of 2005); (Note 3) The actual cumulative size of securitized real estate (as of the end of FY2007); (Note 4) As of the end of FY2007; (Note 5) Including areas for roads, water conduits, etc.

PREA (Pension Real Estate Association in the U.S.)

○ PREA (Pension Real Estate Association in the U.S.): What it is



PREA, located in the U.S., is a membership organization for a wide range of sectors, such as pension funds, corporate pensions, business enterprises and researchers. It specializes in real estate investment and provides a forum for discussion across industries.

What is the PREA (Pension Real Estate Association)?

In 1979, it was established with the aim of providing a forum for conducting communication between investors, management institutions and real estate service operators.

It places focus on the education and enlightenment of members and provides information through conferences, newsletters, etc.

The association provides funds for academic research relating to real estate investment, such as by becoming a sponsor for researchers pertaining to academic research or by conducting management of research institutions.

Participation in the formulation of the Real Estate Information Standard.

The Principles for Responsible Investment

○ Socially Responsible Investment (SRI)

Socially Responsible Investment is the introduction of countermeasures regarding morality, environmental issues, etc. in the evaluation of investment in a company, and not simple the outlook of revenues and growth.

○ The Principles for Responsible Investment (PRI)

The Principles for Responsible Investment is a global guideline for investors, which incorporates the idea of “sustainable development” into the analysis and evaluation of investment and was formulated in 2005 when the then Secretary-General of the United Nations invited major institutional investors across the world for this purpose. It is based on the assumption that “Environmental, Social and Corporate Governance issues” (=ESG) affect investment performance and was formulated with the aim of incorporating the ESG perspective in the decision-making process of the investment decisions of institutional investors of the world, such as major pension funds or management institutions, within their range of responsibilities as trustees.

The work of formulating The Principles for Responsible Investment was led by the United Nations Environment Programme Finance Initiative (UNEP FI) and the UN Global Compact and was officially announced in 2006.

○ Major Points of Responsible Real Estate Investment

One of the working groups of UNEP FI, called the UNEP FI Property Working Group (UNEP FI PWG), conducts activities to promote real estate financing by financial institutions across the world cooperating in bringing about sustainable development. They announced the major points of The Principles for Responsible Investment.

	Focus	Details
1	Energy conservation	Reducing energy consumption
2	Transportation access	Promoting the use of public transportation and reducing the use of automobiles
3	Residential environment and circulation environment	Environment in rooms, common space facilities, measures for the handicapped
4	Environmental protection	Countermeasures against global warming, conserving water resources, utilizing environmentally conscious materials
5	Certification / Branding	Energy conservation, various certifications regarding green buildings (environmentally conscious buildings)
6	Publicness	Compliance with laws and regulations / disclosure, etc.
7	Fairness	Fair labor environment / employment opportunities / low-income housing, etc.
8	Safety / Security	Security measures
9	Urban redevelopment	Contribution to revitalization of urban areas

*Reference: UNEP FI PWG and Responsible Property Investment Center

Discounted Cash Flow Method

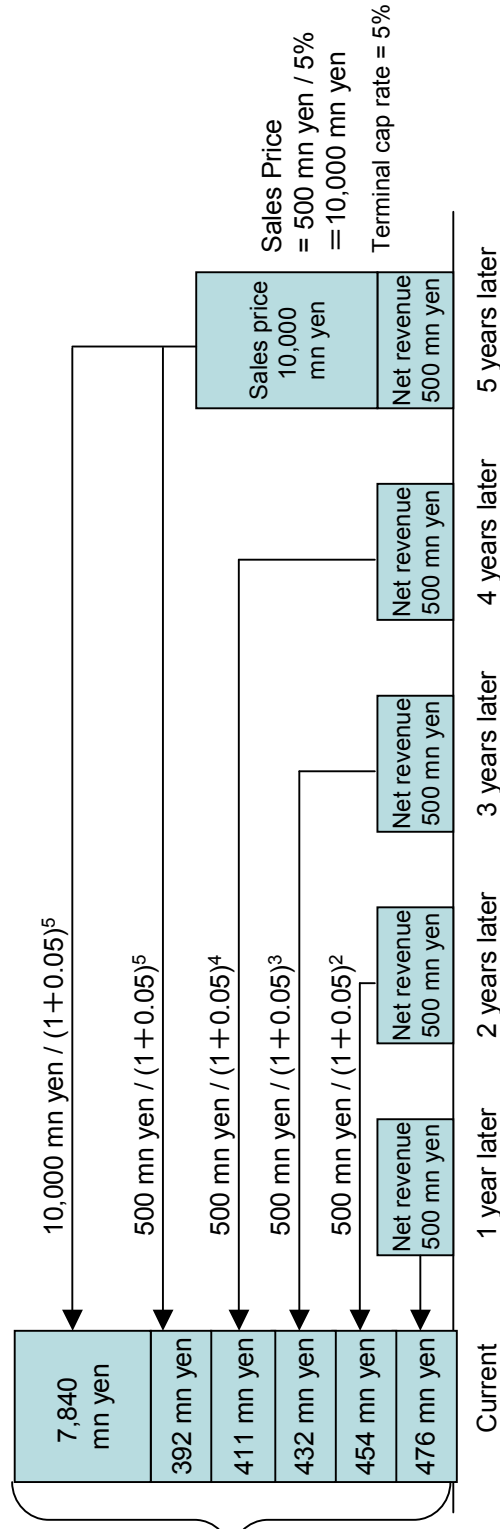
DCF Method

The DCF Method is a method for seeking the current real estate price by discounting the total of net revenues that the targeted real estate will produce in the future over a certain period of time and the sales price after a certain period of time from the current value.

A difference of 1% in the discount rate of a property worth 10,000 million yen results in a difference in real estate price of about 2,000 million yen.

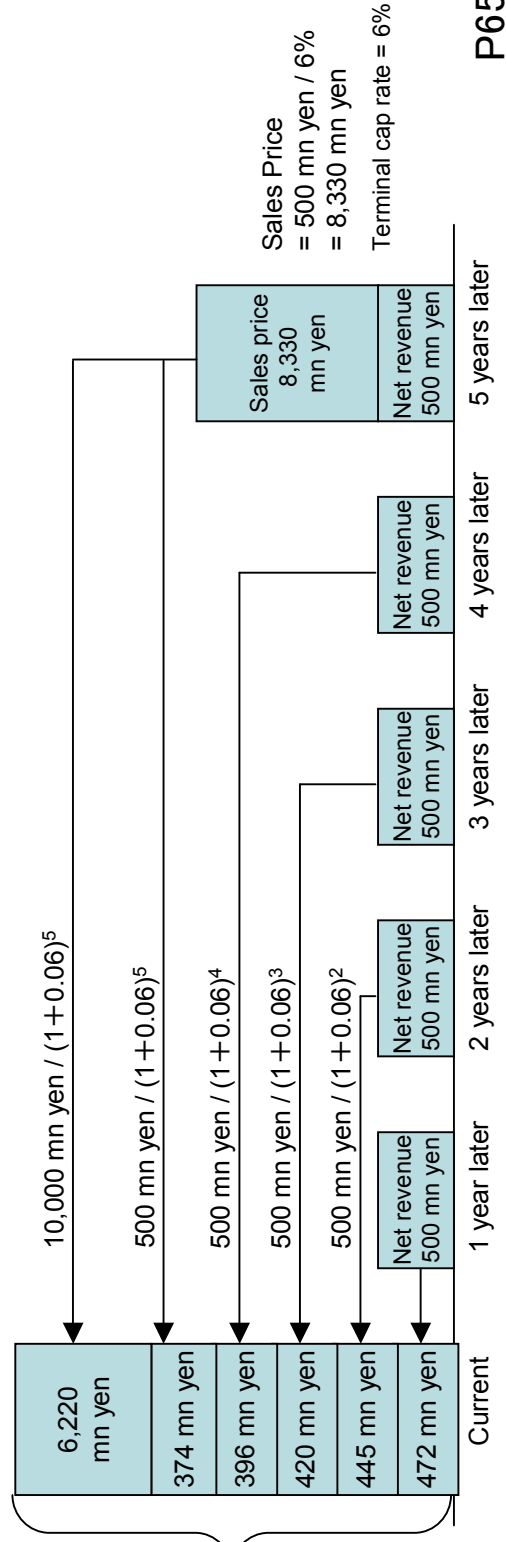
Discount Rate = 5%

Real estate price = 10,000 mn yen



Discount Rate = 6%

Real estate price = 8,300 mn yen



Example of Price Fluctuation Due to Increase in Cap Rate

○ Example of Price Volatility Due to Increase in Cap Rate

As for the appraisal of properties owned by J-REITs at the end of each fiscal term, there can be seen examples of appraisal values decreasing as a result of an increase in the cap rate rather than as a result of a decrease in the estimated rents in the future.

	Building A			Building B		
	End of Dec. 2007	End of Dec. 2008	Volatility	End of Dec. 2007	End of Dec. 2008	Volatility
Appraisal value (survey price)	6280	5260	-16.2%	5730	5190	-9.4%
NCF (appraisal)	227	228	0.4%	232	238	2.6%
Direct capitalization approach	CR (cap rate)	4.3%	-16.3%	4.0%	4.50%	-11.1%
DCF Method	DR (discount rate)	4.2%	-16.7%	3.8%	4.30%	-11.6%
	TCR (terminal cap rate)	4.3%	-16.3%	4.0%	4.50%	-11.1%

*NCF: Net cash flow (= Rent – Expenses + Profit from the management of deposits, etc. – Capital expenditures)

○ Report by the Real Estate Appraisal Working Group of the Land Policy Division at the National Land Council of the Ministry of Land, Infrastructure, Transport and Tourism

The “Report by the Real Estate Appraisal Working Group of the Land Policy Division at the National Land Council of the Ministry of Land, Infrastructure, Transport and Tourism” announced on April 2009 indicated directions that included reinforcing internal control systems in order to enhance the credibility of appraisals.

■ Enhancing the credibility of the appraisal operations of securitized real estate, etc. so that they are widely used by the public

It is thought that appraisal of real estate securitization and real estate in corporate books can greatly impact a wide range of investors and other persons. Therefore, it becomes necessary to ensure the transparency and objectivity of appraisals more than ever before, as well as the independence and neutrality of appraisers from applicants, etc.

1. Enhancing the internal control systems of appraisers

We need to establish a system of auditing the appraisal report and a firewall between the appraisal division and other divisions, such as the sales division, etc., discuss how progress reports given to applicants regarding the value should appear, and establish internal control systems to prevent insider trading, etc.

2. Requiring the involvement of several real estate appraisers / Developing a system of auditing appraisal reports

In order to maintain or improve the quality of appraisals, it is desirable that several real estate appraisers become involved in the production of one appraisal. Thus, a system for auditing an appraisal report made by an appraiser by other appraisers needs to be established, etc.

3. Establishing transparency for applications from related parties and postponement of orders

It is desirable that the independence and neutrality of appraisers / appraisal companies are obvious in an objective manner. Furthermore, as for applications for appraisals made by interested parties and other specially related parties of the targeted real estate, we need to inform the applicant about whether a special relationship exists and we need to strive to maintain transparency by writing the details in appraisal reports.

*Compiled based on “Towards an Appraisal that Better Responds to Changes in Society,” a report by the Real Estate Appraisal Working Group of the Land Policy Division at the National Land Council of the Ministry of Land, Infrastructure, Transport and Tourism .

Information Disclosure by J-REITs

○ Examples of Items Concerning Which Information Disclosure Is Desirable

The following are examples of items, etc. where it is desirable that J-REITs conduct discussions with market participants and continues to do its utmost to make improvements.

Examples	Current Conditions of REITs
English disclosures for overseas investors (including English websites)	35 companies out of 41 listed REITs are implementing English language disclosures.
Disclosure of NOI*, which would form the basis of appraisals and disclosure of cap rates, etc.	39 companies out of 41 listed REITs are conducting disclosure.
Disclosure of long-term repair expenses at the time of property acquisition	17 companies out of 41 listed REITs are conducting disclosure.
Other • Disclosure of assets, etc. that back the funds in the case of forward commitments, etc. • Abstain from incorporating the gain on sales of property for which the sale has not been finalized into performance forecasts. • Disclosure of information regarding contract periods, etc. with large tenants • Disclosure of loan-related expenses • Disclosure of estimated cap rates, etc. at the time of acquiring the property, etc.	

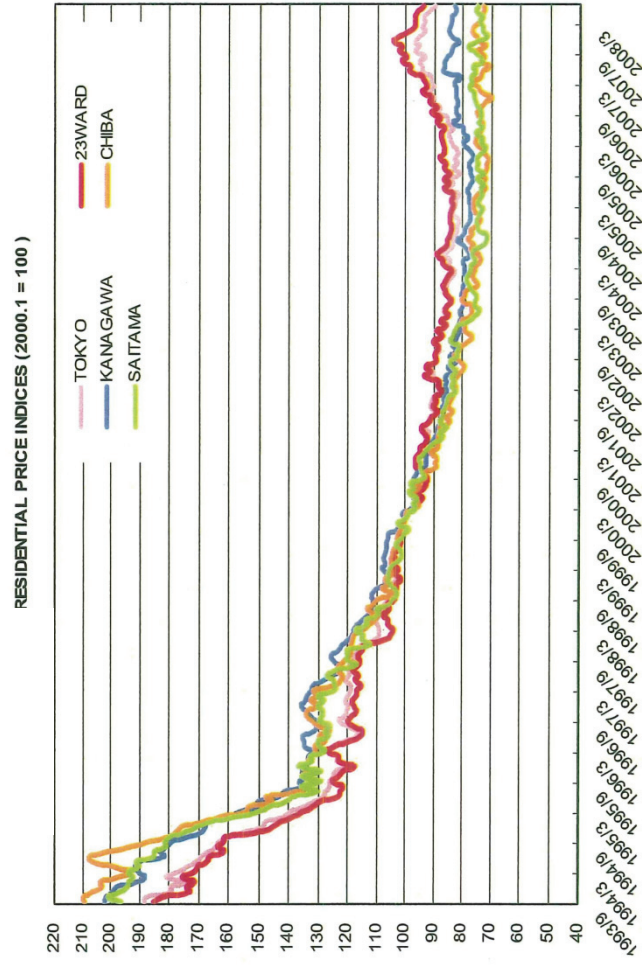
* NOI: Net operating income.

Note: Compiled based on press releases, asset management reports, etc. announced by companies (as of May 20, 2009).

Residential Price Indices

- In the U.S., housing indices based on actual selling prices are publicly available, such as the S&P / Case-Shiller Home Price Indices.*
- As a result, these indices make it possible to grasp housing price trends over a wide range of areas, and serve as important information for investors, business enterprises and buyers of used housing, etc.
- There is no counterpart to these indices in Japan, and some people point out that this lack is one reason why the housing values perceived in the market are lower than what they are supposed to be.

Sample of a Residential Price Index



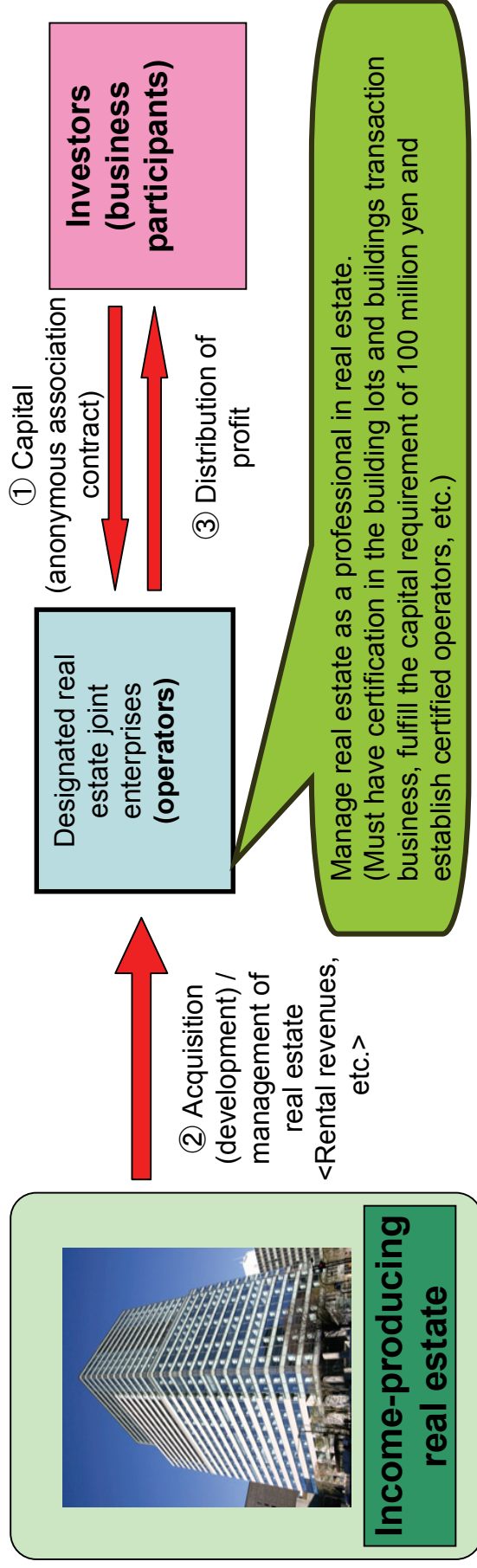
Therefore, we believe it is necessary for Japan to develop housing price indices based on actual selling prices, and to make them widely available.

→ Enhance the transparency of the real estate investment market, which in turn would activate the market.

*The S&P / Case-Shiller Home Price Indices target residential real estate in the U.S. The price indices are provided by the credit rating agency Standard & Poors and are the most commonly used of their kind.

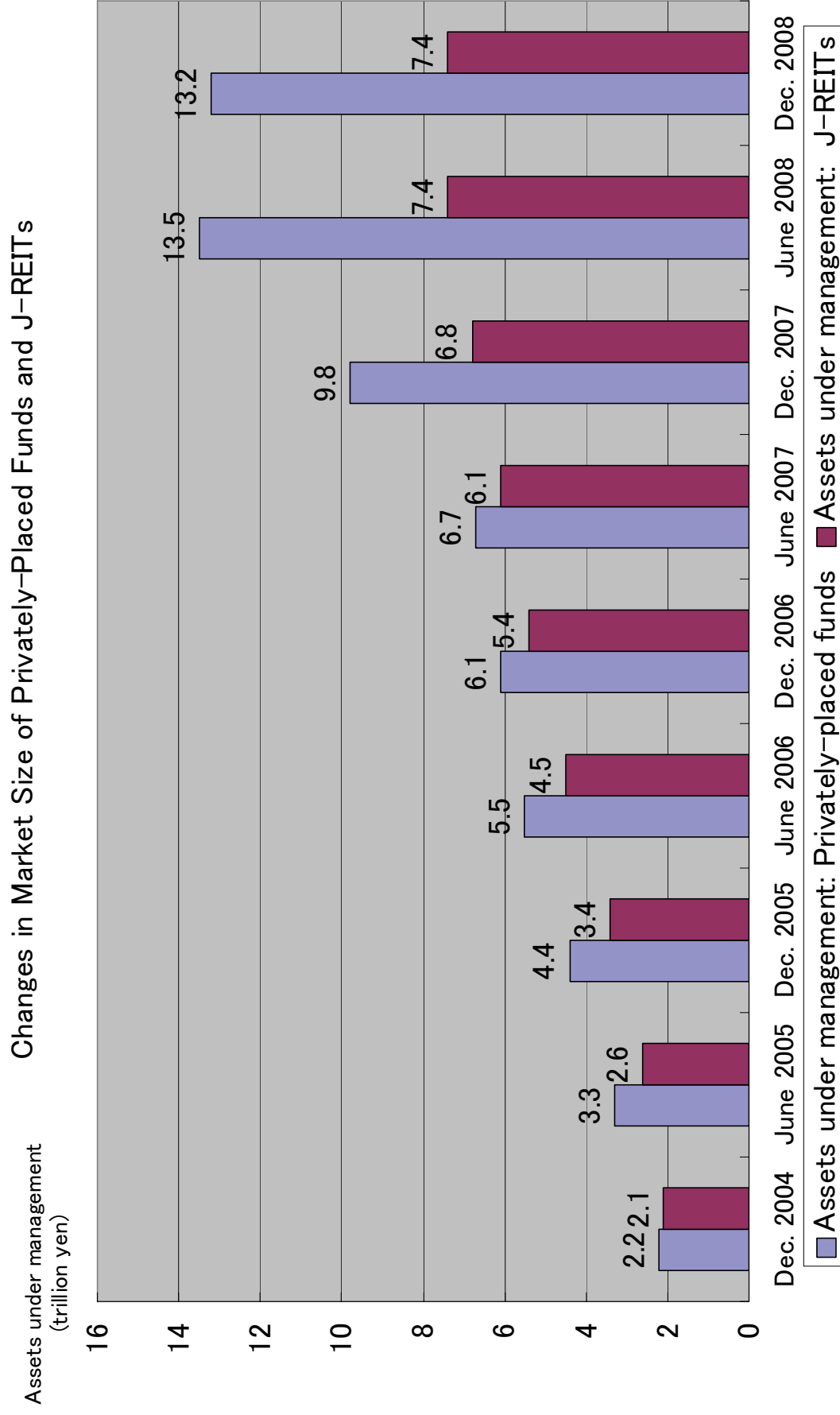
Development of Diversified Business Methods (Example of Demand)

- As for designated real estate joint enterprises, which are part of the securitization scheme of physical real estate, a business operator (a designated real estate joint enterprise) that is party to an equity instrument (anonymous association contract) is required to have more than 100 million yen of capital and must have established certified operation managers, etc. Therefore, it is difficult to use it as a paper company, such as is the case with ordinary SPCs.
- Therefore, some are of the opinion that when a joint enterprise consisting only of developers or professionals in real estate investment tries to undertake a development project using this scheme, it faces difficulties in procuring non-recourse loans through a paper company.



→ **Need to periodically discuss methods for promoting the development of various businesses that respond to market demands**, including measures, etc. for the above types of demands.

Market Size of Privately-Placed Funds



*Reference: STB Research Institute Co., Ltd.

