

Article



REITs, InvITs and AIFs to get fueled further by foreign investors

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Background

Reform is the new buzzword in the political and economic scene in an effort of finding ease of doing business. Right from relaxing external commercial borrowing norms, to liberalizing the FDI policy; it has been understood that the government has been very keen on welcoming foreign investments in India. These changes could provide the much needed impetus to the sectors of the Indian economy which requires funds. The infrastructure sector in particular requires a lot of capital infusion looking at the current needs. Hence in order to pool in sufficient funds relaxation in some of the foreign investment norms have been affected.

Through the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) (Eleventh Amendment) Regulations, 2015, issued by Reserve Bank of India (RBI) on the 16th of November, 2015¹, it had amended the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000. The amendment pertained to allowing foreign investments in Investment Vehicles.

On the 21st of April, 2016, RBI, *vide* circular RBI/2015-16/377 of the A.P. (DIR Series) Circular No. 63² (Present Circular), notified that foreign investment in units issued by Real Estate Investment Trusts (REITs), Infrastructure Investment Trusts (InvITs) and Alternative Investment Funds (AIFs) governed by SEBI regulations shall be allowed, subject to the prescribed conditions.

The purpose behind this move taken is the view to rationalize the foreign investment for AIFs. Facilitation of foreign investment in collective investment vehicles for real estate and infrastructure sectors has also been stated as reasons. Moreover this would extend the lending abilities of the Investment Vehicles beyond the extant sources.

Salient features of the changes

1. Investment vehicles and investors

The following shall be reckoned as “*Investment Vehicle*” for the for the purpose of implementation of the circular:-

1. REITs registered and regulated under the SEBI (REITs) Regulations 2014;
2. InvITs registered and regulated under the SEBI (InvITs) Regulations, 2014;
3. AIFs registered and regulated under the SEBI (AIFs) Regulations 2012.

A person resident outside India, including a Registered Foreign Portfolio Investor (RFPI) and a Non-Resident Indian (NRI) may invest in units of Investment Vehicles.

‘*Person resident outside India*’ as per para 2.1.32 of the FDI policy³ means-

‘*A person who is not a Person resident in India*’

¹ <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10130&Mode=0>

² <https://rbidocs.rbi.org.in/rdocs/notification/PDFs/NT377D62BA8DB105543EA8CB5B2F26D805C24.PDF>

³ http://dipp.nic.in/English/Policies/FDI_Circular_2015.pdf

Where, ‘a person resident in India’ shall have meaning as given in para 2.1.31 of the FDI policy.

‘RFPI’, as per regulation 2 (viib) of Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000 means-

“A person registered in accordance with the provisions of Securities Exchange Board of India (SEBI) (Foreign Portfolio Investors) Regulations, 2014, as amended from time to time.”

‘Unit’ shall mean-

“Beneficial interest of an investor in the Investment Vehicle and shall include shares or partnership interests.”

2. Remittance

The remittance for the units purchased by the foreign investor shall be done by an inward remittance through the normal banking channel including by way of debit to a Non-Resident External account (NRE account) or a Foreign Currency (Non-Resident) account (FCNR account).

3. Sell, transfer, pledge or redemption of securities purchased

There is no restriction on selling or transferring of the securities purchased by the foreign investor. The units may also be redeemed as per the SEBI regulations or the RBI directions. Pledging of such units to secure credit facilities being extended to the non-resident investor was allowed *vide* the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) (Eleventh Amendment) Regulations, 2015.

4. Downstream investment by the Investment Vehicle

To be regarded as foreign investment, downstream investments shall not be by an Investment Vehicle whose either Sponsor or Manager or Investment Manager is Indian ‘owned and controlled’ as defined in Regulation 14 of the Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000, as amended recently *vide* Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) (Second Amendment) Regulations, 2016⁴.

A company shall be considered as owned by resident Indian citizens if:-

1. More than 50% of the capital in it is beneficially owned by resident Indian citizens and/or Indian companies.
2. These Indian citizens/Indian companies need to be ultimately owned and controlled by resident Indian citizens.

⁴ <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10289&Mode=0>

A Limited Liability Partnership will be considered as owned by resident Indian citizens if:-

1. More than 50% of the investment in such an LLP is contributed by resident Indian citizens and/ or entities which are ultimately ‘owned and controlled by resident Indian citizens’ and;
2. Such resident Indian citizens and entities have majority of the profit share

In case the sponsor or manager or investment manager are not in a company or LLP form, SEBI shall determine whether they shall be considered as ‘foreign owned and controlled’. Moreover it has also been clarified that the quantum of investment by foreign investors in an Investment Vehicle shall not be a determining factor in considering whether downstream investment by it is foreign investment or not.

5. Downstream investment in LLP by Investment Vehicle

Downstream investment in an LLP by an Investment Vehicle that is reckoned as foreign investment has to conform to the provisions of Schedule 9 of the Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000; as well as the extant FDI policy for foreign investment in LLPs.

Schedule 9 pertains to the Scheme for Acquisition/Transfer by a person resident outside India of capital contribution or profit share of LLP. It is also stated that an LLP operating in sectors where 100% FDI is allowed under the automatic route of FDI Scheme would be eligible to receive FDI.

6. Regulation 4(b) (iv) – REITs excluded from “Real estate”

In regulation 4(b) (iv) of the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2000, it is stated that foreign investment in any company or partnership firm or proprietary concern or any entity, whether incorporated or not, which is engaged or proposes to engage “in real estate business, or construction of farm houses” is prohibited. But the explanation to the regulation excluded development of townships, construction of residential /commercial premises, roads or bridges from the purview of definition of real estate.

The Present Circular clarifies that REITs, for the purpose of these regulations, shall not be included in “real estate business”.

Hence, looking at all these developments taking place, we hope our growth gets propelled by further foreign investments.

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