REIT IPOs

A QUICK GUIDE
WHY, LAND IS THE ONLY THING IN THE WORLD WORTH WORKIN’ FOR, WORTH FIGHTIN’ FOR, WORTH DYIN’ FOR, BECAUSE IT’S THE ONLY THING THAT LASTS.

GONE WITH THE WIND (1939)
Real estate investment trusts ("REITs") are endlessly inventive. They were first developed in the 1960s as a means for ordinary retail investors to hold interests in real estate. The REIT market has waxed and waned over the years. During the early years of the Great Recession, 2008-2009, REITs surged in popularity due to their dividend yields. Recently, REITs have underperformed the broader market due, in part, to the perception that rising interest rates will negatively impact REITs or narrow yields. However, fundamentals across most REIT sectors remain strong.

REIT market participants have built a REIT portfolio from the ground up, or have converted existing organizations into REITs. Both new REITs and existing REITs have filed registration statements with the Securities and Exchange Commission ("SEC") for proposed initial public offerings ("IPOs").

A REIT is an investment vehicle designed to allow investors to pool capital to invest in real estate assets. It has certain advantages over other investment vehicles; in particular, a REIT is not subject to U.S. federal income tax on the taxable income that it distributes to shareholders even if its equity is publicly traded. REITs remain attractive to investors for this reason, despite the impact of the recently enacted tax code reform. Investors seeking current distributions choose to invest in REITs because REITs must distribute 90% of their taxable income in order to maintain REIT status. REITs generally finance their activities through equity and debt offerings. Although there is an active private market for REIT securities, REIT sponsors often have chosen to pursue IPOs.

The industry and asset focus of REITs is diverse. Most broadly, there are (i) equity REITs that own primarily interests in real property and (ii) mortgage REITs that own primarily loans secured by interests in real property. Equity REITs typically lease their properties to end users and tend to concentrate on a market segment, such as office, retail, industrial, single- or multi-family housing, self-storage, healthcare, lodging, data centers or farmland. Mortgage REITs may also have a focus on particular types of loans (first mortgages, distressed property mortgages, mezzanine financings) or borrowers. Hybrid REITs are relatively rare and own a combination of equity and mortgage interests in real property. At December 31, 2017, there were 181 equity REITs with equity market capitalization of $1.07 trillion and 41 mortgage REITs with equity market capitalization of $67.75 billion (Source: NAREIT®).

### 2016
Three REIT IPOs raised approximately $1.6 billion of gross proceeds

### 2017
Nine REIT IPOs raised approximately $2.9 billion of gross proceeds

Source: NAREIT®.

**ADVANCE PLANNING**

Most companies must make legal and operational changes before proceeding with an IPO. A company cannot wait to see if its IPO is likely to be successful prior to implementing most of these changes. Many corporate governance matters (including those arising under the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley")) and federal securities law requirements (including audited financial statements), as well as applicable securities exchange requirements, must be met when the IPO registration statement is confidentially submitted or filed with the SEC, or the company must commit to satisfy them within a set time period.

A company proposing to list securities on a securities exchange should review the governance requirements of the different exchanges, as well as their respective financial listing requirements, before determining which exchange to choose. Although most REITs list on the New York Stock Exchange, a company proposing to list its securities may choose to list elsewhere for business or other reasons. A company must also address other corporate governance matters, including board structure, committees and member criteria, related party transactions and director and officer
MoFo’s Quick Guide to REIT IPOs

UPREITs AND ROLL-UPS

UPREITs

The most common operating structure for publicly traded equity REITs is the umbrella partnership real estate investment trust (“UPREIT”) structure. In the typical UPREIT, the partners or members of entities holding real estate assets and a newly formed REIT become partners in an operating partnership subsidiary of the REIT (the “Operating Partnership”) through which the REIT’s real estate assets are held and substantially all of the REIT’s operations are conducted. For their respective limited partnership interests in the Operating Partnership (“OP units”), the partners contribute the real estate assets owned by them or their interests in the entities that own such real estate assets, and the REIT contributes the cash net proceeds from its initial public offering in exchange for a number of OP units equal to the number of shares sold in the IPO. The REIT typically is the general partner of the Operating Partnership and the majority owner of the OP units. Determining the value of the contributed assets and the allocation of the OP units being issued as consideration to the property contributors often involves significant analysis and negotiation. The UPREIT structure provides contributors deferral of their taxable gain while providing a kind of “on demand” liquidity to OP unit holders. After a period of time (typically one year), the limited partners may enjoy similar liquidity as the REIT’s shareholders by tendering their OP units for either cash or REIT shares (at the option of the REIT or Operating Partnership). This redemption will result in the limited partners incurring the tax that was deferred at the effective time of the contribution to the Operating Partnership. The OP unit holders may tender their OP units over time, thereby spreading out their tax liability. In addition, when an individual partner holds the OP units until death, the estate tax rules generally allow for a “step up” in tax basis of the OP units, effectively permitting the beneficiaries subsequently to tender the OP units for cash or REIT shares without incurring tax on the built-in gain in the OP units at the time of death.

ROLL-UPS

A REIT can either acquire a property or mortgage loan or other real estate asset directly or through a “roll-up” process in which the REIT acquires the entities (partnerships or limited liability companies) that own the real estate asset in exchange for securities of the REIT or its Operating Partnership. As noted above, the UPREIT structure provides tax deferral advantages. From the securities side of the transaction, the question is whether the REIT is conducting an offering of its securities to the holders of the interests in the entities. The REIT could effect the roll-up transaction as a registered offering of its securities to the holders of the interests in the entities. This process requires careful structuring, and, in the past, the private placement process had to be essentially complete before the IPO was publicly filed. The concern was that the private offering of the OP units in a roll-up transaction could be integrated with the REIT IPO and could lead to application of the SEC roll-up rules (as discussed below) and securities liability for failure to register the OP units.

In the late 1980s and early 1990s, in response to concerns about sponsor abuses in structuring public real estate roll-ups, the U.S. Congress and California passed specific roll-up legislation, the SEC issued targeted roll-up disclosure requirements and the National Association of Securities Dealers (now the Financial Industry Regulatory Authority, or “FINRA”) issued roll-up guidelines, all of which were designed both to give investors necessary information about the transaction and to lessen the coercive effects of the offering. The SEC definition of a “roll-up transaction” has specific exclusions that often now are relevant. But if the exclusions are not applicable, in addition to the requirements of Form S-11 and SEC Industry Guide (“Guide 5”), the SEC will require significant additional disclosure, including about the properties being contributed (including separate supplements for each partnership); additional risk factors and disclosures regarding conflicts of interest; statements as to the fairness of the transaction to the investors in the partnerships, including whether fairness opinions are being rendered; explanation of the allocation of the roll-up consideration and pro forma financial information.

If the transaction is a limited partnership roll-up, in addition to the requirements of Form S-11 and Guide 5, Section 14(h) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and Items 902 through 915 of Regulation S-K will require significant additional disclosure on an overall and per-partnership basis, addressing changes in the business plan, voting rights, form of ownership interest, the compensation of the general partner or another entity from the original limited partnership, additional risk factors, conflicts of interest of the general partner and statements as to the fairness of the proposed roll-up transaction to the investors, including whether there are fairness opinions, explanations of the allocation of the roll-up consideration (on a general and per-partnership basis), federal income tax consequences and pro forma financial information.

There have been few public roll-up transactions in recent years, and most roll-up transactions currently are conducted as private placements, particularly following the SEC’s 2007 interpretive guidance (Release No. 33-8828) on public/private integration issues. The rules promulgated under the Jumpstart Our Business Startups Act (“JOBS Act”) that allow general solicitation and advertising in certain private securities offerings under Rule 506 and Rule 144A so long as the securities are sold to accredited investors or qualified institutional buyers (“QIBs”) also lessen the securities law integration risk.

Any roll-up transaction, whether or not it meets the SEC and FINRA definitions, will have complex accounting and structuring issues that must be addressed with the accountants and counsel early in the IPO planning process, including relating to predecessor presentation and pro forma issues.
liability insurance. The company should undertake a thorough review of its compensation for its directors and officers as well, particularly its use of stock-based compensation.

Most public REITs are organized in Maryland as either corporations or trusts because Maryland has a special REIT law and has a well-developed history as a REIT-focused jurisdiction. This is in contrast to operating companies, which typically incorporate in Delaware if they are preparing for an IPO.

**Primary and Secondary Offerings**

An IPO may consist of the sale of newly issued shares by the company (a “primary” offering), a sale of shares owned by existing shareholders (a “secondary” offering) or a combination of these. Underwriters may prefer a primary offering because the company will retain all of the net proceeds to acquire additional assets, to repay indebtedness or for other general corporate purposes. However, some IPOS include the sale of secondary shares, either in the initial part of the offering or as part of the underwriters’ option to purchase up to an additional 15% of the shares to cover over-allotments. An issuer must also consider whether any of its shareholders have registration rights that could require it to register shares held by existing shareholders in the IPO or thereafter, which could potentially put downward pressure on the share price in the aftermarket.

**Governance and Board Members**

A public company must comply with significant corporate governance requirements imposed by the federal securities laws and regulations and the regulations of the applicable securities exchanges, including with regard to the oversight responsibilities of the board of directors and its committees. A critical matter is the composition of the board itself. All exchanges require that, except under limited circumstances, a majority of the directors be “independent,” as defined by both the federal securities laws and regulations and exchange regulations. In addition, boards should include individuals with appropriate financial expertise and relevant real estate

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**EMERGING GROWTH COMPANIES (“EGCs”)**

The April 2012 JOBS Act amended the Securities Act and the Exchange Act to include a new type of issuer called an emerging growth company (an “EGC”). An issuer qualifies as an EGC if it has a total gross revenue of less than $1.07 billion (originally $1 billion, but adjusted for inflation in 2017) during its most recently completed fiscal year subject to inflationary adjustment by the SEC every five years. An issuer will not be able to qualify as an EGC if it first sold its common stock in an SEC-registered offering before December 8, 2011.

A company that elects to file as an EGC would benefit from the following:

- Disclosure of only two years of audited financials (instead of three);
- No requirement to include financial information in selected financial data or in Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) disclosure for periods before those presented for the IPO;
- Option to rely on certain scaled disclosures available to smaller reporting companies (such as for executive compensation); and
- Ability to test the waters with QIBs and institutional accredited investors to gauge interest before or after filing (See “The Pre-Filing Period” below).

Exemption from:

- The advisory vote on executive compensation (“say-on-pay”);
- The advisory vote on golden parachute payments;
- Disclosing the relationship between executive compensation and financial performance;
- Disclosing CEO pay-ratio;
- Auditor attestation of internal controls under Section 404 of Sarbanes-Oxley;
- Compliance with new or revised accounting standards until the date the standard becomes broadly applicable to private companies; and
- Any Public Company Accounting Oversight Board rules requiring audit firm rotation or modified audit report requirements unless the SEC determines it is necessary.

An issuer will remain an EGC until the earliest of:

- The last day of the first fiscal year after the issuer’s annual revenues exceed $1.07 billion;
- The last day of the fiscal year following the fifth anniversary of the issuer’s IPO;
- The date on which the issuer has, during the previous three-year period, issued more than $1 billion in non-convertible debt; and
- The date on which the issuer qualifies as a large accelerated filer.
industry experience, as well as an understanding of risk management issues and public company experience. A company should begin its search for suitable directors early in the IPO process even if it will not appoint the directors until the IPO is completed. The company can turn to its large investors as well as its counsel and underwriters for references regarding potential directors.

THE OFFERING PROCESS

The IPO process is divided into three periods:

- **The pre-filing period** between determining to proceed with an IPO and the actual filing of the IPO registration statement with the SEC; during this period, the company is in the “quiet period” and subject to potential limits on public disclosure relating to the IPO. This period typically commences when the lead investment banks have been mandated to lead the IPO.

- **The waiting or pre-effective period** between the SEC filing date and date on which the SEC declares the IPO registration statement “effective”; during this period, the company may make oral offers but may not enter into binding agreements to sell the offered security.

- **The post-effective period** between effectiveness of the IPO registration statement and the 25th day after effectiveness. During this period, the underwriters may sell the securities by delivering the prospectus contained in the IPO registration statement.

The Prospectus

The prospectus describes the offering terms, the anticipated use of proceeds, the company, its industry, business, management and ownership, and its results of operations and financial condition. Although it is principally a disclosure document, the prospectus also is crucial to the selling process. A good prospectus sets forth a compelling “investment proposition.”

As a disclosure document, the prospectus functions as an “insurance policy” of sorts in that it is intended to limit the issuer’s and underwriters’ potential liability to IPO purchasers. If the prospectus contains all SEC-required information, includes robust risk factors that explain the risks that the company faces, and has no material misstatements or omissions, investors will not be able to recover their losses in a lawsuit if the price of the stock drops following the IPO.

NON-TRADITIONAL REITs

Over the years, REITs have expanded to assets beyond office, retail, apartment or commercial buildings, such as timber and farmland, self-storage, document storage facilities, cell-phone towers, casinos, private correctional facilities and billboards.

On August 31, 2016, the Treasury Department published final regulations (the “Final Regulations”) adding clarity to what constitutes a “good” REIT real estate asset for purposes of the REIT rules. The Final Regulations flesh out the definition of “real property” contained in regulations promulgated in 1962 to include the types of property for which the IRS previously provided favorable private letter rulings. The Final Regulations define “real property” to include land, inherently permanent structures and structural components; specify certain assets that are per se “real property” for purposes of the REIT rules and adopt a framework using a facts and circumstances approach to determine whether other assets are real property. This guidance provided welcome certainty for REITs.

Because of the tax benefits of a REIT and the growing market for dividend-paying securities in a low-yield environment, there has been increased interest in REIT conversions by corporations and other business entities. However, due to the requirements to qualify as a REIT and to maintain REIT status as discussed below, converting into a REIT is a complicated process and requires careful consideration and significant restructuring. In addition, tax-free spin-offs of real estate in the form of a REIT by non-REIT businesses (for example, restaurant businesses that own their underlying real property) largely were curtailed with the enactment of the Protecting Americans from Tax Hikes Act (the “PATH Act”) in 2015.
A prospectus should not include “puffery” or overly optimistic or unsupported statements about the company’s future performance. Rather, it should contain a balanced discussion of the company’s business, along with a detailed discussion of risks and operating and financial trends that may affect its financial condition, results of operations and prospects.

SEC rules require a substantial number of specific disclosures to be made in the prospectus. Most new REITs will qualify as emerging growth companies (“EGCs”) and can take advantage of the scaled disclosure requirements available for smaller public reporting companies. Furthermore, and in contrast to the general requirements of Form S-1, Form S-11 and Industry Guide 5 contain detailed requirements regarding real estate ownership, investment policies, operating data, descriptions of the real estate and disclosure about the prior experience of sponsors and their affiliates.

Depending on the nature of the specific REIT—UPREIT, DownREIT, equity, mortgage, externally managed, self-managed, blind pool, etc.—there will be additional necessary disclosures. If the transaction meets the SEC definition of a “roll-up transaction,” there are further disclosure obligations (see “UPREITs and Roll-ups” on page 4).

In addition, the federal securities laws, particularly Rule 10b-5 under the Exchange Act, require that documents used to sell a security contain all the information material to an investment decision and do not omit any information necessary to avoid misleading potential investors. Federal securities laws do not define materiality; the basic standard for determining whether information is material is whether a reasonable investor would consider the particular information important in making an investment decision. That simple statement is often difficult to apply in practice.

Although the JOBS Act provides for certain reduced disclosure requirements for EGCs, an issuer should be prepared for a time-consuming drafting process, during which the issuer, investment bankers and their respective counsel work together to craft the prospectus disclosure.

INTERNALLY OR EXTERNALLY MANAGED REITs

A REIT can be either internally or externally managed. In a REIT with an internal management structure, the REIT’s own officers and employees manage the portfolio of assets. A REIT with an external management structure usually resembles a private equity style arrangement, in which the external manager receives both a fixed management fee and an incentive fee for managing the REIT’s portfolio of assets. The external manager provides day-to-day management of the REIT’s operations, a senior management team and appropriate support personnel. There is a continuing debate over which management method best serves shareholder interests. The controversy has centered on which method of management produces higher returns for investors, with some arguing that conflicts of interest underpinning compensation arrangements for external managers create incentives that may not be aligned with the interests of shareholders. Generally, the fixed management fee that an external manager receives is based on the asset value under management, which may create an incentive on the external manager’s part to purchase assets and incur leverage, while the incentive fee is based on income, total shareholder return or the sale of assets.

The Pre-Filing Period

The pre-filing period begins when the company and the lead underwriters agree to proceed with an IPO. During this period, key management personnel will generally make a series of presentations to the underwriters covering the company’s business and industry, market opportunities and financial performance. The underwriters will use these presentations as an opportunity to ask questions and establish a basis for their “due diligence” defense. In particular, underwriters will want to visit the most significant properties owned by equity REITs as well as to analyze the mortgage loan portfolios of mortgage REITs. From the first all-hands meeting forward, all statements...
concerning the company should be reviewed by the company’s counsel to ensure compliance with applicable rules. Communications by an issuer more than 30 days prior to filing a registration statement are permitted as long as they do not reference the securities offering. Statements made within 30 days of filing a registration statement that could be considered an attempt to condition the market or pre-sell the IPO may be considered an illegal prospectus, creating a “gun jumping” violation. This might result in the SEC delaying the IPO or requiring prospectus disclosures of these potential securities law violations. Press interviews, participation in investment banker-sponsored conferences and new advertising campaigns are generally discouraged during this period.

However, the JOBS Act has softened the gun-jumping fears. If the company is an EGC under the JOBS Act, it can engage in oral and written test-the-waters communications with certain sophisticated investors referred to as qualified institutional buyers (“QIBs”) and institutional accredited investors to gauge interest in the IPO during both the pre-filing period and after filing without being required to file written communications with the SEC. However, the SEC will ask to review copies of any written materials used for this purpose. Current market practice has been to use test-the-waters communications, which usually take place after the first confidential submission of the registration statement.

In general, at least four to six weeks will pass between the distribution of a first draft of the registration statement and its filing with, or confidential submission to, the SEC. To a large extent, the length of the pre-filing period will be determined by the amount of time required to prepare the required financial statements. An issuer may confidentially submit a draft registration statement for non-public review but must file its registration statements publicly at least 15 days prior to commencing the IPO road show. The confidential submission process allows an issuer to commence the SEC review process.

Non-traded REITs are REITs whose common stock is registered under the Securities Act of 1933, as amended (the “Securities Act”), but is not traded on a national securities exchange. A non-traded REIT’s securities usually have no secondary trading market, and their value does not typically change with the market. Because a non-traded REIT does not have to satisfy the earnings and capitalization requirements of a national securities exchange, they are particularly useful in blind pool capital raises where the specific real properties to be acquired are identified after the capital raise based on a predetermined investment strategy. Therefore, the reputation and past experience of the sponsor or the general partner is critical in such cases because an investor will make investment decisions based on that information. Additionally, offerings for non-traded REITs usually are done on a best-efforts basis.

In August 2012, FINRA alerted investors about the greater risks associated with non-traded REITs than traded REITS, noting the following risks:

- Distributions are not guaranteed and may exceed operating cash flow.
- Lack of a public trading market creates illiquidity and valuation complexities.
- Early redemption is often restrictive and may be expensive.
- High front-end fees that can be as much as 15% of the per share price.

The SEC Staff has also expressed concern about the valuation of non-traded REITs and has also issued guidance regarding distributions, dilution, redemptions, disclosures, and estimated value per share.

On April 11, 2016, FINRA adopted amended rules that changed the way that the per share value of a non-traded REIT is reported on its customer account statement in an effort to increase transparency. Statements can now either list the purchase price less any fees or commissions or sponsors can list an appraised value of the security. Previously, it was common for statements to only show a gross purchase price. Additionally, appraised value must be based on a third-party annual valuation of the non-traded REIT’s underlying assets.
In general, a REIT is able to offer publicly traded equity through an IPO without altering the tax treatment of the REIT. The issuer and underwriter will need to perform a substantial amount of due diligence to confirm that the issuer is and will be eligible to be taxable as a REIT, including confirmation that the issuer will satisfy applicable shareholder composition, asset, income and distribution requirements. If the issuer qualifies as a REIT, its income generally will not be subject to tax at the REIT level to the extent distributed to shareholders. Instead its shareholders generally will be taxed on amounts distributed by the REIT. Ordinary REIT dividends generally are taxable to domestic shareholders as ordinary income. However, with the recent enactment of the Tax Cuts and Jobs Act, individual REIT shareholders generally can deduct 20% of the aggregate amount of ordinary dividends distributed by a REIT, subject to certain limitations, which reduces the effective tax rate for individuals on the receipt of such ordinary dividends from a maximum federal income tax rate of 37% to a maximum federal income tax rate of 29.6%.

As alluded to, in order to maintain REIT qualification, a REIT must satisfy several tests regarding the nature and value of its assets. Generally, these tests must be satisfied at the end of each calendar quarter of each tax year of the REIT, subject, in certain circumstances, to a 30-day grace period. At least 75% of a REIT’s assets must consist of “real estate assets” (such as ownership or leasehold interests in real property or mortgages), cash, cash items and government securities. No more than 20% of the value of a REIT’s total assets can consist of securities of a taxable REIT subsidiary (a “TRS”), which is a wholly owned subsidiary of a REIT that is taxed as a regular C corporation. No more than 5% of the value of the REIT’s assets may consist of the securities of any one issuer, other than a TRS, and a REIT may not hold more than 10% of the voting power or value of the securities of any one issuer (other than a TRS).

At least 75% of a REIT’s gross income must be attributable to real property, such as “rents from real property.” In addition, at least 95% of a REIT’s gross income must consist of income items qualifying for the 75% income test as well as dividends, non-mortgage interest and gain from sales of stock and securities. Thus, only 5% of a REIT’s gross income can come from categories (such as service income) not qualifying for the 75% or 95% income tests.

In general, a REIT must make qualifying distributions equal to 90% of its taxable income in order to maintain its REIT qualification, although in practice REITs typically distribute in excess of their taxable income.

If a REIT engages in a prohibited transaction, the gains from that transaction are subject to a 100% tax. A prohibited transaction is the sale or other disposition of property held primarily for sale to customers in the ordinary course of business, commonly referred to as “dealer” property. REITs can avoid prohibited transactions by ensuring that any potential transactions meet certain “safe harbor” requirements.

In the process of converting from a corporation to a REIT, built-in gains with respect to assets transferred from the corporation to the REIT may be subject to tax. The direct or indirect transfer of property by a regular C corporation to a REIT will cause the REIT to be taxable as a regular C corporation on any net built-in gain of the property transferred to the REIT if such property is sold during the 5-year period following the date of transfer. Similar rules may apply to a partnership that transfers property to a REIT if the partnership has direct or indirect corporate partners.

Careful tax planning is required to address these concerns.

RIDEA

The REIT Investment Diversification and Empowerment Act of 2007 (“RIDEA”) was signed into law in July 2008, enabling health care REITs to structure their investments similar to hotel REITs. Rent received from a corporation in which a REIT owns 10% or more of the total voting power or total value of shares is excluded as “rent from property” under the income tests described above. Hotel REITs are exempt from this rule if they use an eligible independent contractor to manage the hotel facilities. After the enactment of RIDEA, health care REITs are similarly exempt.
**REG A OFFERINGS FOR REITs**

In June 2015, the final rules implementing Title IV of the JOBS Act became effective. These rules provide an exemption for U.S. and Canadian companies that are not required to file reports under the Exchange Act to raise up to $50 million in a 12-month period in Regulation A offerings. The rules create two offering tiers: Tier 1 for smaller offerings raising up to $20 million in any 12-month period and Tier 2 for offerings raising up to $50 million. The rules modernize the Regulation A framework by, among other things, requiring that disclosure documents be filed on EDGAR, allowing an issuer to make a confidential submission with the SEC, permitting test-the-waters communication, and disqualifying bad actors. The rules impose different disclosure requirements for Tier 1 and Tier 2 offerings, with more disclosure required for Tier 2 offerings, including audited financial statements. Tier 1 offerings are subject to both SEC and state blue sky, pre-sale review. Tier 2 offerings are subject to SEC, but not state blue sky pre-sale review; however, investors in Tier 2 offerings are subject to investment limits (except when securities are sold to accredited investors or are listed on a national securities exchange). Following the completion of the Regulation A offering, Tier 2 issuers are required to comply with periodic filing requirements, which include a requirement to file current reports upon the occurrence of certain events, semi-annual reports and annual reports. A Tier 2 issuer may concurrently list a class of securities on a national exchange through a short-form Form 8-A, without filing a separate registration statement on Form 10. Regulation A offerings have proven to be a popular capital-raising alternative for real estate-related companies, including REITs. Of the 307 qualified Regulation A offerings as of December 31, 2017, 35 were REITs and 79 were real estate-related businesses that did not intend to qualify as REITs.

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**The Waiting Period**

**Responding to SEC Comments on the Registration Statement**

The SEC targets 30 calendar days from the registration statement filing or confidential submission date to respond with comments. It is not unusual for the first SEC comment letter to contain a significant number of comments that the issuer must respond to both in a letter and by amending the disclosures in the registration statement. After the SEC has provided its initial set of comments, the issuer and the underwriters often will have more clarity with respect to when the registration process is likely to be completed and the road show can commence. In most cases, offering participants delay the offering process and avoid distributing a preliminary prospectus until all material changes suggested by the SEC Staff have been addressed.

**Preparing the Underwriting Agreement, the Comfort Letter, and Other Documents; FINRA Filings**

During the waiting period, the issuer, the underwriters and their respective counsels and the company’s independent auditor will negotiate a number of agreements and other documents, particularly the underwriting agreement and the auditor’s “comfort letter.”

The purpose of the “comfort letter” is to assist the underwriters in establishing their due diligence defense against potential liability under the federal securities laws with respect to financial information included in the prospectus. In the comfort letter, the auditor affirms (i) its independence from the company and (ii) the compliance of the financial statements with applicable accounting regulations and SEC rules.

The auditor also will note period-to-period changes in certain financial items. These statements follow prescribed forms and are usually not the subject of significant negotiation. The underwriters will also usually require that the auditor undertake certain “agreed-upon” procedures, which can be subject to significant negotiation, in which it compares financial information in the prospectus (outside of
the financial statements) to the issuer’s accounting records to confirm its accuracy.

Marketing the Offering

During the waiting period, marketing begins. The only written sales materials that may be distributed during this period are the preliminary prospectus (which must include an estimated price range for the IPO); additional materials known as “free writing prospectuses,” which must satisfy specified SEC requirements, and any EGC test-the-waters communications described above. While binding commitments cannot be made during this period, the underwriters will receive indications of interest from potential investors, indicating the price they would be willing to pay and the number of shares they would purchase at various price levels. Once SEC comments are resolved, or it is clear that there are no material open issues, the issuer and underwriters will undertake a one-to-two-week “road show,” during which company management will meet with prospective investors. As noted above, an issuer must publicly file the confidentially submitted registration statement, along with any amendments, at least 15 days before commencing the road show.

Once SEC comments are cleared and the underwriters have assembled indications of interest for the offered securities, the company and

EXECUTIVE COMPENSATION MATTERS

Well before its IPO, an issuer should begin to approach executive compensation as would a public company. The IPO registration statement requires the same enhanced executive compensation disclosures that public companies provide in their annual proxy statements, including a discussion of compensation philosophy, an analysis of how compensation programs implement that philosophy and a discussion of the effects of risk taking on compensation decisions. In mortgage REITs and REITs that are not self-managed or self-administered, the REIT will also be required to provide extensive disclosure of both the compensation paid to the managers and the process to manage conflicts of interest. Under the JOBS Act, an EGC is required to include only summary compensation information in the IPO registration statement rather than the more extensive discussion and analysis of compensation required for a non-EGC. However, an EGC should always keep in mind that it may be required to include more substantial executive compensation disclosure in future filings.

Issuers contemplating an IPO should consider:

• **Systematizing compensation practices.**
  Compensation decisions should be made more systematically—doing so will require:
  - establishing an independent compensation committee of the board of directors;
  - using more formal market information to set compensation, which often can be achieved by engaging a compensation consultant familiar with the REIT industry; and
  - establishing a regular compensation grant cycle.

• **Confirming accounting and tax treatment.** The issuer should be sure that the Internal Revenue Code (“Code”) Section 409A valuation used to establish stock value for stock option purposes is consistent with that used for financial accounting purposes. The issuer also should consider whether to limit option grants as the IPO effective date approaches.

• **Complying with securities laws.** The issuer should confirm that equity grants were made in compliance with federal and state securities rules, including Rule 701 of the Securities Act limits, to avoid rescission or other compliance concerns.

• **Adopting plans.** An issuer will have greater flexibility to adopt equity compensation plans (including employee stock purchase plans) prior to its IPO. Accordingly, planning ahead is essential. An issuer should adopt the plans it thinks it may need during its first few years of life as a public company and reserve sufficient shares for future grants. Public companies are required to obtain shareholder approval for new equity compensation plans and material amendments. Certain awards (both equity and cash) made under plans adopted pre-IPO may also qualify for IPO transition relief under Code Section 162(m).

• **Establishing a DRIP.** Since REITs typically must pay dividends, in order to recapture a portion of such amounts and raise additional capital, many REITs adopt Dividend Reinvestment or Stock Repurchase Plans, or DRIPs.
its counsel will request that the SEC declare the registration statement “effective” at a certain date and time, usually after the close of business of the U.S. securities markets on the date scheduled for pricing the offering.

The Post-Effective Period
Once the registration statement has been declared effective and the offering has been priced, the issuer and the managing underwriters execute the underwriting agreement, and the auditor delivers the executed comfort letter. This occurs after pricing and before the commencement of trading on the following day. Within two business days of pricing the IPO, the company must file a final prospectus with the SEC that contains the final offering information.

On the second or third business day following pricing, the closing occurs, the shares are issued and the issuer receives the net proceeds (after underwriting discounts and commission and expenses payable by the issuer). The closing completes the IPO process. Then, for the following 25 days, aftermarket sales of shares by dealers must be accompanied by the final prospectus or a notice with respect to its availability. If during this period there is a material change that would make the prospectus misleading, the company must file an amended prospectus.

THE UNDERWRITER’S ROLE
A company will identify one or more investment banks that will act as lead underwriters that will be responsible for the IPO. A company chooses an underwriter based on its industry expertise, including the knowledge and following of its research analysts, the breadth of its distribution capacity and its overall reputation. A company should consider the underwriter’s commitment to the sector and its distribution strengths.

For example, does the investment bank have a particularly strong retail distribution network, or is it focused on institutional distribution? Is its strength domestic, or does it have foreign distribution capacity? The company may want to include a number of co-managers in order to balance the respective strengths and weaknesses of the underwriting syndicate.

A company should keep in mind that underwriters have at least two conflicting responsibilities—to sell the IPO shares on behalf of the company and to recommend to potential investors that the purchase of the IPO shares is a suitable and a worthy investment. In order to better understand the company—and to provide a defense in case the underwriters are sued in connection with the IPO—the underwriters and their counsel are likely to spend a substantial amount of time performing business, financial and legal due diligence in connection with the IPO; visiting the properties and making sure that the prospectus and any other offering materials are consistent with the information provided. The underwriters will market the IPO shares, set the price (in

THE MAGIC PAGE
The “Magic Page” is where a REIT discloses its dividend policy and distribution plans using a pro forma presentation that shows anticipated dividend payouts relative to cash available for distribution. The issuer, the underwriters and their respective advisors should begin contemplating the Magic Page presentation early in the IPO process to give the SEC ample time to review the issuer’s presentation and avoid SEC comments challenging the presentation closer to the launch of the road show.

The SEC has provided several comments addressing acceptable content for the Magic Page, including the application of both U.S. Generally Accepted Accounting Principles (“GAAP”) and non-GAAP financial measures. For more information about non-GAAP financial measures, please see our publications, Non-GAAP Explained, Practice Pointers on Non-GAAP Financial Measures and Practice Pointers on Anticipating and Addressing SEC Comments on Non-GAAP Financial Measures.
## SEQUENCING KEY EVENTS

**6-12 months before IPO**
- Company rounds out management team (if needed)
- Focus on “corporate cleanup”
- Identify real estate assets that may be acquired

**3-4 months before IPO**
- Company decides formally to undertake IPO
- Appoint the lead underwriter(s)
- Publicity restrictions commence
- Finalize structure — UPREIT, DownREIT, etc.
- Analyze valuation of real estate assets
- Begin process to effect private roll-up transaction, if applicable

**1-2 months before first SEC filing**
- Conduct due diligence
- Commence prospectus drafting
- Complete audit of full-year financial statement and review of interim financial statements
- Complete required audits of significant assets or businesses acquired or to be acquired in accordance with Rules 3-14 and 3-05, respectively, of Regulation S-X
- Conduct test-the-waters meetings

**Initial SEC filing or confidential submission**
- File Form S-11 with the SEC or submit confidentially to the SEC and submit application to an exchange

**Typically 2-3 months after first filing**
- Adopt public company policies, controls, procedures and other corporate governance matters if not already done
- Resolve material SEC comments
- Obtain listing approval from a national securities exchange
- Bulk print preliminary (“red”) prospectus

**No later than 15 days prior to commencement of the road show**
- Publicly file registration statement

**Typically 1-2 weeks**
- Road show

**Transaction Effective**
- Form S-11 declared effective
- Price deal and begin trading on an exchange
- Close IPO and related contribution transactions 2-3 days after pricing

Consultation with the company) at which the shares will be offered to the public and, in a “firm commitment” underwriting, purchase the shares from the company (at a discount) and then re-sell them to investors. In order to ensure an orderly market for the IPO shares, after the shares are priced and sold, the underwriters are permitted in many circumstances to engage in certain stabilizing transactions to support the stock. Typically, the company will grant the underwriters a 30-day option to purchase up to an additional 15% of the shares offered in the IPO (at the IPO price, less discounts and commissions) to cover over-allotments resulting from selling more shares in the IPO than they are required to purchase from the company. “Covered” short sales are sales made in an amount not greater than the underwriters’ overallotment option described above. The underwriters may close out any covered short position by either exercising their overallotment option or purchasing shares in the open market.

**SEC GUIDANCE**
As discussed under “UPREITS and Roll-ups” elsewhere in this Guide, REIT formation transactions can be complex, resulting in significant accounting issues. The SEC is available to discuss these accounting and structuring issues even in advance of a confidential submission or filing of a registration statement, and it is advisable to approach the SEC early in the process to avoid costly delays.
NYSE vs. NASDAQ: Principal Quantitative Listing Requirements

The following table summarizes the principal quantitative listing requirements; there are also qualitative requirements. The overwhelming majority of REITs list on the NYSE.

<table>
<thead>
<tr>
<th>SELECTED LISTING REQUIREMENT</th>
<th>NYSE</th>
<th>NASDAQ GLOBAL MARKET</th>
</tr>
</thead>
<tbody>
<tr>
<td>Minimum Number of Shareholders</td>
<td>400 round lot holders</td>
<td>Same¹</td>
</tr>
<tr>
<td>Minimum Number of Publicly Held Shares</td>
<td>1,100,000²</td>
<td>Same, with similar exclusions</td>
</tr>
<tr>
<td>Minimum Aggregate Market Value of Publicly Held Shares</td>
<td>$40 million</td>
<td>Any of: • $8 million under the Income Standard; • $18 million under the Equity Standard; or • $20 million under the Market Value Standard³ or the Total Assets/Total Revenue Standard.⁴</td>
</tr>
<tr>
<td>Minimum Price per Share</td>
<td>At least $4.00 at initial listing</td>
<td>Same⁵</td>
</tr>
<tr>
<td>Minimum Number of Market Makers</td>
<td>N/A</td>
<td>Four, unless company qualifies for listing under the Income or Equity Standards, which each require three.⁶</td>
</tr>
<tr>
<td>Minimum Financial Standards</td>
<td>One of the following: • Earnings Test: Adjusted pre-tax earnings from continuing operations must total (1) $10 million for the last three fiscal years,⁸ including a minimum of $2 million in each of the two most recent fiscal years and positive amounts in all three years, or (2) if there is a loss in the third fiscal year, $12 million for the last three fiscal years, including a minimum of $5 million in the most recent fiscal year and $2 million in the next most recent fiscal year;⁹ or • Global Market Capitalization Test: $200 million in global market capitalization (existing public companies must meet the minimum global market capitalization for a minimum of 90 consecutive trading days prior to listing on the NYSE); or • REIT Test:¹⁰ $60 million in stockholders’ equity.</td>
<td>One of the following:⁷ • Income Standard: (1) $1 million in annual pre-tax income from continuing operations in most recently completed fiscal year or in two of the three most recently completed fiscal years; and (2) stockholders’ equity of $15 million; or • Equity Standard: (1) stockholders’ equity of $30 million; and (2) two-year operating history; or • Market Value Standard: N/A for IPOs; or • Total Assets/Total Revenue Standard: total assets + total revenue of $75 million each for the most recently completed fiscal year or two of the three most recently completed fiscal years.</td>
</tr>
</tbody>
</table>

1. For the Nasdaq Global Select Market, at least 550 total holders and an average monthly trading volume over the prior 12 months of at least 1,100,000 shares; or at least 2,200 total holders; or a minimum of 450 round lot holders. For the Nasdaq Capital Market, a minimum of 300 round lot holders.
2. The number of shareholders includes shareholders of record and beneficial holders of shares held in street name. Shares held by directors, officers or immediate families and other concentrated holdings of 10% or more are excluded.
3. Market Value Standard is not applicable to IPOs.
4. For the Nasdaq Global Select Market, $45 million. For the Nasdaq Capital Market, $15 million under the Equity or the Market Value of Listed Securities Standards and $5 million under the Net Income Standard.
5. For the Nasdaq Capital Market, $4 bid price or $2 closing price under certain conditions.
6. For the Nasdaq Capital Market, three.
7. The other tiers (Nasdaq Global Select Market and Nasdaq Capital Market) have different requirements.
8. Under certain circumstances, a company may qualify with $10 million in aggregate for two years and nine months.
9. A company that qualifies as an EGC and avails itself of the provisions of the Securities Act and the Exchange Act permitting EGCs to report only two years of audited financial statements can qualify under the Earnings Test by meeting the following requirements: Pre-tax earnings from continuing operations, as adjusted, must total at least $10 million in the aggregate for the last two fiscal years together with a minimum of $2 million in both years.
10. Only for REITs with less than three years of operating history.
FINANCIAL REPORTING AND ACCOUNTING

The IPO registration statement must include audited financial statements for the last three fiscal years (two years for EGCs); financial statements for the most recent fiscal interim period, compared with interim financial information for the corresponding prior fiscal period (may or may not be audited depending on the circumstances) and income statement and condensed balance sheet information for the last five years (the earliest two years may be derived from unaudited financial statements) and interim periods presented. The SEC also requires special income statement and balance sheet captions for REITs.

Often, a REIT may not be able to provide full financial statements with respect to significant real estate assets or businesses to be acquired. For most equity REITs, the SEC will require audited statements of revenue and certain expenses (i.e., 3-14 financial statements) with respect to significant real estate assets to be acquired; however, some REITs must prepare audited financial statements in accordance with Rule 3-05 of Regulation S-X, which is required when an issuer acquires a significant business. For instance, lodging REITs must prepare audited financial statements with respect to the hotels they acquire.

If an issuer is unable to prepare the necessary financial statements, the issuer should seek relief from the SEC in the form of a “pre-clearance” letter, which may result in the SEC allowing the issuer to include more limited financial information than would otherwise be required under the SEC’s rules.

Early on, the issuer should identify any problems associated with providing the required financial statements (including any complex predecessor
MoFo’s Quick Guide to REIT IPOs

analysis or similar issues in a “roll-up” IPO) in order to seek necessary accommodations from the SEC. These statements must be prepared in accordance with GAAP, as they will be the source of information for the MD&A.

EGC TRENDS

Now that the JOBS Act is more than five years old, some trends in EGC IPOs have become apparent. Some EGCs are not taking full advantage of the various accommodations. In 2016:

- Approximately 83% of EGC IPOs have taken advantage of the confidential review process;
- Approximately 58% of EGC registration statements included only two years of audited financial statements and selected financial data (not including EGCs that are also smaller reporting companies or who do not have two years of reporting history); and
- Approximately 72% of EGC registration statements excluded a compensation discussion and analysis (not including EGCs that are also smaller reporting companies).

EGCs are taking advantage of the ability to use test-the-waters communications while broker-dealers are still generally not publishing research reports during the registration process or during the customary 25-day post-closing “quiet period.” In addition, most REIT EGCs elect to comply with new or amended financial accounting standards.

In 2017, real estate companies accounted for 6.4% and 8.6% of EGC IPOs based on the number of IPO offerings and total dollar offering amount, respectively.

Source: CCH IPO Vital Signs

Additionally, an EGC may omit financial information for historical periods that otherwise would be required by Regulation S-X at the time of filing or submission, provided that the omitted financial information will not be required to be included in the registration statement at the time of the consummation of the offering and that, prior to distribution of a preliminary prospectus to investors, the registration statement includes all required financial statements. In August 2017, the SEC Staff issued guidance clarifying that an EGC may omit from its draft registration statements interim financial information that it reasonably believes it will not be required to present at the time of the offering, but interim financial information that will be included in a historical period that a non-EGC reasonably believes will be required to be included at the time of its first public filing may not be omitted from its filed registration statements.

Measuring Performance

FFO

The real estate industry discloses a unique operating metric that the SEC traditionally has allowed. “Funds from Operations,” or FFO, is neither operating income nor cash flow from operations. The National Association of Real Estate Investment Trusts (“NAREIT”), the REIT industry’s primary trade association and advocate, has taken the lead in establishing a base definition of FFO since at least 1991, although many REITs disclose various forms of adjusted FFO. A typical FFO disclosure, reflecting the SEC focus on the purpose of the metric and comparability, follows:

“FFO is computed in accordance with the definition adopted by the Board of Governors of the National Association of Real Estate Investment Trusts (“NAREIT”). NAREIT defines FFO as GAAP net income or loss adjusted to exclude net gains from sales of depreciated real estate assets and real estate impairment losses, depreciation and amortization expense from real estate assets, extraordinary items and other specified non-cash items, including the pro rata share of such adjustments of unconsolidated subsidiaries. FFO and FFO per diluted share are non-GAAP financial measures used by management, investors and analysts to facilitate meaningful comparisons of operating performance between periods and among our peers because it excludes the effect of real estate depreciation and amortization and net gains on sales, which are based on historical costs and implicitly assume that the value of real estate diminishes predictably over time, rather than fluctuating based on existing market conditions. FFO does not represent cash generated from operating activities and is not necessarily indicative of cash available to fund cash requirements and should not be
considered as an alternative to net income as a performance measure or cash flows as a liquidity measure. FFO may not be comparable to similarly titled measures employed by other companies.”

Other Performance Measures

Most REITs now disclose a variety of non-GAAP financial measures such as net operating income (“NOI”), cash/funds available for distribution (“CAD/FAD”) or adjusted funds from operations (“AFFO”). NOI is the operating income after operating expenses but before income taxes and interest are deducted. CAD/FAD is used to measure a REIT’s ability to generate cash and to distribute dividends and is generally equal to FFO minus recurring capital expenditures. AFFO is equal to FFO after adjustments for certain non-comparable items. Depending on the adjustments, the AFFO calculation varies from company to company, which can make a comparability analysis difficult.

Additionally, mortgage REITs may use other non-GAAP financial measures such as “core earnings” (or other similarly titled measures). Core earnings is typically defined as net income (loss) excluding realized and change in unrealized gains (losses), gains (losses) on financial derivatives and any other nonrecurring items of income (loss). Core earnings and similar metrics are typically useful for mortgage REIT investors because they assess a mortgage portfolio’s performance by evaluating its effective net yield.

SEC Treatment of Non-GAAP Financial Measures

Regulation G requires issuers to include a reconciliation and general disclosure with respect to any non-GAAP financial measures that are publicly disclosed. The reconciliation requirement provides that whenever an issuer publicly discloses (whether in an SEC-filed report or in an earnings call or investor presentation) material information that includes a non-GAAP financial measure, it must accompany that non-GAAP financial measure with (i) a presentation of the most directly comparable financial measure calculated and presented in accordance with GAAP and

CONTROLLING YOUR SHARES AND LOCK-UPS

To provide for an orderly market and to prevent existing shareholders from dumping their shares into the market immediately after the IPO, underwriters will require the issuer as well as directors, executive officers and large shareholders (and sometimes all pre-IPO shareholders) to agree not to sell their shares of common stock, except under limited circumstances, for a period of up to 180 days following the IPO, effectively “locking up” such shares. Exceptions to the lock-up include issuances of shares in acquisitions and in compensation-based grants. Shareholders may be permitted to exercise existing options (but not sell the underlying shares), transfer shares to family trusts and sometimes make specified private sales, provided that the acquiror also agrees to be bound by the lock-up restrictions. These lock-up exceptions often will be highly negotiated.

Note that, in an UPREIT structure, the OP unit holders may also be locked up, but they may also be subject to a longer holding period before they can tender OP units for cash or shares (at the REIT’s election).

In connection with an IPO, the issuer may want the option to “direct” shares to directors, officers, employees and their relatives, or specific other designated people, such as vendors or strategic partners. Directed share (or “friends and family”) programs, or DSPs, set aside stock for this purpose, usually 5% to 10% of the total shares offered in the IPO. Participants pay the initial public offering price. Shares not sold pursuant to the DSP are sold by the underwriters.

Generally, directed shares are freely tradable securities and are not subject to the underwriter’s lock-up agreement, although the shares may be locked up for some shorter period. Each underwriter has its own program format. There are, however, guidelines that must be followed. The DSP is not a separate offering by the company but is part of the plan of distribution of the IPO shares and must be sold pursuant to the IPO prospectus.
(ii) a quantitative reconciliation of the differences between the non-GAAP financial measure and the most directly comparable GAAP financial measure.

On May 17, 2016, the SEC staff issued updated Compliance and Disclosure Interpretations (“CD&Is”) on the use of non-GAAP financial measures. The updated CD&Is included certain updates to the use of the FFO and AFFO performance metrics. The SEC staff stated that it continues to accept NAREIT’s definition of FFO, as in effect as of May 17, 2016, as a performance measure and does not object to such presentation on a per share basis. The SEC staff also stated that a REIT may present FFO on a basis other than as defined by NAREIT (such as AFFO), provided that any adjustments made to FFO must comply with the requirements of Item 10(e) of Regulation S-K for a performance measure or a liquidity measure. Depending on the nature of the adjustments, if FFO is presented or adjusted as a liquidity measure, then the presentation of FFO/AFFO on a per share basis is prohibited.

For more information, see our publications Non-GAAP Explained and Practice Pointers on Non-GAAP Financial Measures.

Internal Control over Financial Reporting
An issuer will not be required to include either a management’s report on its internal control over financial reporting or an auditor’s report on such internal control until the second annual report following its IPO. However, so long as the company is an EGC under the JOBS Act, it will be exempt from providing an auditor’s report on the effectiveness of such internal controls.

SEC COMMENTS
An integral part of the IPO process is the SEC’s review of the registration statement. Once the registration statement is filed or confidentially submitted, a team of SEC Staff members is assigned to review the filing. The team consists of accountants and lawyers, including examiners and supervisors. The SEC’s objective is to assess the company’s compliance with its registration and disclosure rules.

THE FAST ACT
Under the Fixing America’s Surface Transportation (FAST) Act, enacted in December 2015, an EGC can omit financial information for historical periods otherwise required to be submitted in its draft registration statement if it reasonably believes that such financial information will not be required at the time of the contemplated offering.

The Review Process
The SEC’s principal focus during the review process is on disclosure. In addition to assessing compliance with applicable requirements, the SEC considers the disclosures through the eyes of an investor in order to determine the type of information that would be considered material. The SEC’s review is not limited to just the registration statement. The SEC Staff will closely review websites, databases, and magazine and newspaper articles, looking in particular for information that the SEC Staff thinks should be in the prospectus or that contradicts information included in the prospectus.

The review process is time-consuming. While there was a time when the review process could be completed in roughly two months, now, given the length of the prospectus and the complexity of the disclosure, it can take two to four months. This depends on the complexity of the company’s business and the nature of the issues raised in the review process.

Initial comments on Form S-11 are typically provided in about 30 days—depending on the SEC’s workload and the complexity of the filing, the receipt of first-round comments may be sooner or later. The initial letter for REITs typically runs about 20 to 30 comments, with a significant number of the comments addressing accounting issues. The company and counsel will prepare a complete and thorough response. In some instances, the company may not agree with the SEC Staff’s comments and may choose to schedule calls to discuss the matter with the SEC Staff. The company will file or confidentially submit an
amendment revising the prospectus and provide the response letter along with any additional information. The SEC Staff generally tries to address response letters and amendments within 10 days, but timing varies considerably.

**Frequent Areas of Comment**

It is easy to anticipate many of the matters that the SEC will raise in the comment process. The SEC makes the comment letters and responses from prior reviews available on its website, so it is possible to determine the most typical comments raised during the IPO process.

Overall, the SEC Staff looks for a balanced, clear presentation of the information required in the registration statement. Some of the most frequent comments raised by the SEC Staff on disclosure, other than the financial statements, include:

- **Front cover and gatefold**: On the theory that “a picture is worth a thousand words,” does the artwork present a balanced presentation of the company’s business, properties or geographies?

- **Prospectus summary**: Is the presentation balanced? Is it too lengthy to provide a true summary of the disclosure found elsewhere in the prospectus?

- **Risk factors**: Are the risks specific to the company and devoid of mitigating language? The following are risk factors as to which recent SEC comments have been issued:
  - Specificity of the risk factor heading;
  - Adequate disclosure of the consequences if one or more risks were to be realized;
  - With respect to externally managed REITs, risks related to the external manager such as internalization of management functions or difficulty in terminating or not renewing the manager for poor performance;
  - Conflicts of interests;
  - Liquidity events;
  - Distributions paid in excess of earnings and cash flow;
  - Geographic or asset concentrations;
  - Any guarantee obligations in connection with

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**RULE 144 HOLDING PERIOD FOR OP UNITS**

On March 14, 2016, the SEC Staff issued interpretative guidance with respect to the required Rule 144 holding period following the redemption of OP units for shares of its parent REIT shares. Rule 144 provides a safe harbor from registration for the sale of restricted securities if certain conditions are satisfied, including a holding period requirement. The holding period requirement varies from six months to one year depending on whether the issuer has been subject to the reporting requirements of the Exchange Act during the preceding 90-day period. Generally, the holding period commences at the time a person acquires a security. However, the interpretative guidance clarifies that, for purposes of Rule 144(d)(1), the holding period for REIT shares issued in transactions consistent with certain conditions commences upon the earlier acquisition of the OP units. The conditions noted in the interpretive guidance include the following: (i) the OP unit holders paid the full purchase price for the OP units at the time they were acquired from the Operating Partnership; (ii) an OP unit is the economic equivalent of a REIT share, representing the same right to the same proportional interest in the same underlying pool of assets; (iii) the exchange of REIT shares for OP units is entirely at the discretion of the parent REIT; and (iv) no additional consideration is paid by the OP unit holders for the REIT shares.

As a result of the interpretive guidance, registration rights may no longer be necessary in many OP unit transactions because holders generally will be able to immediately sell any REIT shares received upon redemption of OP units. However, OP unit holders may still want registration rights, particularly if a significant number of OP units are being issued and the holders want the right to sell their shares in an underwritten offering or “piggyback” on an underwritten offering by the REIT. If OP units are being issued to affiliates, those affiliates also may want registration rights because they will still be subject to the volume limitation and manner of sale requirements under Rule 144. In addition, the interpretive guidance is limited solely to the UPREIT structure, as the SEC Staff did not address the ability to tack the Rule 144 holding period in other transaction structures, such as the DownREIT structure.
related financing transactions;
- Change of investment strategy and financing strategy without shareholder approval; and
- Identification of material weakness in internal controls.

- **Use of proceeds:** Is there a specific allocation of the net proceeds among identified uses, and, if funding acquisitions is a designated use, are acquisition plans identified? Will debt be repaid with all or a portion of the net proceeds?

- **Selected financial data and other financial information:** Does the presentation of non-GAAP financial measures comply with SEC rules?

- **MD&A:** Does the discussion address known trends, events, commitments, demands or uncertainties, including the impact of the economy, trends with respect to liquidity and critical accounting estimates and policies?

- **Business:** Does the company provide support for statements about market position and other industry or comparative data? Is the disclosure free of, or does it explain, business jargon? Are the relationships with customers and suppliers, including concentration risk, clearly described?

- **Management:** Is the executive compensation disclosure clear?

- **Prior performance information:** Is the description of prior performance by related real estate entities complete, responsive to disclosure requirements, and balanced?

- **Underwriting:** Is there sufficient disclosure about stabilization activities (including naked short selling), as well as factors considered in early termination of lock-ups and any material relationships with the underwriters?

- **Exhibits:** Do any other contracts need to be filed based on disclosure in the prospectus?

**A FINAL THOUGHT**

While windows open and close, and REITs and their advisors may have different views concerning the right moment to commence active and intense preparation for an IPO, it is rarely too early to undertake the advance planning described above. Much of this preparatory work is neither time-consuming nor expensive. Yet it will enhance greatly the opportunity to get into the market quickly when the opportunity arises. And even if an IPO does not turn out to be the option of choice, this preparatory work should prove valuable in facilitating other funding opportunities, or even acquisition by an existing public company.
### IPO ACCOMMODATIONS FOR EGCs

<table>
<thead>
<tr>
<th>AVAILABLE ACCOMMODATIONS</th>
<th>AN EGC</th>
<th>A NON-EGC</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Confidential submission?</strong></td>
<td>Yes, an EGC may submit its IPO registration statement to the SEC for confidential review as a result of JOBS Act provisions. Confidentiality is established by statute. <em>Securities Act Section 6(e)(2).</em></td>
<td>New policy allows a non-EGC to submit its registration statement to the SEC for confidential review. A non-EGC must request confidential treatment for its submission under Rule 83.</td>
</tr>
<tr>
<td><strong>When must registration statement be filed publicly?</strong></td>
<td>15 days prior to commencement of a traditional road show.</td>
<td>15 days prior to commencement of a traditional road show.</td>
</tr>
<tr>
<td><strong>Test-the-waters?</strong></td>
<td>Yes.</td>
<td>No.</td>
</tr>
<tr>
<td><strong>Disclosure accommodations?</strong></td>
<td>Yes. These are discussed earlier under “EGC Accommodations.”</td>
<td>No.</td>
</tr>
<tr>
<td><strong>Financial information that may be omitted?</strong></td>
<td>Confidential submissions may omit annual and interim financial statements that will not be required to be presented at the time of the offering.</td>
<td>In reliance on new guidance, confidential submissions may omit annual and interim financial statements that will not be required to be presented at the time of the first public filing.</td>
</tr>
<tr>
<td><strong>Governance and other SOX-related accommodations?</strong></td>
<td>Yes. These are discussed earlier under “EGC Accommodations.”</td>
<td>No.</td>
</tr>
</tbody>
</table>
### THE LIKELY ALTERNATIVES

A growing real estate company has a number of financing alternatives, in addition to a traditional firm commitment, underwritten IPO.

#### WHICH WAY TO GO?

<table>
<thead>
<tr>
<th>PRIVATE CAPITAL RAISE/BANK LOAN</th>
<th>PRIVATE SALE</th>
<th>DUAL-TRACK APPROACHES (IPO/PRIVATE SALE)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Benefits:</strong></td>
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<td><strong>Benefits:</strong></td>
</tr>
<tr>
<td>• Control</td>
<td>• Can be complete realization event</td>
<td>• Potential to maximize shareholder value</td>
</tr>
<tr>
<td>• Less or no dilution</td>
<td>• Avoids market instability</td>
<td>• More responsive to market conditions</td>
</tr>
<tr>
<td>• Less expensive and time-consuming</td>
<td>• No public obligations or expense</td>
<td></td>
</tr>
<tr>
<td>• No public obligations</td>
<td><strong>Considerations:</strong></td>
<td><strong>Considerations:</strong></td>
</tr>
<tr>
<td>• No acquisition “currency”</td>
<td>• Typically, no continuing involvement</td>
<td>• Unsuccessful sale could affect IPO valuation</td>
</tr>
<tr>
<td>• Limits equity compensation</td>
<td>by management and founders</td>
<td>• More time-consuming and expensive</td>
</tr>
<tr>
<td>• Investor pressure for realization event</td>
<td>• May be time-consuming and expensive</td>
<td></td>
</tr>
<tr>
<td>• No “public” profile or market following</td>
<td><strong>Benefits:</strong></td>
<td><strong>Considerations:</strong></td>
</tr>
<tr>
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</tr>
<tr>
<td><strong>ALTERNATIVE APPROACHES</strong></td>
<td><strong>Benefits:</strong></td>
<td><strong>Considerations:</strong></td>
</tr>
<tr>
<td>Reverse Merger IPO (merger into a public shell)</td>
<td>• Combination IPO and sale</td>
<td>• Has a bad reputation</td>
</tr>
<tr>
<td>Rule 144A IPO/“PIPO” (private IPO)</td>
<td>• SEC-style disclosure; no SEC review and delay</td>
<td>• Need to find “clean” public shell</td>
</tr>
<tr>
<td>Regulation A+ Offering (with exchange listing)</td>
<td>• Provides IPO on-ramp</td>
<td>• Attractive to smaller private companies</td>
</tr>
<tr>
<td>Spin-Off</td>
<td>• SEC-style disclosure; no SEC review and delay</td>
<td>• Limited to institutional investors</td>
</tr>
<tr>
<td></td>
<td>• Provides IPO on-ramp</td>
<td>• Available only to certain industry sectors</td>
</tr>
<tr>
<td><strong>Benefits:</strong></td>
<td>• Scaled SEC disclosure</td>
<td>• Delays but may not avoid public disclosure and other obligations</td>
</tr>
<tr>
<td>• SEC-style disclosure; no SEC review and delay</td>
<td>• Attractive to smaller private companies</td>
<td>• Blue Sky exemption only for Tier 2 offerings (up to $50 million)</td>
</tr>
<tr>
<td><strong>Considerations:</strong></td>
<td>• Scaled SEC disclosure</td>
<td>• Not available for certain companies (Exchange Act registrants, registered investment companies, business development companies, asset-backed issuers)</td>
</tr>
<tr>
<td>• Limited to institutional investors</td>
<td>• Attractive to smaller private companies</td>
<td>• Compliance with complex tax requirements and new restrictions</td>
</tr>
<tr>
<td>• Available only to certain industry sectors</td>
<td>• SEC process is substantially similar to IPO</td>
<td>• Recent change in law generally prohibits REIT tax-free spin-offs by non-REIT entities</td>
</tr>
<tr>
<td>• Delays but may not avoid public disclosure and other obligations</td>
<td>• All considerations of being public</td>
<td>• SEC process is substantially similar to IPO</td>
</tr>
</tbody>
</table>

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Because of the generality of this guide, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations.

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