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Interviewed by Tony Korsten
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Industry-led approach gives

BDO

the real estate edge in assurance, tax and advisory services

“Over 1,800 people providing clarity in audit, tax, advisory and business outsourcing to companies across numerous industries. Nine offices in South Africa and over 91,000 people in 167 countries around the globe.”

BDO South Africa's introductory 'soundbite' seems to say it all about this leader in the audit, tax and advisory space, but when

Asset sat down to speak to members of their expert real estate and construction (REC) sector team, the depth and significance of its sharply focused industry-led approach was a revelation.

Paul Badrick is head of public entity practice as well as leader of the national REC team at BDO, and is based in Johannesburg.



From left: Louis van Manen, Michelle Botha and Paul Badrick



"18 months ago we took the decision to adopt a go-to-market strategy," he tells Asset, "which saw us create various focus sectors within our firm: natural resources, financial services, the public sector, technology/ media/telecoms, consumer business, and real estate and construction. As the REC leader I work with a dedicated team which understands the changes and challenges facing the real estate and construction industry, and is at the forefront of the industry's conversation in terms of audit, tax and advisory expertise."

But that's not all. In talking to Paul and his team it soon becomes apparent that through active involvement in related trade bodies, they are also able to lend perspective to trends, opportunities, and issues that affect their real estate and construction clients. BDO's strategic shift is in line with the group's international model which has established sector specialisation. The global BDO REC Steering Committee, of which Paul is a member, meets on a monthly basis, and its insights feed into the South African team's deep understanding of the industry.

"We are leaders within the REC space because of the experience and expertise embedded in our sector team. As a 'legacy' firm that brought various entities together to make BDO what it is today, we have wide access to additional support drawn from across the firm. As a result we are attracting a lot of real estate work, and the construction side is growing as the economic environment stabilises a bit more post-lockdowns."



With REITs having taken a battering over the past year and a half, the REC team is exceptionally well-placed to 'hold their hand' as they deal with Covid-linked fallout. Both Paul and **Louis van Manen**, a director of BDO and the tax leader on the REC team, are specialists in REITs. BDO has handled numerous listings and currently manages assurance, tax and advisory work, including audits, for at least 12 REITs that are listed on the Johannesburg Securities Exchange.

Paul says it is well-accepted in the listed real estate industry that the REC team is highly experienced in all matters related to REITs. So much so that over the past months the SA REIT Association reached out to BDO to get a view and clarification on how various issues precipitated by Covid-19 were being navigated.

"The SA REIT Association, in its discussions with the JSE, needed guidance globally on matters such as LTVs, differences in valuation methodologies, as well as the impact of reduced dividend payout ratios. We were easily able to supply this guidance from a global perspective by tapping into our BDO member firms across the world."

The tax legislation which governs REITs is unique to the sector and inextricably linked to the listing requirements, as Louis explains. Loss of rental income during lockdown catapulted many listed real estate companies into a situation where dividend payments could not be made.

"Listing on the JSE requires that at least 75% of distributable profits, which is a

concept determined by our Income Tax Legislation, is distributed annually, subject to the Companies Act's solvency and liquidity test. REITs can distribute less and still retain their REIT status but they are then subject to having to justify failing the solvency and liquidity test. If they are able to provide a robust enough analysis of their solvency liquidity test – which they

failed – they can still retain status," he says.

However, there are very real tax implications if REITs don't distribute 100%.

"We have noticed a heightened scrutiny of REITs by SARS in recent times," Louis points out, "and although we see SARS asking relevant questions, we also see misunderstandings, and misconceptions. While the REIT-specific tax legislation has been in force for about seven years it is still relatively new and actually quite complex. Companies need to ensure they do a proper assessment of their tax in line with the legislation. At the same time SARS is having to get up to speed and do proper assessments and reviews of tax submissions by the listed entities."



Michelle Botha, associate director: technical IFRS for BDO in Johannesburg, concedes that IFRS – an international set of accounting rules which all listed entities must abide by – can become very complicated to work with, even for company accountants. This is where the REC team steps up to the mark for its listed commercial property clients, drawing on BDO accounting experts to offer full support on how to apply the rules.

“Standards change periodically and we keep up to speed so we can assist clients fully,” says Michelle. “The introduction of the new accounting standard IFRS 16 from 1 January 2019 introduced significant changes governing the treatment of leases, which became very relevant during the height of Covid-19. Leases were turned on their heads as property companies worked to retain their tenants. Every lease and every change in a lease has to be reassessed in the light of IFRS 16. When there is a modification for example, where a landlord gives a tenant a discount or a rental holiday, there are tax implications. It is very intricate and SARS is very unsympathetic to VAT errors or REITs that fall below the stipulated 75% rental income threshold.”

The main benefit of being a REIT is that there is no capital gains tax on disposal of qualifying property assets. What may transpire in this environment, says Louis, is that there could be opportunistic asset investment and disposals. In other words REITs may cross the Rubicon and become property traders but these profits won't be exempt from tax.

The vastly changed rental landscape over the past 18 months has created uncertainty around valuations. Here too the REC has been able to guide financial directors through the minefield of IFRS and JSE requirements for company financial statements.

“In the fair value measurement there is more uncertainty than usual of forward-

looking cashflows based on estimates and judgements which predict how tenants will perform,” Michelle notes.

“Rentals have been stabilising but the uncertainty is coming through in the valuations. From an IFRS perspective and with the JSE there are two specific requirements: you need to disclose the sensitivities of those valuations in the financial statements, and you need to be specific as to why those inputs are sensitive and how you have applied your estimates and judgements. We work alongside the financial director when companies prepare their statements to make sure the necessary requirements are met.”

Both Paul and Louis sound notes of caution from an advisory perspective. Paul advises non-listed companies who may be considering listing to weigh up why they want to do it. “It can become onerous,” says Paul. “The company becomes a corporate requiring a CFO and an audit committee, and tax angles change.” Louis's advice is aimed at REITs who venture offshore and burn their fingers because they do not abide by the golden rule from a tax point of view: “Know the tax landscape of the country you're investing in. You don't want any tax surprises that will affect your yields. And understand the interaction between the tax laws of the two countries, for example, place of residence, transfer pricing, and access to a double tax agreement.”

Fayaz Mohamed and **Bradley Jackson** are partners at BDO in Cape Town and lead the advisory and assurance component of the REC team.

Fayaz says one of the services which is really 'headlining' for clients in the real estate and construction industry is

ESG support. From an ESG perspective investors want to know the purpose behind what they're investing in and are not focused solely on the profit line.

"More and more clients are asking us to audit their ESG requirements and provide a review of the non-financial



Bradley Jackson and Fayaz Mohamed



information for the integrated report. On the JSE front there is a demand for our services to assist companies in meeting legislated JSE requirements. CEOs and financial directors have to formally attest in their annual reports that internal financial controls are adequately designed and operating effectively. We provide them with the necessary expertise from an internal audit and consulting perspective.

"BDO's people and business solutions team commented recently that for a large part of the working population, the pandemic has proved that many organisations can function and, in many cases, function quite well working

remotely. The stigma of remote work is virtually gone. Internationally we are seeing a rise in the co-trend models such as co-retail, co-living and co-working, all of which are recalibrating the office to meet workforce needs."

"Our REC data analytics team, spearheaded by **Michael Rayner**, one of our directors, has seen an increase in the number of clients using data analytics software," says Fayaz. "Data models are used to prepare performance management dashboards and even management accounts, assisting management to monitor performance and make decisions with more precision."

The role independent assurance plays in improving the quality of information available to companies is vital, notes Bradley, especially when it comes to decision-making. BDO's role in ensuring that information is accurate and reliable, reduces risk and reflects transparency, cannot be over-estimated.

"Assurance is extremely challenging, with the regulator keeping a close eye over us as auditors. Companies are relying on us far more so it's not just about signing off on financial statements. There is far greater responsibility resting on the auditor. We need experienced and expert teams to work with us and have established a steering group on

each listed client. This aids us in meeting tight deadlines, servicing our clients to a world-class standard and keeping ahead of the regulator. We're making very good progress," he says.

BDO's go-to-market strategy shift from a service line approach to an industry-led one

is clearly paying dividends. And there is every reason to believe that it will continue to do so. By reaching out to the real estate and construction sector to lend its experience and expertise, it is building strong relationships, winning clients and contributing positively to an economically significant and increasingly complex space. **A+**

