REITS IN HAWAII: MISPERCEPTIONS CORRECTED

Misperception: Hawaii and its residents do not benefit by investment in REITs by Hawaii shareholders.

Fact: Yes, Hawaii benefits a great deal from investment by its residents in REITs.

In 2015, REITs were associated with more than 11,700 jobs representing labor earnings of nearly $500 million and $95 million in tax revenue in Hawaii. In the past five years REIT-related construction activity is estimated to have generated $3 billion in Hawaii GDP.

As an example, Taubman Centers, Inc.'s International Market Place development is currently under construction and is projected to generate over a series of years $10 million annually in general excise tax (from landlord rents and by tenants from retail sales of merchandise), over $4 million annually in property taxes, and employment of over 1,000 construction jobs and 2,500 permanent jobs (which will generate individual income tax revenues). At Ala Moana Center, General Growth Properties has or will be investing almost $1 billion in capital to construct additional retail square footage and luxury residences, along with local partners Hawaiian Dredging Company, The MacNaughton Group, The Kobayashi Group, and Blacksand Capital. During the multi-year construction period, economic activity of 11,600 full- and part-time jobs and over $146 million of state revenue has been estimated. Post the construction period, the shopping center investment alone will produce an incremental $33 million of state revenue and 3,000 jobs annually.

There are actually thousands of REIT shareholders in Hawaii. In 2014, over 9,000 Hawaii investors had investments in over 70 public, non-listed REITs and received almost $30 million in distributions. Shareholders in general have benefited from stock exchange-listed REIT investment: the 15-year compound annual return for the period ending June 30, 2015 of the S&P 500 stock index was 4.36%, while that of listed equity REITs was 11.34%. Additionally, Hawaii state and county employees also benefit from REITs through the approximately $70 million investment of the Hawaii Employer-Union Health Benefits Trust Fund's investment in a REIT index fund (as of June 2014). Furthermore, as of September 30, 2015, a number of institutional money managers based in Hawaii manage over $20 million in REITs almost all of which own no Hawaii properties.

Misperception: Hawaii has enough local capital without outside REIT investment.

Fact: Creating thousands of new jobs and millions of dollars in additional GET and property tax revenue when insufficient local capital existed to do so, REITs have invested in, and revitalized Hawaii properties.

Unlike other business entities, REITs are required to be widely-held, and hundreds are listed on major stock exchanges or sold over broker-dealer networks. This access to the capital markets provides REITs with the avenue to raise funds which they are able to deploy as needed to develop or improve existing properties.

For example, American Assets Trust, a San Diego-based REIT, partnered with Outrigger Enterprises in Hawaii to redevelop Waikiki Beach Walk, at a time when it appeared that there was insufficient local capital to do so. Douglas Emmett, Inc., which has been investing in Hawaii for over a decade, currently owns over 1,500 apartment units in Honolulu, and is expanding workforce housing options at a number of places, including Hawaii's Moanalua Hillside Apartments, with the addition of 504 units. Taubman Centers, Inc., and Queen Emma Land Company have moved forward with their plans to revitalize the International Market Place in Waikiki. As one of the most valuable land assets of Queen Emma Land Company, International Market Place's redevelopment will support the mission of The Queen's Medical Center to improve the well-being of Native Hawaiians and all the people of Hawaii. General Growth Properties' expansion of Ala Moana Mall and WP Glimcher's maintenance and improvements to Pearlridge Center have provided thousands of jobs and millions of dollars in General Excise Tax (GET) and property taxes.

Misperception: Taxing REITs like any other corporation would not affect Hawaii's ability to attract investment.

Fact: Taxing REITs differently from the way virtually every other state does would make Hawaii an outlier – and REITs likely to shift their investment and jobs to the mainland.

Today, all states, including Hawaii, that impose an income tax on corporations (other than New Hampshire) conform to the federal income tax rules and allow widely-held and/or publicly traded REITs (and mutual funds) to deduct their dividends (including capital gain dividends) paid to shareholders. In fact, although both Hawaii and New Hampshire have roughly equivalent contributions to the nation economy, REIT investment in Hawaii is about four times that of New Hampshire.[1] Most REITs investing in Hawaii, such as widely-held CNL Lifestyle Properties, Inc. which owns Wet'n'Wild Hawaii, have the majority of their investments in states other than Hawaii, and many of them could choose to sell their Hawaii properties, or at the least not contribute additional funds to, or expand their Hawaii operations, because investments in other states could produce better after-tax returns. Removing many, if not most, REITs as potential investors in Hawaii could depress commercial real estate values and the general excise taxes paid by REITs, their tenants and customers, and potentially result in job loss.

Misperception: Not many Hawaii residents are REIT shareholders.

Fact: Thousands of Hawaii investors directly or through mutual funds own millions of dollars in REIT stock.

As noted above, in 2014, over 9,000 Hawaii investors had investments in over 70 public, non-listed REITs and received almost $30 million in distributions, and tens of thousands more directly or indirectly own shares in stock exchange-listed REITs. As of June 30, 2015, a number of Hawaii-based investment managers reported positions worth over $50 million in approximately 20 stock exchange-listed REITs. The majority of these REITs own no Hawaii properties, but the dividends paid to Hawaii residents are taxable by the state. Also, as of February 2015, one of largest REIT-dedicated mutual fund sponsors had over 3,000 Hawaii-based investor accounts worth about $60 million and in 2014 these accounts in Hawaii received income and capital gain distributions totaling $8.5 million.

Misperception: REITs don't pay a fair share of taxes in Hawaii.

Fact: REITs, their affiliates and tenants, and their shareholders, pay substantial taxes in Hawaii.

Over 20 publicly traded REITs have invested billions of dollars in Hawaii real estate that produces millions of dollars in state and local taxes. These include the general excise and property taxes generated in the shopping malls and centers REITs own in Hawaii. Taubman Centers Inc.'s redevelopment of International Market Place alone is expected to generate $10 million in additional general excise tax (GET) and $4 million in property taxes. Also, Hawaii income taxes are owed on REIT dividends distributed to Hawaii residents who own REIT stocks no matter where the REITs do business.

Misperception: REITs operate like any other entity that owns real estate, and should pay income taxes like regular corporations.

Fact: Unlike regular corporations, REITs must: be widely-held; own and earn most of their income from real estate or real estate loans held for a long-term horizon; and currently distribute all of their taxable income (so the income is currently taxable to shareholders).

While regular corporations can and typically do retain their after-tax earnings, the REIT model was designed to ensure that a REIT's income would flow through and be taxed to the shareholders. In 2014 alone, SEC-registered REITs distributed more than $46 billion to their shareholders, and for the period 1994-2014, they have distributed over $388 billion to shareholders, with that income currently taxable at the shareholder level.

For more detailed data and research regarding REITs, go to www.reit.com.

1. REIT Investments as a Percentage of State GDP – a Partial Ranking (excerpted from Economic Impacts of Real Estate Investment Trusts in Hawaii, by Paul H. Brewbaker.)