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REIT M&A, Activism and Governance – Ten Themes for 2018

Following are some of the key board-level themes we expect to continue playing out in 2018:

1. **Consolidation**. The steady aggregation of assets into larger REITs continues, not infrequently driven by activist pressure or technological disruption, but also by proactive strategic planning. Cross-border activity continues to be incremental and mostly episodic. REITs entering into deals should factor the potential for activist response into deal diligence and strategy.
2. **Activism**. Already a major factor in the retail sector (particularly with the recent entry of larger, non-REIT-dedicated activist funds), activist intervention is expected to expand to other REIT sectors, especially those with perceived NAV gaps, and to REITs with governance that doesn't comport with the expectations of the very large index investors that increasingly dominate the share registers of all REITs. Approaches for building thoughtful relationships with these investors that are focused on substance rather than check-the-box approaches are continuing to evolve.
3. **Technological Change**. Again most evident in the retail sector so far, but likely to expand to other sectors and potentially to require rethinking existing business models. This remains one of the key risks and opportunities to be managed by REIT boards. For the first time, four of the ten largest REITs are "tech-REITs".
4. **Shareholder Outreach**. Building strong relationships with major shareholders, a handful of whom are the biggest investors in most REITs and can determine the outcome of any vote – including in transactional or activist situations – has never been more important. Adverse proxy advisory firm recommendations will need to be managed effectively without letting ISS dictate what makes sense for the company. Most major institutional investors have made clear their commitment to a long term perspective and to a productive ongoing dialogue with senior REIT management and, as appropriate, directors.
5. **Long Term Strategy**. Regardless of the governance flavor of the day, the board's responsibility is to keep its eye on long-term strategy and value creation. Check-the-box governance prescriptions may affect various short-term "scores," but the board's core responsibility is to formulate and implement a long-term, sustainable strategy, vision, and corporate culture. Tone at the top matters.
6. **Executive Compensation**. Careful thought should be given to allowing board compensation committees greater discretion to reward outstanding performance, regardless of whether rigid mathematical targets are achieved. In too many cases, forces outside of the control of key executives, like macro trends that reduce TSRs, result in outperforming management teams being undercompensated. While the use of relative, rather than absolute, goals may be useful in this regard, outstanding REITs usually are a reflection of outstanding management, and a board's ability to attract, retain and motivate management should not be held hostage to rigid objective criteria.
7. **Succession Planning**. Few issues are more central to the board's long-term responsibilities than succession planning and implementation. A board will want to consider whether the successor CEO should be an insider or an outsider, whether the bench should be built out with an eye to succession, whether a "tournament approach" among two or more internal candidates is advantageous or whether it is best to pick a single candidate who can be groomed.

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8. Board Quality. Board quality, including composition, is an increasingly important issue, with particular focus on relevant expertise, average tenure, diversity and, of course, independence, in addition to the baseline requirements of character and integrity. Quotas and other formulaic approaches are often a disservice to REITs, and in most cases it is better to implement a more nuanced evaluation of the ongoing needs of the company, the experience, expertise and contributions of existing board members, and opportunities to strengthen the current composition. Conveying to investors the board's strength, involvement and quality, including through the annual proxy statement and other means, will remain important.
9. MUTA and Other Matters Maryland. The preponderance of Maryland-incorporated REITs continues to be a source of both strength and scrutiny. Careful attention to ongoing developments in Maryland law, including their utility in the context of both friendly and contested acquisitions and activist engagements, is important for every Maryland REIT, as is careful monitoring of investor and governance advisor perspectives on the Maryland landscape.
10. Tax Reform. As laid out in our [December 23 memo](#), the new tax law is expected to have far-reaching implications for domestic and multinational businesses as well as domestic and cross-border transactions, impacting the structure, pricing and, in some cases, viability of broad categories of deals. Of particular relevance to REITs, as a result of eligibility of REIT distributions for the new 20% deduction for pass through companies, REIT investors will benefit from an effective 29.6% rate on REIT ordinary income dividends, much lower than prior law rates of 39.6%, which is expected to have a number of ripple effects and potentially stimulate the growth of REITs.

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