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CLIENT ALERT

# NASAA Proposes Changes to the REIT Guidelines

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On July 12, 2022, the North American Securities Administrators Association, Inc. ("NASAA") announced it is seeking public comment on proposed revisions to the NASAA Statement of Policy Regarding Real Estate Investment Trusts (the "REIT Guidelines"). NASAA is a membership organization of securities regulators of the 50 states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands, the 13 provinces and territories of Canada, and the country of Mexico. In addition to representing those regulators' interests and providing investor education, NASAA works to coordinate state regulation of broker-dealers, investment advisers and securities offerings. NASAA's Sections and Project Groups[1], made up primarily of employees of the member regulators, propose Statements of Policy and other guidance to be adopted by the NASAA membership for use by state regulators, including the REIT Guidelines.

Since 1996, the Securities Act of 1933, as amended, has provided a preemption of the substantive state securities law requirements for a number of types of securities and offerings. However, certain securities offerings, including publically offered real estate investment trusts that do not list their securities on a stock exchange ("non-traded REITs"), remain subject to state securities law registration requirements and to review by state securities regulators in addition to review

[1] The Corporation Finance Section ("Section") and the Direct Participation Programs Project Group ("Project Group") of NASAA have proposed these changes to the REIT Guidelines. See the Request For Public Comment here.

by the Securities and Exchange Commission (the "SEC"). The REIT Guidelines have been adopted by a number of state securities regulators or used by their staff in reviewing such offerings.[2]

The REIT Guidelines were last amended in 2007 and set out requirements for REIT sponsors, advisers and persons selling REITs including provisions dealing with suitability of investors, conflicts of interest, investment restrictions, and rights of shareholders as well as disclosure and marketing.

**Proposed Changes**

NASAA has proposed revisions to the REIT Guidelines in four areas:

(1) Adding a new Conduct Standard definition applicable to persons selling, recommending or providing investment advice concerning shares of non-traded REITs, which specifically includes the SEC's new Regulation Best Interest ("Reg BI") and other standards that may be adopted by other jurisdictions under federal or state law;[3]

(2) Increasing the investor net income and net worth suitability thresholds from the current (i) $70,000 of annual gross income and net worth of $70,000 or net worth of $250,000 to (ii) $95,000 of annual gross income and net worth of $95,000 or net worth of $340,000, to account for inflation occurring since last adjustment;

(3) Adding a new standardized concentration limit on the investment in the REIT, its affiliates or other non-traded direct participation programs of no more than 10% of the investor's liquid net worth to the suitability section.[4] Liquid net worth to be defined as net worth consisting of cash, cash equivalents, and readily marketable securities; and

(4) Adding a new prohibition against using gross offering proceeds to make distributions.

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[2] The REIT Guidelines are currently used by the securities regulators in Alabama; Arizona; Arkansas; Hawaii; Indiana; Iowa; Kansas; Massachusetts; Missouri; Nebraska; Nevada; New Mexico; North Carolina; North Dakota; Ohio; Oklahoma; Pennsylvania; South Dakota; Tennessee; Texas; Utah; Virginia; Washington; Wisconsin and Wyoming.

[3] The proposed revisions to the REIT Guidelines also add persons recommending or advising on non-traded REIT shares to those required to comply with investor suitability requirements and a prohibition of indemnification to associated persons, investment advisers or investment adviser representatives for violations of federal or state laws, and adding items such as "tax status," "investment time horizon," "liquidity needs," and "risk tolerance" to the items of information a financial professional should obtain for determining the suitability of the investor.

[4] A number of states currently impose their state-specific concentration limits which are similar but vary from state to state and in a number of cases are less restrictive than this new proposed limit. Non-traded REIT prospectuses include a section listing those for each state that imposes them. This proposal has no exception for investors that qualify as accredited investors under Regulation D as is the case with some state-specific standards.

In the request for comment NASAA points out that if adopted, the revisions to the REIT Guidelines have the potential to influence updates to other Guidelines, including those for Asset-Backed Securities, Commodity Pools, Equipment Leasing, Mortgage Programs and Real Estate Programs (other than REITs) and the Omnibus Guidelines.

The deadline for public comment is August 11, 2022. After reviewing the comments, the Section and Project Group will consider whether to present the proposed revisions to the REIT Guidelines, in their current or revised form, to the NASAA Board of Directors for potential adoption by vote of the NASAA membership.

If you have any questions regarding this client alert, please contact the following attorney or the attorney with whom you regularly work.

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