REITs: You Might Want to Think Twice Before Buying

Description

There is a movement afoot here in Canada to improve the corporate governance of real estate investment trusts, so the unitholders of the 57 or so REITs that trade on the TSX are treated the same as shareholders of public companies.

It's common sense, right?

Yet most retail investors are woefully unaware of the fundamental lack of protection provided by REIT investments here in Canada. *The Financial Post* recently spoke to Stephen Erlichman, executive director of the Canadian Coalition for Good Governance (CCGG). He stated, "CCGG believes that unit holders of REITs and other public business trusts should have the fundamental rights and remedies that are available to shareholders of public corporations."

Basically, a REIT has a Declaration of Trust (DOT), which details an investor's rights when purchasing units of that REIT. For example, **H&R Real Estate Investment Trust** (TSX:HR.UN), one of the biggest REITs in Canada, has a 74-page DOT—light reading, it's not.

The CCGG first broached this subject back in 2007.

"CCGG's view was that the rights of investors in public income trusts should be standardized (which has been the case for corporations in Canada for decades) and that those rights should mirror, to the extent legally possible given the differences in legal form, the rights given to shareholders of corporations governed by the Canada Business Corporations Act," the corporate governance organization stated in its November 2015 position paper on DOTs.

According to the head of the CCGG, six out of 21 income trusts that make up the S&P/TSX Income Trust Index are moving to implement these best practices when it comes to corporate governance, including H&R and **RioCan Real Estate Investment Trust** (TSX:REI.UN).

That said, until they do, you might want to reconsider buying REITs, because in many cases you aren't currently afforded the same rights you would be if you owned **Brookfield Asset Management Inc.** or some other real estate corporation.

While corporate governance is a concern, a bigger issue investors might want to consider is overall suitability.

I get the fact that REITs generate good income—most yield 5% or more—but with 68% home ownership in this country, adding more of this asset class hardly seems wise at a time when home prices are starting to spin their wheels either through economic slowdowns (Alberta and Newfoundland) or by government intervention (15% foreign buyers' tax) as we've seen in B.C.

The average Canadian home price in July was $480,743. Statistics Canada suggests the typical Canadian has 73% equity in their home, which amounts to $351,000. Real estate represents 50% of the average Canadian's total assets.

So, if an investor brought $1 million to a financial advisor to invest and said, "I currently rent and don't plan to ever buy a home," I find it hard to believe that a competent investment professional would recommend putting 50% of that money into REITs. I just don't.

Yet here we sit with retail investors putting money into REITs when they've already got several hundred thousand dollars invested in real estate.

If the first point I've made doesn't deter you, the second should.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:HR.UN (H&R Real Estate Investment Trust)
2. TSX:REI.UN (RioCan Real Estate Investment Trust)

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