SEBI releases amended REIT and InvIT Regulations

December 2, 2016

In brief

Post extensive public consultation and stakeholder deliberations, the Securities and Exchange Board of India (SEBI) has issued the SEBI (Real Estate Investment Trusts) (Amendment) Regulations, 2016 and SEBI (Infrastructure Investment Trusts) (Amendment) Regulations, 2016 (together referred to as “Amendment Regulations”), amending the SEBI (Real Estate Investment Trusts) Regulations, 2014 (REIT Regulations) and SEBI (Infrastructure Investment Trusts) Regulations, 2014 (InvIT Regulations), respectively.

In addition to the changes highlighted in the minutes of the SEBI board meeting dated 23 September, 2016, the Amendment Regulations have introduced a few other amendments to the REIT Regulations and InvIT Regulations. The Amendment Regulations have come into force from the date of their publication in the Official Gazette i.e. 30 November, 2016.

This news alert provides a snapshot of the key amendments made to the REIT Regulations and InvIT Regulations.

In detail

The key amendments made to the REIT Regulations are summarised below.

Changes relating to the “sponsor”

- Concept of “sponsor group” introduced.
- The term “sponsor group” defined to include:
  a. the sponsor;
  b. where the sponsor is a body corporate:
     - entities/ persons controlled by such body corporate;
     - entities/ persons controlling such body corporate ; and
  c. entities/ persons controlled by entities / persons controlling such body corporate and;where the sponsor is an individual;
     - relatives of such individual; and
     - entities/ controlled by such individual
- For each sponsor group, not less than one person shall be identified as the “sponsor.”
- Limit on the maximum number of sponsors removed.
- Sponsors and the sponsor group shall collectively hold:
  a. a minimum of 25% of the total units on a post-issue basis; and
  b. a minimum of 15% of the outstanding units of the REIT at all times.
- Each sponsor shall hold a minimum of 5% of the outstanding units of the listed REIT at all times.

Changes relating to “public issue”

- Multiple classes of units not permitted.
- However, subordinate units carrying inferior rights may be issued only to the sponsor and its associates.
- Restriction on investment by associates of trustee in units of REIT removed.

- Slabs for minimum offer size and public float introduced:

  a. If post issue capital is less than INR 1,600 crores: minimum 25% or INR 250 crores, whichever is higher.

  b. If post issue capital is equal to or more than INR 1,600 crores but less than INR 4,000 crores: minimum INR 400 crores.

  c. If post issue capital is equal to or more than INR 4,000 crores: minimum 10%.

- However, the public float in all cases shall be increased to a minimum of 25% within a period of three years from the date of listing.

- Minimum number of subscribers (other than sponsors, its related parties and its associates) at the time of public offer shall be 200. However, if the number of public unit holders falls below 200, there shall be no mandatory requirement to delist the units of the REIT.

- Minimum subscription percentage increased from 75% to 90%.

Changes relating to holding structure

- REIT allowed to hold assets through two-level entity structure.

- Concept of holding company (Hold Co) introduced. Hold Co defined to mean a company or a limited liability partnership:

  a. in which the REIT holds or proposes to hold a controlling interest and minimum 51% of the equity share capital/ interest; and

  b. which is not engaged in any activity other than holding of underlying SPVs/ real estate assets.

- Investment through Hold Co should be subject to:

  a. ultimate holding interest of the REIT in the SPVs of at least 26%;

  b. other shareholders/ partners do not restrict the REIT, Hold Co or SPV from complying with the REIT Regulations, and an agreement shall be entered into with such other shareholders/ partners to that effect;

  c. the manager shall appoint majority of the board members of Hold Co and/ or SPV; and

  d. in every meeting of Hold Co and/ or SPV, the voting of the REIT shall be exercised.

- Minimum net distributable cash flows to be distributed by Hold Co to the REIT (subject to provisions of the Companies Act, 2013 and Limited Liability Partnership Act, 2008):

  a. 100% of cash flows received from the SPVs; and

  b. 90% of the balance.

- Minimum holding in SPV by REIT/ Hold Co increased from 50% to 51%.

- Hold Co/ SPV to mandatorily distribute the proceeds from sale of any property, even if there is a re-investment opportunity.

Changes relating to investment conditions

- Definition of “real estate” or “property” widened to include:

  a. hotels, hospitals and convention centers, forming part of composite real estate projects, whether rent generating or income generating; and

  b. common infrastructure for composite real estate projects, industrial parks and special economic zones.

- Removal of investment sub-limit of 10% of value of REIT assets in the following assets:

  a. under-construction properties; and

  b. completed and not rent generating properties.

- Minimum percentage of income of REIT/ Hold Co/ SPV from rental, leasing and letting out real estate assets or other incidental income reduced from 75% to 51%.

- Maximum 10% of the amount raised by REIT by public issue of units could be used for “general purposes” as mentioned in the offer document.

Changes relating to voting conditions

- Minimum percentage voting in favour of resolutions revised as under:

  a. issues requiring unit holder approval in the ordinary course of business (such as approval of annual accounts, approval of auditor and auditor’s remuneration, valuation reports, appointment of valuer, etc.): reduced from not less than 60% to more than 50%;

  b. important issues (such as investment conditions, distribution policy, related parties, valuation, etc.): Reduced from not less than 60% to more than 50%; and

  c. material changes (such as removal of manager, material change in investment strategy, delisting of units, change in trustee, etc.): reduced from not less than 75% to not less than 60%.

Relaxation of conditions to be satisfied prior to public offer

- Investment related conditions to not apply prior to public offer.
- No valuation required to be undertaken at the time of purchase or sale of properties prior to public offer.

Other changes

- Definition of "valuer" widened to include "financial" and "technical" valuation of REIT assets. The list of "financial" and "technical" valuers prescribed.
- Minimum experience requirement for a valuer reduced from 10 years to 5 years.
- Definition of "'associate'" and "'related party'" (erstwhile term "'related parties of the REIT'") amended to align with the definition of the term under the Companies Act, 2013 or under the applicable accounting standard. Further, a unit holder holding more than 20% of the units of the REIT (directly or indirectly) shall now not be treated as a "related party."
- Definition of Net Asset Value (NAV) amended to exclude "external debt" in the calculation of NAV.
- Audit of accounts of the REIT shall be undertaken once in a year (erstwhile, twice in a year). Further, the time limit for submitting the audit report to the designated stock exchanges increased from 45 to 60 days from the end of the financial year.
- Time limit for initial/ follow-on/ rights offer by a REIT from the date of issuance of observations on offer document by SEBI increased from six months to one year.
- Manager shall maintain records pertaining to activities of the REIT for a minimum period of seven years.
- Powers granted to SEBI to relax strict enforcement of the REIT Regulations in the interest of investors or for the development of the securities market.
- In addition to the above, a few other procedural and operational changes have been carried out in the REIT Regulations.

The key amendments made to the InvIT Regulations are summarised below:

Changes relating to "sponsor"

- Limit on the number of sponsors removed.
- Each sponsor shall be clearly identified in the application of registration to SEBI and in the offer document/ placement memorandum.
- Minimum sponsor holding reduced from 25% to 15% on a post-issue basis.
- Other conditions:
  a. sponsors would be responsible to the InvIT for all acts, omissions and representations/ covenants related to formation and transfer of assets/ securities;
  b. InvIT/ trustee shall have recourse to the sponsor for any breach with respect to (a) above; and
  c. sponsor/ associate of the sponsor shall act as the project manager for a minimum period of three years, unless a suitable replacement is appointed by unitholders. However, this condition shall not apply if the sponsors hold a minimum of 25% stake on post-issue basis for atleast three years from the date of listing.

Changes relating to "public issue"

- Multiple classes of units not permitted.
- However, subordinate units, carrying inferior rights, may be issued only to the sponsor and its associates.
- Restriction on investment by associates of trustee in units of REIT removed
- Slabs for minimum offer size and public float introduced:
  a. If post-issue capital is less than INR 1,600 crore: Minimum 25% or INR 250 crore, whichever is higher;
  b. If post-issue capital is equal to or more than INR 1,600 crore but less than INR 4,000 crore: Minimum INR 400 crore; and
  c. If post-issue capital is equal to or more than INR 4,000 crore: Minimum 10%.
- However, the public float in all cases shall be increased to a minimum of 25% within a period of three years from the date of listing.
- Minimum subscription percentage increased from 75% to 90%.

Changes relating to holding structure

- InvITs allowed to hold assets through two-level entity structure.
- Concept of holding company ("Hold Co") introduced. Hold

Co defined to mean a company or a limited liability partnership:

a. in which InvIT holds or proposes to hold controlling interest and minimum 51% of the equity share capital/ interest; and

b. which is not engaged in any activity other than holding of underlying SPVs/ infrastructure projects.

- Investment through Hold Co should be subject to the following:

a. ultimate holding interest of the InvIT in the SPVs is atleast 26%;

b. other shareholders/ partners do not restrict the InvIT, Hold Co or SPV from complying with the InvIT Regulations, and an agreement shall be entered into with such other shareholders/ partners to that effect;

c. the investment manager shall appoint majority of the board members of Hold Co and SPV; and

d. in every meeting of Hold Co and SPV, the voting of the InvIT shall be exercised.

- Minimum net distributable cash flows to be distributed by Hold Co to InvIT:

a. 100% of cash flows received from the SPVs; and

b. 90% of the balance.

- Minimum holding in SPV by InvIT/ Hold Co - 51%.

Changes relating to investment conditions

- Scope of PPP projects expanded to include infrastructure projects having achieved commercial operations date and not having a track record of revenue from operations for a period of atleast one year.
- Maximum 10% of the amount raised by InvIT by public issue of units could be used for "general purposes" as mentioned in the offer document. Issue-related expenses shall not be considered as a part of general purposes.
- Further, retained oversubscription proceeds shall not be utilised towards such general purposes.

Changes relating to privately placed InvITs

- If a privately placed InvIT invests or proposes to invest 80% or more of the value of the InvIT assets in completed and revenue generating projects:

a. Minimum investment from an investor shall be INR 25 crore; and

b. Trading lot shall be INR 2 crore.

- Private placement issue shall open within three months from the receipt of in-principle approval for listing.
- Further, a placement memorandum shall be filed with the SEBI atleast five days prior to the opening of the issue.

Changes relating to voting conditions

- Minimum percentage voting in favour of resolutions revised as follows:

a. Issues requiring unitholder approval in the ordinary course of business (such as approval of annual accounts, approval of auditor and auditor's remuneration, valuation reports, appointment of valuer, etc.): Reduced from not less than 60% to more than 50%;

b. Important issues (such as investment conditions, distribution policy, related parties, valuation, etc.): Reduced from not less than 60% to more than 50%; and

c. Material changes (such as removal of investment manager, material change in investment strategy, delisting of units, change in trustee, etc.): Reduced from not less than 75% to not less than 60%.

Other changes

- Definition of "valuer" broadened to include "financial" and "technical" valuation of the InvIT assets. The list of "financial" and "technical" valuers has been prescribed.
- Minimum experience requirement for a valuer reduced from ten to five years.
- Definition of "associate" and "related party" (erstwhile term "related parties of the InvIT") amended to align with the definition of the term under the Companies Act, 2013 or under the applicable accounting standard. Further, an unitholder holding more than 20% of the units of the InvIT (directly or indirectly) shall no longer be treated as a "related party."
- Definition of Net Asset Value ("NAV") amended to exclude "external debt" in the calculation of NAV.
- Lending by InvIT to Hold Co/ SPV shall be permitted.
- Audit of accounts of the InvIT shall be undertaken once in a year (erstwhile, twice a year).

- Time limit for initial/ follow-on/ rights offer by an InvIT from the date of issuance of observations on offer document by SEBI increased from six months to one year.
- Power granted to SEBI to relax strict enforcement of the InvIT Regulations in the interest of investors or for the development of the securities market.
- In addition to the above, a few other procedural and operational changes have been carried out in the InvIT Regulations.

The takeaways

As has been the trend since the introduction of the REIT and InvIT Regulations, SEBI continues with its "inclusive" approach in evolving these regulations.

Based on the discussions with the professional bodies and stakeholders, SEBI has aligned these regulations as per the requirements of certain business practices as well as ironed out a few operational-level discrepancies.

Let's talk

For a deeper discussion of how this issue might affect your business, please contact your local PwC advisor

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