



Framework regulating

REIT

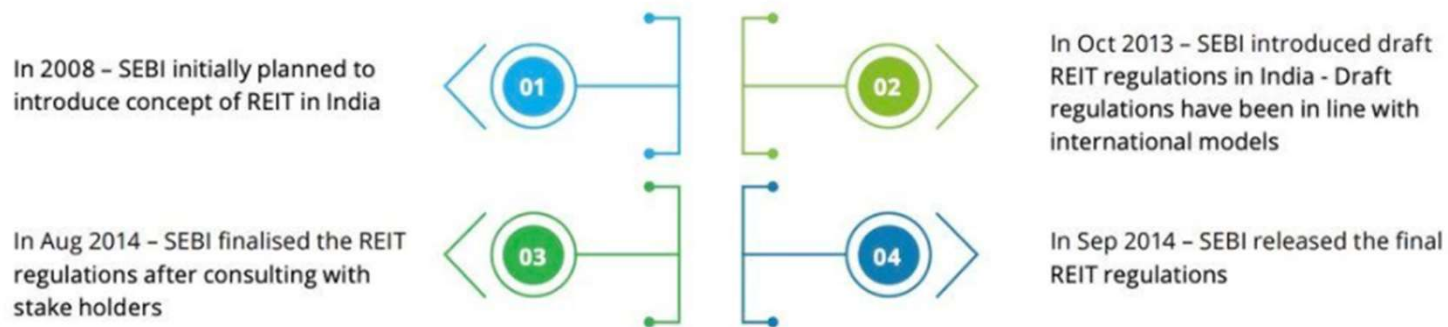
Real Estate Investment Trust

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Origin of Real Estate Investment Trust in India

- ▶ The concept of REIT originates from the USA. The Association of Mutual Funds of India recommended introduction of REITs in India. The system of REITs was to be introduced by SEBI in 2008, however the concept was realised only in 2014.
- ▶ To encourage the concept, the Finance Act, 2014 accorded a 'tax pass through status' to the income received by the REIT from the SPV.



Meaning – Real Estate Investment Trusts

- ▶ REITs in India are regulated by SEBI (Real Estate Investment Trusts) Regulations, 2014.
- ▶ According to Regulation 2(1)(zm) of the SEBI (REIT) Regulations, 2014, a REIT shall mean “a trust registered under these regulations.”
- ▶ The REIT is in the form of a trust set up under the Indian Trusts Act, 1882.
- ▶ In general terms, a REIT is an investment vehicle that invests in rent-yielding completed real estate properties either directly or through SPVs.

A REIT is based on the model of ‘mutual funds’ whereby funds are pooled from various unitholders and a specialized group of experts invests the collected funds in the real estate sector.

REIT Structure (1/2)

A REIT shall be in the form of trust and following shall be the parties to the REIT as per Regulation 2(1)(zc) of the REIT Regulations :

➤ **Sponsor Groups** : Shall include:

The sponsor(s) wherein a sponsor shall mean to be a person(s) who set(s) up the REIT and designated as such at the time of application made to the SEBI and includes an inducted sponsor.

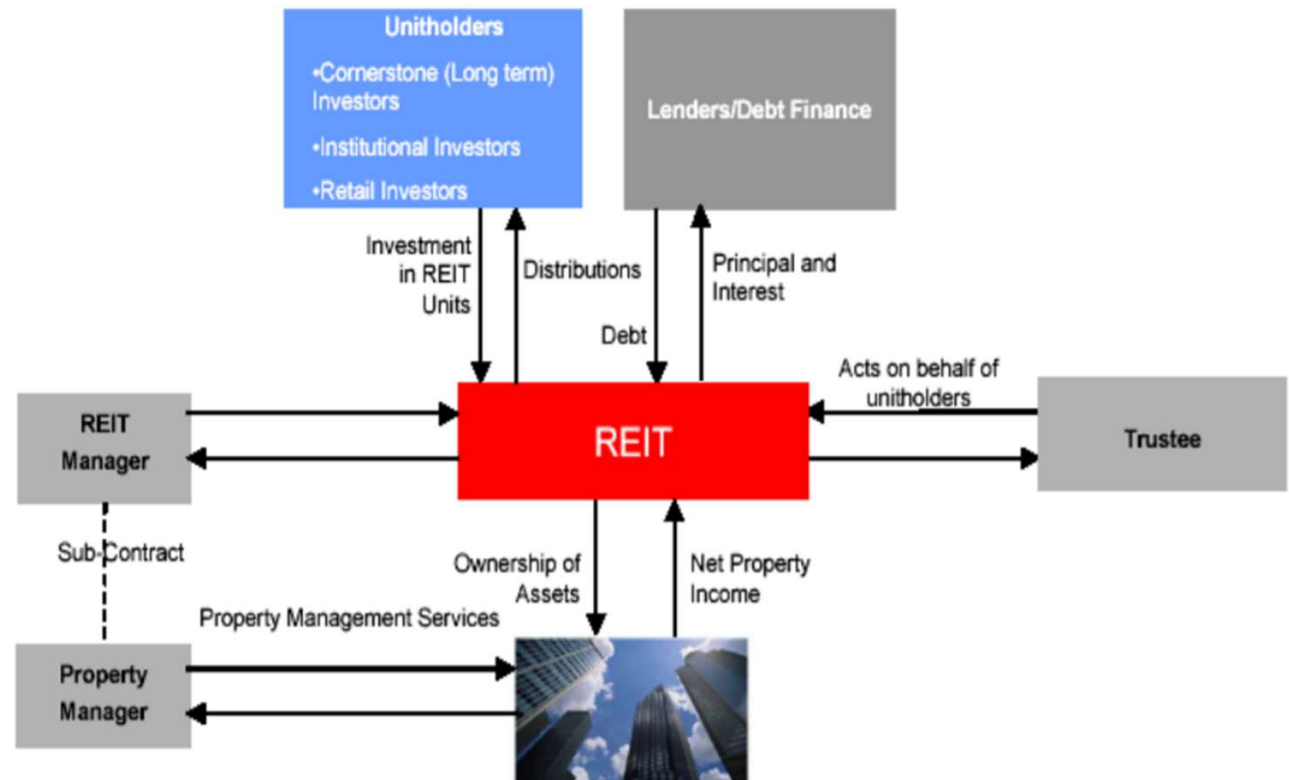
In case the sponsor is a body corporate :

- a. entities or person(s) which are controlled by such body corporate;
- b. entities or person(s) who control such body corporate;
- c. entities or person(s) which are controlled by person(s) as referred at clause b.

in case sponsor is an individual:
an immediate relative of such individual (i.e., any spouse of that person, or any parent, brother, sister or child of the person or of the spouse); and entities or person(s) which are controlled by such individual

REIT Structure (2/2)

- **Manager:** A manager means a company or an LLP or Body Corporate incorporated in India which manage the assets and investments of the REIT and undertakes operational activities of the REIT.
- **Trustee:** Means a person who holds the REIT assets in trust for benefit of the unit holders.
- **Inducted Sponsor:** Any change in sponsor due to entry of a new sponsor with or without exit of an existing sponsor.



Investment Avenues – REIT (1/4)

A REIT may invest in :

- ✓ holdco and/or SPV
- ✓ properties
- ✓ securities
- ✓ Transferable Development Rights in India

In accordance with investment strategy detailed in offer document.

A REIT shall not invest in :

- ✓ vacant land
- ✓ agricultural land
- ✓ mortgages other than mortgage back securities.

The exception to the above being that a REIT may invest in any land which is contiguous and extension of an existing project being implemented in stages.

Investment Avenues– REIT (2/4)

- a. **Not less than** 80% of total assets of REIT assets shall be in the form of completed and rent and/or income generating properties.
- b. **Not more than** 20% of total assets of the REIT assets shall be in the form of assets other than as provided in point 'a' above and such other investment shall only be in :
 - Properties, which are:
 - Under - construction properties to be held by the REIT for minimum 3 years after completion;
 - Under - construction properties which are a part of the existing income Generating properties owned by the REIT to be held by it for minimum 3 years after completion;
 - Completed and not rent generating properties to be held by the REIT for minimum 3 years from date of purchase;

Investment Avenues – REIT (3/4)

In continuation of the above, Not more than 20% of total assets of the REIT assets shall be in the form of:

- Listed or unlisted debt of companies or body corporate in real estate sector
- Equity shares of companies listed in India whose not less than 75% of operating income is from Real Estate activity in the previous Financial Year;
- Unlisted equity shares of companies whose not less than 75% of operating income from Real Estate Activity in the previous Financial Year;
- Mortgage backed securities;
- Government securities;
- Unutilized FSI of a project;
- TDR acquired for the purpose of Utilization with respect to a project where it has already made investment;
- Money market instruments or Cash equivalents;

Investment Avenues – REIT (4/4)

Not Less Than 51% of the consolidated revenues of the REIT, holdco and the SPV, shall be from rental, leasing and letting real estate assets or any other incidental income.

Such income shall not be from gains arising from disposal of properties

A REIT shall not invest in units of other REIT

No Schemes shall be launched under REIT

A REIT shall not undertake lending to any other person. exception being in any holdco, SPV in which REIT has invested in or debt securities.

A REIT shall hold completed and revenue generating property for minimum 3 years from the date of purchase, whether directly or indirectly.

Real Estate - Meaning

Real Estate means “*land and any permanently attached improvements to it, whether leasehold or freehold and includes buildings, sheds, garages, fences, fittings, fixtures, warehouses, car parks, etc. and any other assets incidental to the ownership of real estate but does not include mortgage*”

Provided that asset falling under the purview of ‘infrastructure’ in accordance with notification by the Ministry of Finance shall not be classified as real estate.

However, the real estate shall include:

- Hotel, hospitals , convention centers forming part of real estate project whether rent generating or income generating.
- Common infrastructure for real estate projects, industrial parks and SEZ.

Issue of Units of REITs to PROs (1/3)

Eligible Instruments for investment by Person Resident Outside India

Debt Instruments

As per notification by Ministry
Of Finance , Central
Government

FEM (Debt instruments)
Regulations,2019

Non Debt Instruments

As per notification by
Ministry Of Finance , Central
Government

FEM (Non Debt
Instruments) Rules, 2019

FEM (Mode Of Payment and
Reporting of Non Debt
Instruments)Regulations,2019

Issue of Units of REITs to PROIs (2/3)

Units of REIT are Debt Instruments which qualify as Eligible Investment and where a PROI can invest in. Other debt instruments are as follows:

Equity Tranche of securitisation structure	Investment in units of REIT/AIF/InVIT	Contribution to trusts
Depository receipts against equity instruments	Acquisition, sale or dealing directly in immovable property	Investments in equity of incorporated entities
Investment in units of mutual fund and ETFs which invest more than 50% in equity	Capital participation in LLPs	Instruments notified in FDI Policy from time to time

Issue of Units of REITs to PROIs (3/3)

The Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017 regulate allotment of units of REIT to a person resident outside India (hereinafter “PROI”)

The said regulations define ‘Unit’ as a ‘beneficial interest of an investor in an investment vehicle’

Schedule 8 of the Regulations prescribe that a PROI or an entity incorporated outside India (other than citizen or an entity incorporated in Pakistan or Bangladesh) may invest in units of Investment Vehicles.

Investment made by an Investment Vehicle into an Indian entity shall be deemed to be indirect foreign investment for the investee Indian entity if the Sponsor or the Manager or the Investment Manager (when the same are in form of companies or LLPs)

- (i) is not owned and not controlled by resident Indian citizens or
- (ii) is owned or controlled by persons resident outside India.

REITs in Indian Context

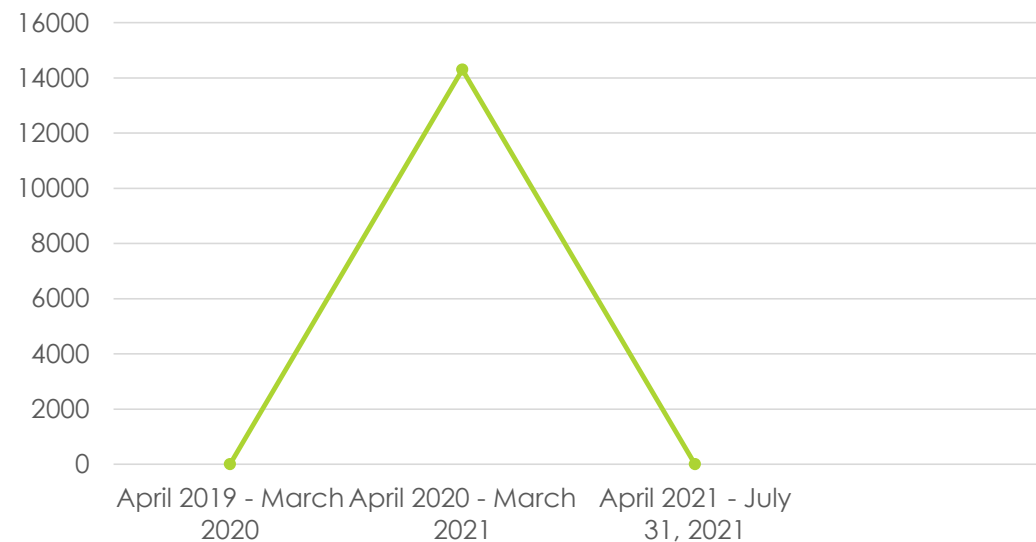
The concept of REITs remains highly unpopular even after 7 years of being.

Only 3 REITs have been listed since inception namely:

- Brookfield India Real Estate
- Mindspace Business Parks REIT
- Embassy Office Parks REIT

These too have been concentrated during the Financial Year 2020 – 2021 and have raised an aggregate of Rs.14300 crore.

FUND RAISED BY REITs



Data Source: SEBI Statistics

Taxation of REITs as a Business Trust (1/2)

A REIT may derive income from the following sources:

Interest income received by the REIT pursuant to investment in SPV by way of debt bearing instruments

- Such interest received is fully exempt in hands of REIT under section 10(23FC) of the Income Tax Act, 1961 and thus, the SPV is not required to deduct TDS on interest.

Dividend income received by the REIT pursuant to investment in SPV by way of shares

- Such dividend received is exempt in hands of REIT under section 10(23FC) of the Income Tax Act, 1961 and thus, the SPV is not required to deduct TDS on dividend.

Rental income by way of renting/leasing/letting out any real estate asset owned by the REIT

- Rental Income is exempt in the hands of REIT under section 10(23FCA) of The Income Tax Act, 1961

Taxation of REITs as a Business Trust (2/2)

- ▶ Any income other than the incomes mentioned above , shall be taxable in the hands of the REIT as mentioned :

INCOME	TAXABILITY
Long Term Capital Gain u/s 112	Taxable @ 20%
Short Term Capital Gain u/s 111A	Taxable @ 15%
All other income	Taxable @ 42.744% (30%+36% SC +4%HEC)

How REIT Contributes to Value Addition? (1/2)

- ▶ From the investors' perspective, REIT contributes to the economic value by :

Pursuant to Regulation 18(16) of the REIT Regulations, minimum 90% of net distributable cash flows of REIT shall be distributed to the unit holders on a half yearly basis . This ensures sustainable returns to the unitholders over a period of time.

Small investors who intend to invest in real estate however are unable to do the same due to limited funds , may invest in REIT and build a diversified property portfolio.

Informed decision-making enabled for investors as information is made available by the REITs pursuant to Regulation 23 of the REIT Regulations which mandates yearly and half yearly disclosures by the REIT.

Regulation 16(1) of the REIT regulations , mandates listing of units of REIT post initial offer on a recognised stock exchange having a nationwide trading terminal. This provides adequate liquidity to small investors.

How REIT Contributes to Value Addition? (2/2)

- ▶ At the Macro level , the REITs enhance value by :

Being regulated by SEBI, the REITs follow a transparent approach towards their activities thereby enhancing corporate governance standards.

This will reduce the quantum of malpractices in the real estate sector.

Increased funding and development in the real state sector which will facilitate recovery of the sector and growth thereafter.

Fund raising from the public will decrease the financing burden on banks by reducing exposure to real estate, thereby enabling the creation of additional capital for other sectors.

Risks Involved in Investing in REITs

► While REITs have inherit advantages, they are bundled with certain limitations such as :



Rent and capital appreciation of the real estate properties are subject to market fluctuations thereof. Also, Rental income for REITs depends on finding quality clients for office space and their ability to pay rents on time.



With increasing 'work from home' opportunities due to the Covid-19 pandemic, rentals for properties are facing a slump thereby decreasing the returns generated by the REITs.



Limited REIT options in the Indian context restricts the investment avenues.



When going through a one year trend of the unit price of the listed REITs , substantially all three REITs in India have reported depreciation in unit value rendering it an unattractive avenue of investment.



THANK YOU