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SEBI introduces REIT in India- issues draft SEBI (Real Estate Investment Trusts) Regulations, 2013

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BACKGROUND:

REIT exists in several countries including USA, Australia, Singapore, Japan , UK etc and is considered as one of the preferred investment vehicles around the world.

In India, SEBI had introduced legal framework on 16-04-2008 by way of SEBI (Mutual Funds) (Amendment) Regulations, 2008¹ and inserted Chapter VI A – Real Estate Mutual Funds Schemes (REMFs). REMFs were subject to following restrictions:

- Close ended schemes.
- Listing of units on a recognized stock exchange.
- Atleast 35% of the Net assets of the scheme to be invested directly in real estate assets.
- Atleast 75% of the net assets of the Scheme shall be invested in:
 - a. real estate assets;
 - b. mortgage backed securities (but not directly in mortgages);
 - c. equity shares or debentures of companies engaged in dealing in real estate assets or in undertaking real estate development projects, whether listed on a recognized stock exchange in India or not

INTRODUCTION OF DRAFT REGULATIONS:

SEBI, on 10th October, 2013, issued a Consultation paper on draft SEBI (Real Estate Investment Trusts) Regulations, 2013² inviting public comments on the same latest by October 31, 2013.

Eligibility Criteria for registration as REIT

- Applicant needs to be a Trust and Trust deed should be registered;
- Sponsor(s) should have a consolidated net worth of atleast ₹ 20 crores;
- Each Sponsor should have atleast 5 yrs experience in real estate industry;
- Manager should have minimum net worth of ₹ 5 crores and should have atleast 5 years experience in fund management/ advisory services/property management in the real estate industry or in development of real estate; and atleast 2 key personnel in its investment committee should individually have atleast 5 years experience in fund management/ advisory services/property management in the real estate industry or in development of real estate;
- Trustees should be registered with SEBI under SEBI(Debenture Trustees) Regulations, 1993 and should not be associate of the sponsor/manager/trustee. Atleast 50% of the Trustee's directors should be independent and not related parties to the REIT.

¹ http://www.sebi.gov.in/cms/sebi_data/commondocs/notificationamend_p.pdf

² http://www.sebi.gov.in/cms/sebi_data/attachdocs/1381398382013.pdf



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- Principal valuer should not be an associate of the sponsor/manager/trustee and should have atleast 5 years of experience in valuation of real estate;
- All unit holders of the REIT should enjoy equal voting rights.

While the draft regulation appears to be in line with US and Singapore regulations³ on REIT, it differs from the same in view of certain unique provisions, discussed hereunder;

- Listing of units is mandatory and in order to ensure that only large assets and established players enter the market, one of the conditions laid down by SEBI for coming out with initial offer is that the value of REIT assets should be atleast ₹ 1000 crores.
- Further, Investment upto 100% of the corpus of REIT shall be permitted in a single project subject to the prescribed minimum size i.e. the value of the REIT assets is atleast ₹ 1000 crores.

Comparative Chart on REIT Regulations –India (Proposed Structure) v/s USA v/s Singapore

Regulation Requirement	India (Proposed)	USA	Singapore
Year of Introduction	2013	1960	2002
Governing Code	SEBI (Real Estate Investment Trusts) Regulations, 2013	Real Estate Investment Trust Act, 1960, Section 856 of IRC	Securities and Futures Act (SFA), Monetary Authority of Singapore (MAS) -Code of Collective Investment Schemes (guidelines for Property Funds)
Legal Structure	Trust set up under Indian Trusts Act, 1882	Corporation, trust of association	Trust
Listing requirement	Mandatory	Not mandatory	Not mandatory
Investment conditions	At least 90% of the value of the REIT assets ⁴ shall be in completed rent generating properties ⁵ .	At least 75 percent of its gross income from real estate related sources, including rents from real property and interest on mortgages financing real property or	At least 75% of the property fund's deposited property should be invested in income-producing real estate

³http://www.mas.gov.sg/~media/resource/legislation_guidelines/securities_futures/sub_legislation/RevisedCode30Sep2011final.pdf

⁴ "REIT assets" means real estate and other assets held by the REIT whether directly or through a Special Purpose Vehicle

⁵ 'rent generating property' shall mean property of which not less than 75% of the area has been rented/leased out



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Regulation Requirement	India (Proposed)	USA	Singapore
		At least 95 percent of its gross income from such real estate sources and dividends or interest from any source.	
Other Permissible Investments	<ul style="list-style-type: none"> • Developmental properties⁶; • Listed or unlisted debt of companies; • mortgage backed securities; • Equity shares of companies listed on a recognized stock exchange in India which derive not less than 75% of their revenues from Real Estate activity; • Government securities; • Money market instruments or Cash equivalents; 	-	<ul style="list-style-type: none"> • real estate-related assets, wherever the issuers/assets/securities are incorporated/located/issued/ traded; • listed or unlisted debt securities and listed shares of, or issued, by local or foreign non-property corporations; • government securities (issued on behalf of the Singapore Government or governments of other countries) and securities issued by a supranational agency or a Singapore statutory board; and • cash and cash equivalent items <p>Not more than 5% of the property fund's deposited property may be invested in any one issuer's securities or any one manager's funds. A corporation and its subsidiary companies are regarded as one issuer or manager.</p>
Revenue Restrictions	Not less than 75% of the revenues of the REIT other than gains arising from disposal of properties shall be from rental, leasing and letting real estate assets at	Sec. 856 (c) (2) of IRC lays the minimum income from real asset and financial investments of the REIT (Atleast 95%), while sec. 856 (c) (3) lays down the minimum income from real-estate	A property fund should not derive more than 10% of its revenue from sources other than: a) rental payments ⁷ from the tenants of the real

⁶ Provided that such investment shall only be in properties which shall be held by the REIT for not less than three years after completion and shall be leased out;

⁷ Rental payments include income that is ancillary or incidental to the leasing of real estate such as income from



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Regulation Requirement	India (Proposed)	USA	Singapore
	all times	related assets (Atleast 75%)	estate held by the property fund; or b) interest, dividends, and other similar payments from SPVs and other permissible investments of the property fund.
Shareholder restriction	-	<ul style="list-style-type: none"> • Minimum of 100 shareholders • no more than 50 percent of its shares held by five or fewer individuals during the last half of the taxable year 	-
Distribution of Income	Atleast 90% of the net distributable income after tax of the REIT shall be distributed as dividend to the unit holders.	at least 90 percent of its taxable income in the form of shareholder dividends	Any distributions made by S-REITs to foreign or local investors shall be exempt from tax provided atleast 90% of the taxable income is distributed
Mode of Investment in properties	Directly or through SPVs holding atleast 90% of their assets directly in such properties		Direct ownership or a shareholding in an unlisted special purpose vehicle (“SPV”) constituted to hold or own real estate
Location Restrictions	REIT shall only invest in assets based in India.	No such restriction	Can invest both in or outside Singapore.
Non permissible investment	Vacant land or agricultural land or mortgages other than mortgage backed securities.	-	vacant land and mortgages (except for mortgage-backed securities)
Permitted investment in a single project	100% of the corpus of the REIT, subject to the condition that minimum size of such asset is not less than Rs. 1000 crore	Concentration limits has been laid down in Para 4 (B) of Section 856 (c)	-
Initial offer restrictions	<ul style="list-style-type: none"> • REIT should be 	-	<ul style="list-style-type: none"> • Minimum asset size of

use of signage space and advertising contributions by tenants.



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Regulation Requirement	India (Proposed)	USA	Singapore
	<p>registered with SEBI</p> <ul style="list-style-type: none"> Value of REIT assets⁸ should be atleast ₹ 1000 crores. Minimum offer size should be atleast ₹ 250 crore. Minimum public⁹ float should be of 25% 		<p>S\$20 million (For REITs denominated in foreign currency the minimum asset size is of at least US\$20 million);</p> <ul style="list-style-type: none"> Atleast 25% of the units are to be held by 500 public unit holders
Minimum Subscription and unit size	Under both the initial offer and follow-on public offer, minimum subscription amount shall be atleast ₹ 2 lakhs. The unit size shall be of ₹ 1 lakh.	-	-
Borrowings and Deferred payments	<ul style="list-style-type: none"> The aggregate consolidated borrowings and deferred payments of the REIT shall never exceed 50% of the value of the REIT assets. If the aggregate consolidated borrowings and deferred payments of the REIT exceed 25% of the value of the REIT assets, for any further borrowing: <ul style="list-style-type: none"> (a) credit rating shall be obtained from a credit rating agency registered with SEBI; and (b) approval of unit holders shall be 	-	<ul style="list-style-type: none"> The total borrowings and deferred payments¹⁰ (collectively, the “aggregate leverage”) of a property fund should not exceed 35% of the fund's deposited property. The aggregate leverage of a property fund may exceed 35% of the fund's deposited property (up to a maximum of 60%) only if a credit rating of the property fund from Fitch, Moody's or Standard and Poor's is obtained and disclosed to the public. The property fund should continue to maintain and disclose a credit rating so long as its aggregate leverage exceeds 35% of

⁸ "Value of the REIT assets" means aggregate value of all the assets under the REIT as assessed by the valuer

⁹ 'public' shall not include any related party to the REIT or any person as may be specified by the Board

¹⁰ Deferred payments include deferred payments for assets whether to be settled in cash or in units in the property fund.



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	obtained in the manner specified.		the fund's deposited property.
Cap on income from other sources	25%		10%
Investment in units of other REITs	Not permitted		Permitted
Transaction with related parties	Permitted subject to fulfillment of conditions specified in Regulation 19.		Permitted subject to fulfillment of conditions specified in Paragraph 5