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News Alert
11 October 2013



SEBI releases Draft REIT Regulations

Background

The Securities and Exchange Board of India (SEBI) has released on 10 October 2013 a consultation paper along with draft regulations for Real Estate Investment Trusts (REIT). This is another positive step by the market regulator that could help reinvigorate the real estate sector and push it further up the maturity curve.

The draft REIT regulations aim to provide a regulated platform in India for investment in stabilised real estate assets. REITs could provide a secure and liquid avenue for real estate investments and broaden the investor base for the sector. It would also set the benchmark for investment grade real estate assets.

Internationally, REITs invest in income-yielding real estate assets with the aim of delivering stabilised return to investors, with a potential for upside by way of appreciation in market value of assets. In the current economic environment

where exit options are limited, the REIT regime could help allay developers'/ investors' fears by potentially providing an additional avenue for monetisation of real estate assets.

While in the past, there have been attempts to implement a real estate focused investment regime, it has met with limited success. In some way, the reintroduction of REIT regulations is another beginning. There could be roadblocks, though none insurmountable if there is collective effort on the part of industry and regulators to make it work. This would include amending the tax laws and providing for relaxations in the exchange control regime to mobilise foreign capital.

In this news alert, PwC provides an overview in tabular form of the draft REIT regulations. We have summarised the key aspects of the regulations in some of the popular REIT jurisdictions.

Synopsis of Draft Regulations

1	Legal form	- Trust set up under Indian Trust Act, 1882 - No other form of entity (for example, Company or LLP) is permitted
2	Key definitions	<i>Related parties of REIT</i> - Sponsor, Redesignated Sponsor, Manager, Trustee and Principal Valuer, their associates, their promoters and their directors (including associates of such directors and promoters) - Persons holding >20% of units directly or indirectly/ associates of such persons <i>Completed property</i> - Property in respect of which occupancy certificate has been received from relevant authority <i>Developmental property</i> - Property in respect of which occupancy certificate has not been received <i>Special Purpose Vehicle (SPV)</i> - Body corporate in which REIT holds or proposes to hold controlling interest
3	Key eligibility criteria	<i>Sponsor(s)</i> - Minimum consolidated net worth of INR 20 crore - Minimum real estate experience of 5 years (to be tested for each sponsor) <i>Manager</i> - Minimum net worth of INR 5 crore - Minimum experience of 5 years in either fund management, property management or real estate development <i>Investment Committee</i> - At least 2 key personnel who meet the above-mentioned 5 years experience criterion - At least 50% members to be independent and not considered Related Parties to REIT <i>Trustee</i> - Required to be registered with SEBI - Should not be an associate of the Sponsor, Manager or the Principal valuer 50% of the Trustees directors are independent / not considered Related parties to REIT - Should not be an investor in REIT <i>Principal valuer</i> - Should not be an associate of the Sponsor, Manager or the Trustee - Minimum experience of 5 years in undertaking valuation for real estate - Should not be an investor in REIT

4	Key investment conditions	• Real estate assets in India (other than vacant land, agricultural land, transferable development rights) • Securities of SPVs holding permissible real estate assets in India • Investment in SPVs, subject to: a) SPVs holding =>90% of assets directly b) SPVs to not invest in other SPVs c) REIT to hold controlling interest and =>51% of equity share capital of the SPVs • =>90% of REIT assets / proportionate SPV assets to be completed and rent generating (i.e. =>75% area to be rented) • =<10% REIT assets to be- a) Development properties with 3-year lock-in post-completion and leased out b) Debt of companies c) Listed shares of companies earning =>75% revenues from real estate activity d) Government securities, money market instruments, mortgage-backed securities • Investment in single project permitted if asset value is =>INR 1,000 crore • Investments in other REITs not permitted • Co-investors not to have more favourable terms than the REITs
5	Dividend policy	• =>90% of post-tax income to be distributed • Dividend declared to be paid within 15 days
6	Public offer	• Minimum market capitalisation – INR 1,000 crore • Minimum float – 25% • Minimum offer size – INR 250 crore • Foreign investment permitted, subject to exchange control regulations • Unit size – INR 1 lakh; Minimum subscription – INR 2 lakh
7	Listing / Delisting	<i>Listing</i> • Mandatory listing within 15 days of IPO • Trading of units permissible only through stock exchange <i>Delisting</i> • Mandatory if public float <25%; number of unitholders (other than Related parties to REIT) is <20 • Voluntary delisting subject to approval of =>75% unitholders by value and number
8	Key roles and obligations	<i>Trustee</i> • Ensuring proper legal and marketable titles • Execution of Investment Management Agreement • Overseeing Manager's activities and operations • Review of related party transactions • Appointing a new Manager within 3 months in the case of vacancy

		<i>Manager</i> • Identifying and recommending investment opportunities • Complying with the investment conditions and strategy • Constituting a minimum 5 member Investment Committee • Appointing other service providers • Undertaking lease management (directly or through agents) • Overseeing development activities and ensuring leasing the assets after completion • Distributing dividends • Ensuring half-yearly audit, valuation and reporting to its Board • Reporting to the Trustee on prescribed matters <i>Sponsor</i> • Minimum pre-IPO holding =>25% a) 3-year lock-in of 25% of pre-IPO holding b) 1-year lock-in for balance pre-IPO holding • Continued holding of =>15% units of REIT. • Divestment of 15% continued holding subject to- a) Possible only after 3 years from date of listing; and b) Another Sponsor acquiring the minimum holding with prior approval of unitholders <i>Valuer</i> • Impartial, true and fair valuation of real estate assets • Remuneration not to be linked to valuation • Exercising diligence and ensuring adequately experienced team
9	Related party transactions	<i>General</i> • To meet arm's length pricing requirement • To be consistent with the investment strategy and objective of the REIT • Specific disclosure to be made to stock exchanges and unitholders <i>Property transactions</i> • 2 valuation reports • Purchase price to be =< average valuation • Sale price to be => average valuation • Leasing subject to the following- a) Lease area, value of assets, rental income to be =<20% of underlying assets b) Fairness opinion to be obtained from an independent valuer

		<i>Other related party transactions (post-IPO)</i> • Prior unitholders' approval is required (whether by way of a single transaction or beyond the threshold) for - a) Investment in securities / acquisition of properties >5% of value of REIT b) Rentals from related parties >5% of total rentals c) Borrowings from related parties >5% of total borrowings
10	Valuation	• Full valuation (in prescribed format) to be undertaken by Principal valuer • Acquisition price – cap of 110% of Principal valuer's valuation • Sale price – floor of 90% of Principal valuer's valuation
11	Leveraging	• Borrowings and deferred payments to be =<50% of value of assets • Borrowings and deferred payments >25% of the value of assets are subject to- a) Credit rating b) Approvals of =>75% unitholders by value and number • 3-month cure period in the case of movement in price of assets/ securities
12	Governance aspects	• Convening unitholders meetings at least once a year. Maximum gap between meetings to be 18 months • General matters in annual meetings – approval of =>60% unitholders required (by value and by number) • Approval of => 75% unitholders required (by value and by number) for a) Related Party transactions b) Transaction value =>15% of REIT assets c) Change in investment strategy / manager d) Acquisition of units in excess of 50% by a non-Sponsor along with associates • Change in Sponsor a) Prior approval of =>60% of unitholders; or b) Providing an exit option to all unitholders • Annual report to be provided to unitholders within 2 months from end of Financial Year; Half-yearly report to be provided within 1month • Price-sensitive information to be disclosed to stock exchange

We give overleaf a comparative table of REIT regulations in different countries.

REITs worldwide

Country	Legal form	Minimum investment in real estate	Shareholding	Minimum dividend payout ratio	Taxation of REIT
USA (1960)	Corporation, Trust or an Association	75%	Largest 5 shareholders can hold up to 50%.	90%	Not taxable to the extent distributes its taxable income
Australia (1971)	Trust	None	None	Not Specified	Exempt if distributes 100% of its taxable income.
Japan (2000)	Investment trusts / Corporations	95% real asset and liquid assets	Lead investors may hold up to 75% Minimum 1,000 investors other than lead investors	90%	Not taxable to the extent distributes its taxable income
Singapore (2002)	Trust	70% in real estate and real estate related assets	Minimum public float applies	90%	Tax transparent in respect of taxable income distributed
Hong Kong (2003)	Listed Unit Trust	100%, directly or indirectly through SPVs	None	90%	REIT and SPVs generally taxed. Unit holder exempt.
UK (2007)	Company or group of companies with a parent	75%	Minimum public float applies	90%	Exempt for property-letting business
India – as proposed	Listed Trust	90%, directly or indirectly through SPVs	Minimum public float (25%) applies	90%	Yet to be prescribed

(Source: Compare and Contrast –Worldwide REIT Regimes, May 2013, a PwC Publication)

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