

Frequently Asked Questions (FAQs) - Framework for Small and Medium REITs (SM REITs)

DISCLAIMER – *This is not a legal document. These FAQs offer only a simplistic explanation / clarification of terms / concepts related to the SEBI (Real Estate Investment Trusts) Regulations, 2014 [“REIT Regulations”]. Any such explanation / clarification that is provided herein should not be regarded as an interpretation of law nor be treated as a binding opinion / guidance from the Securities and Exchange Board of India [“SEBI”]. For full particulars of laws governing SM REITs, please refer to actual text of the Acts / Regulations / Circulars appearing under the Legal Section on the SEBI website.*

1. What is the basic difference between the framework for a SM REIT and the existing REITs?

- As per the REIT Regulations, the value of assets under existing REIT should be at least rupees 500 crores. The framework for SM REIT allows for a reduced asset value of rupees 50 crores with a view to facilitate pooled investment in real estate assets or properties, thereby facilitating further growth of REITs in India.
- Further the existing REIT structure is a single pool of investor money i.e. all new assets acquired by the REIT are added to the same pool of assets and accordingly all unitholders have beneficial interest in the entire pool of assets under the REIT. However, in the SM REIT structure, a single SM REIT can launch multiple schemes for investment in real estate assets (similar to mutual funds). Accordingly, a SM REIT can house different real estate assets under different schemes and each scheme will have its own set of unitholders.

2. Can a real estate developer launch its own SM REIT? OR Can real estate developers list their assets and become the Investment Manager of the SM REIT?

- REIT Regulations provide the eligibility conditions for the Investment Manager under Regulation 26J(2)(d), hence any company including a real estate developer satisfying the eligibility conditions can act as the Investment Manager for a SM REIT.
- However, if a developer is the Investment Manager of the SM REIT, then it will not be able to transfer its own assets to the SM REIT as the SM REIT framework does not permit related party transactions.

- The SM REIT framework aims to bring professional Investment Managers to sponsor SM REIT to acquire and manage third party assets on behalf of unitholders through specific scheme/s established for the same.

3. Can a real estate developer be the tenant of the property which is held under a SM REIT?

- REIT Regulations do not impose any restriction on who can be the tenant of the property held under a SM REIT. However, the regulations provide that a SM REIT shall not enter into any transaction with related parties and the term '*related party*' is defined in Regulation 2(1)(zo)¹ of the REIT Regulations. Accordingly, a real estate developer can be a tenant of the property held under a SM REIT provided the developer does not fall within the ambit of related party under the REIT Regulations.

4. Can the Investment Manager launch multiple schemes under a SM REIT?

- REIT Regulations provide flexibility to the Investment Manager to launch multiple schemes under a single SM REIT. However, the Investment Manager and the trustee should ensure that the assets of each scheme, the bank accounts, investment or demat accounts and the books of accounts of each scheme are segregated and ring-fenced.

5. SM REIT can launch multiple schemes. In this case what will be the legal form / legal identity of a scheme of SM REIT?

- REIT Regulations defines a scheme as a distinct and separate scheme of a SM REIT launched under the regulations for owning of real estate assets or properties through special purpose vehicles. The scheme structure under a SM REIT is similar to the distinct schemes in a mutual fund. Further, the regulations mandate that assets of each scheme, the bank accounts, investment or demat accounts and the books of accounts of each scheme should be segregated and ring-fenced.

**6. Can a single scheme of SM REIT invest in multiple Special Purpose Vehicles (SPVs)? OR
Can two different real estate assets be held under one scheme?**

¹ Regulation 2(1)(zo) of the REIT Regulations states as under:
"related party" shall be defined under the Companies Act, 2013 or under the applicable accounting standards and shall also include:

(i) parties to the REIT;
(ii) omitted
(iii) promoters, directors and partners of the persons in clause (i)

- Yes, a single scheme of a SM REIT can invest in multiple SPVs subject to compliance with REIT Regulations. Also, two different real estate assets can be held under one scheme within a SM REIT.

7. As per REIT Regulations, the SPV shall directly and solely own all assets that are acquired or proposed to be acquired by the scheme of the SM REIT, of which SPV is the wholly owned subsidiary. Is there any limit on number of SPVs in a single scheme?

- There is no limit on the number of SPVs that can be held within a single scheme of a SM REIT. However, each SPV should solely and directly own all the assets under it.

8. Can multiple SPVs jointly own a single property?

- REIT Regulations require that the SPV shall directly and solely own all assets that are acquired or proposed to be acquired by the scheme of the SM REIT, of which SPV is the wholly owned subsidiary. Hence, multiple SPVs cannot jointly own a single property.

9. Is there any limit on the number of real estate assets which can be housed in a single SPV? Example: 5 real estate assets of rupees 10 crores each in a single special purpose vehicle is satisfying eligibility criteria.

- There is no limit on the number of real estate assets that a single SPV can hold under the REIT Regulations. Further, the collective value of assets proposed to be acquired under a single scheme should be at least rupees fifty crores and should not exceed rupees five hundred crores.

10. Is it permitted for a SM REIT to launch three schemes with proposed asset size of rupees 450 crore in each scheme thereby meaning a total proposed asset size under the SM REIT of rupees 1350 crores?

- REIT Regulations require that the size of the asset proposed to be acquired in a scheme of SM REIT should be at least rupees fifty crores and less than rupees five hundred crores. Further, multiple schemes can exist under a SM REIT and there is no cap on the collective value of assets held across all schemes under a SM REIT. Accordingly, three schemes with proposed asset sizes of rupees 450 crores each (and totaling rupees 1350 crore) is permitted.

11. The term ‘Special Purpose Vehicle’ or ‘SPV’ is defined under Regulation 2(1)(zs) as well as under Regulation 26H(f) of the REIT Regulations. Which definition of SPV should be considered for the purpose of SM REIT?

- Regulation 26H of the REIT regulations provide that for the purpose of Chapter VIB which lays down the provisions for SM REITs, the terms defined under the Chapter shall have the meanings as assigned therein. Accordingly, for the purpose of SM REIT, the definition of SPV given under Regulation 26H(f)² shall be applicable.

12. Can the property be bought (and warehoused) in a related entity of the Investment Manager and then brought in as part of a SM REIT Scheme? OR Can an AIF Category II fund with an Investment Manager that is a group company of the SM-REIT's Investment Manager sell its assets to the SM-REIT?

- REIT regulations provide that the SM REIT shall not enter into any transaction with related parties. The term ‘related parties’ has been defined under the REIT Regulations. Accordingly, a SM REIT cannot acquire any asset from an entity which falls within the definition of ‘related party’.

13. Is there any guideline on capping of fees of Investment Manager?

- There is no guideline on capping of fees of the Investment Manager as on the date of publication of this FAQ. However, at the time of initial offer of the scheme, the Investment Manager is required to make disclosure of the fees charged to the scheme of SM REIT by the Investment Manager. Further, for any change in fees payable to the Investment Manager, approval from unitholders of the scheme of the SM REIT is required, where votes cast in favour of the resolution shall not be less than one and a half times the votes cast against the resolution.

14. Can a scheme of SM REIT be slowly folded by exiting from the properties one by one?

- REIT Regulations mandate that the Investment Manager shall apply for delisting of units of the scheme of SM REIT if there are no projects or assets remaining under the scheme of SM REIT for a period exceeding six months. This period may be extended by further six months with the approval of

² Regulation 26(H)(f) states as under:

“special purpose vehicle” or “SPV” means any company which is a wholly owned subsidiary of the scheme of the SM REIT and the SPV shall not have any other capital or ownership interest in it;

unitholders in the manner as specified in regulation 26ZM of the REIT Regulations.

- Accordingly, a scheme of SM REIT shall be subject to delisting and winding up if all the assets under the SM REIT are gradually sold and all sale proceeds are gradually distributed to the unitholders.

15. Is there any requirement to take approval from SEBI in case there is any shareholding change in the Investment Manager?

- Prior approval from SEBI as well as unitholders is required in case of shareholding change in the Investment Manager if it amounts to change in control of the Investment Manager. It may be noted that ‘*change in control*’ is defined under Regulation 2(1)(g)³ of the REIT Regulations. Further, prior approval from SEBI as well as unitholders is also required for any change in the Investment Manager due to removal or otherwise.

16. Are foreign investors allowed to invest in the Investment Manager? Are there any restrictions on promoters of Investment Manager?

- REIT Regulations do not impose any restriction with regard to the shareholders and promoters of the Investment Manager. However, the Investment Manager shall be a company incorporated in India and is required to meet the eligibility criteria specified in the REIT Regulations. Further, all details related to the Investment Manager specified in the regulations including shareholding pattern of the Investment Manager are required to be submitted to SEBI at the time of filing of an application for registration of SM REIT.

17. Can a distributor be engaged by a SM REIT to market its offer?

- REIT regulations does not envisage engagement of a distributor separately by a SM REIT. However, the public issue of units of a scheme of SM REIT shall be made through the stock exchange platform. Further, there is a requirement of appointment of merchant banker for carrying out the obligations related to the public issue. The merchant banker will, *inter-alia*, take up the responsibility

³ Regulation 2(1)(g) of the REIT Regulations state as under:

“change in control”, -

(i) in case of a body corporate, -

(A) if its shares are listed on any recognized stock exchange, shall be construed with reference to the definition of control in terms of regulations framed under clause (h) of sub-section (2) of section 11 of the Act;

(B) if its shares are not listed on any recognized stock exchange, shall be construed with reference to the definition of control as provided in sub-section (27) of section 2 of the Companies Act, 2013 (18 of 2013);

(ii) in a case other than a body corporate, shall be construed as any change in its legal formation or ownership or change in controlling interest.

Explanation- For the purpose of sub-clause (ii), the expression “controlling interest” means an interest, whether direct or indirect, to the extent of not less than fifty percent of voting rights or interest;

of marketing the issue and the investors will apply for subscription of units of the scheme of SM REIT through securities market intermediaries at the stock exchange platform.

18. Can Investment Manager market the scheme of SM REIT after filing the draft offer document but before receiving in-principle approval of stock exchange to list the scheme?

- REIT regulations require that the draft scheme offer document, once filed with SEBI, shall be made public for comments by hosting it on the websites of SEBI, designated stock exchanges and merchant bankers associated with the issue for a minimum period of twenty-one days.
- Further, REIT Regulations also permit Investment Manager to provide link to the scheme offer document for investors on the website of SM REIT. Accordingly, once the draft scheme offer document is filed with SEBI and made public, the merchant banker can then do marketing for attracting investor interest. However, any public communication including advertisement, publicity material, research reports, etc. concerned with the issue should not be misleading and should not contain any matter extraneous to the contents of the scheme offer document.

19. Is there a defined threshold ratio of 'Other Expenses' to Asset Cost by SEBI?

- REIT Regulations require the scheme offer document to disclose the total expense ratio for the scheme of SM REIT to ensure transparency to the investors about the costs associated with their investment. However, the regulations do not provide any specific threshold ratio of 'Other Expenses' to Asset Cost for SM REITs.

20. Is there a defined threshold of cap rate (net rental yield) to launch a SM REIT?

- REIT Regulations do not specify a minimum cap rate (net rental yield) for coming out with a SM REIT. However, the investment conditions stipulated in the regulations *inter-alia* require that the scheme of SM REIT invests at least ninety-five per cent of the value of the schemes' assets in completed and revenue generating properties in order to ensure a stable income stream for the unitholders.

21. Will the book building process for SM-REITs be a fixed-price mechanism or an auction-driven mechanism?

- REIT Regulations require the Investment Manager of the SM-REIT to use the book building platform of stock exchanges to accept bids from investors for units of the scheme of SM REIT. The regulations do not envisage fixed-price issue for units of a scheme of SM REIT.

22. Is migration of existing structures with fractional real estate assets mandatory? If migration is not mandatory, can fractional real estate firms selectively choose which existing assets to migrate and which to retain?

- The migration of existing structures with fractional real estate assets into the SM REIT structure is not mandatory if such structure does not fall under the ambit of the definition of REIT.
- REIT Regulations require that an applicant for SM REIT (i.e. entity seeking to be the Investment Manager) undertake due migration of existing structures, and accordingly, the applicant shall submit details of existing structures proposed to be migrated and a migration plan along with the application for registration.
- It is noted that REIT Regulations also require that the Investment Manager of SM REIT shall ensure that the trademark, brand name, website and other medium of communication of the SM REIT are used exclusively for the activities of SM REIT and no links or information about any other entity, structure or person shall be made available on its website or on any other medium of communication.

23. Are entities allowed to use trademarks, brand names and websites utilized for SM-REIT for other SEBI-regulated entities, such as an AIF?

- REIT Regulations require that the trademark, brand name, website and other mediums of communication of the SM REIT are used exclusively for the activities of the SM REIT, hence it cannot be used for any other activities including for SEBI regulated entities. It aims to prevent confusion among the investors and to ensure that the communication channels of SM REIT are solely dedicated to its operations.

**24. If an asset is migrated, is the Investment Manager required to comply with the five percent minimum holding requirement? OR
If an asset is migrated, is the Investment Manager required to comply with the requirements pertaining to asset size and minimum number of unitholders?**

- No. The compliance with minimum unitholding requirement by the Investment Manager is exempt for units issued against swap of securities which were allotted prior to the date of notification of SM REIT regulatory framework (i.e. March 08, 2024) while migrating existing structures in SM REIT, subject to the applicant submitting an application for registration within six months from the date of notification and the migration being completed within six months from the date of grant of registration.
- Further, in relation to migration of existing structures, the requirements pertaining to asset size and minimum number of unitholders stipulated in Regulation 26P(2)⁴ of the REIT Regulations are not applicable, subject to the applicant submitting an application for registration within six months from the date of notification and the migration being completed within six months from the date of grant of registration.

25. In cases where more than 75% of investors of an asset under the fractional real estate model opt for transition to SM-REIT, but a few choose not to, what process must be followed? Can investors unwilling to transition to SM-REIT exit through a fresh public offering at the time of migration?

- REIT Regulations do not prescribe any approval threshold from existing security holders for migration of existing structure to SM REIT. Migration to SM REIT should be in accordance with the extant legal and contractual rights and obligations (including drag-along, buy-back, buy-out or redemption, as applicable) governing the existing security holders and the SPV.
- Once migration is complete and units of scheme of SM REIT are issued to investors against previously held securities, and duly listed, then the investor may sell the units in the secondary market.

26. Can the Investment Manager (or its group company) of a SM REIT also manage investments under the existing fractional real estate model?

- REIT Regulations require the Manager of a REIT to ensure that it has adequate controls in place to ensure segregation of its activity as Manager of REIT from

⁴ Regulation 26P(2) of the REIT Regulations state as under:

No offer of units by a scheme of the SM REIT shall be made unless,–

(a) the size of the asset proposed to be acquired in a scheme of the SM REIT is at least rupees fifty crores and less than rupees five hundred crores; and

(b) the minimum number of unitholders of the scheme of the SM REIT other than the investment manager, its related parties and associates of the SM REIT are not less than two hundred investors:

Provided that nothing in this sub-regulation shall be applicable to the migration of existing persons, entities or structures as on the date of this chapter coming into force which are included as part of the migration plan in case the applicant is applying for a certificate of registration under sub-regulation (1) of regulation 26N.

its other activities. Further, the Manager shall ensure that it has adequate infrastructure and sufficient key personnel with adequate experience and qualification to undertake management of the REIT at all times. These provisions are also applicable to the Investment Manager of a SM REIT.

- Further, the Investment Manager (or its group company) while doing activities other than management of SM REIT, shall ensure compliance with the provision of REIT Regulations that mandates Investment Manager of SM REIT to ensure that the trademark, brand name, website and other medium of communication of the SM REIT are used exclusively for the activities of SM REIT and no links or information about any other entity, structure or person shall be made available on its website or on any other medium of communication.

27. Will performance-linked fees such as ‘Carried Interest’ allowed under SM-REITs?

- No. Carried interest is not allowed for SM REITs.

28. Are investments in warehousing assets with minimum area of 1 lakh sq. ft. and minimum investment of rupees 25 crores permissible, considering their classification as ‘Infrastructure’?

- No. REIT Regulations require that any asset falling under the purview of ‘infrastructure’ shall not be considered as ‘real estate’ or ‘property’ for the purpose of REIT Regulations. Accordingly, since a warehousing facility with investment of minimum rupees 25 crores and minimum area of 1 lakh sq. ft. is classified as infrastructure, a SM REIT cannot make investment in such asset. However, if such warehouse falls under the common infrastructure forming part of composite real estate projects, industrial parks and SEZ, then such investments shall be permitted by SM REIT.

29. In cases where the sum of deposit and reserves exceed 5% of the assets at the scheme level, potentially limiting the investment in real estate assets to less than 95%, what will be the resolution?

- REIT Regulations require that the scheme of SM REIT shall invest at least ninety-five percent of the value of the schemes’ assets for each of its schemes in completed and revenue generating properties. Also, up to five percent of the value of the schemes’ assets may be invested in liquid assets, which shall be unencumbered.

- As regards the security deposit received from tenants, it will not form part of assets of the scheme of SM REIT for the purpose of compliance with investment conditions stipulated in the REIT Regulations.
- With regard to reserves, it is reiterated that reserves are created out of profits hence the same can be distributed to unitholders in order to ensure compliance with REIT Regulations.
- Further, in cases where reserves and/or other investments exceed five percent of the value of the schemes' assets, the same would result in violation of the REIT Regulations and the Investment Manager would need to reallocate funds or adjust the schemes' financial structure to ensure compliance with the ninety-five percent investment threshold in completed and revenue generating properties, thus maintaining the primary investment focus of the SM REIT.

30. Please provide clarity on which expenses will be included in the calculation of the 'Total Expense Ratio'.

- The total expense ratio for a SM REIT scheme would encompass all annual operating expenses, including but not limited to management fees, advisory fees, trustee fees, audit fees, and other operational costs directly attributable to the scheme. The total expense ratio is required to be disclosed in the scheme offer document, ensuring transparency to investors regarding the costs associated with their investment.

31. Can residential properties come under SM REIT?

- Yes. REIT Regulations does not differentiate between commercial and residential properties. Any real estate asset satisfying the definition of 'real estate' or 'property' provided under Regulation 2(1)(zi)⁵ of the REIT Regulations can be acquired and held subject to the real estate asset being completed and revenue generating.

⁵ Regulation 2(1)(zi) of the REIT Regulations states as under:

"real estate" or "property" 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 any asset falling under the purview of 'infrastructure' as defined vide Notification of Ministry of Finance dated October 07, 2013 including any amendments or additions made thereof shall not be considered as 'real estate' or 'property' for the purpose of these regulations;

Notwithstanding the above, following captured within the abovementioned definition of infrastructure shall be considered under "real estate" or "property",-

(i) hotels, hospitals and convention centers, forming part of composite real estate projects, whether rent generating or income generating;

(ii) common infrastructure" for composite real estate projects, industrial parks and SEZ;

**32. If few parts of the property are not completed and revenue generating but will become later, then can such properties come under the SM REIT scheme?
OR**

Can a property that is under-construction at this point, but will be revenue generating later, come for migration to SM REIT?

- REIT Regulations mandate that SM REIT shall invest only in completed and revenue-generating properties. Properties that are either not completed (i.e. under-construction properties) or are non-revenue generating cannot be held under a SM REIT.

33. Can land be brought under the framework of SM REIT?

- REIT Regulations defines 'real estate' or 'property' as land and any permanently attached improvements to such land, hence it is clarified that vacant land cannot be brought under the framework of SM REIT.

34. Can the Investment Manager take up facility management of the properties under a SM REIT?

- REIT Regulations require that the Manager of a REIT shall undertake management of the REIT assets including lease management, maintenance of the assets, regular structural audits, regular safety audits, etc. either directly or through the appointment and supervision of appropriate agents. These provisions are also applicable to the Investment Manager of a SM REIT.
- REIT regulations also require that a SM REIT shall not shall not enter into any transaction with related parties including transactions for facility management and property management. However, payment of fees by the SM REIT to the Investment Manager and Trustee for carrying out the activities of SM REIT is permitted.
- Hence, facility management of properties under a SM REIT by the Investment Manager is permitted.

35. Can one asset be disposed, potentially reducing the asset size of a scheme of SM REIT below the fifty crores threshold post partial exit?

- REIT Regulations require that the value of real estate assets or properties in each scheme of SM REIT should be at least fifty crore rupees. Further, the Investment Manager of SM REIT shall apply for delisting of units of the scheme of SM REIT to SEBI and the stock exchanges if there are no projects or assets remaining under the scheme of the SM REIT for a period exceeding six months

(which can be extended by further six months with unitholders approval). Accordingly, the Investment Manager should strive to ensure continuous compliance with the regulations including minimum asset size requirement.

36. REIT Regulations require that the minimum price of each unit of the scheme of the SM REIT shall be rupees ten lakhs. For migration of existing structures, units of scheme of SM REIT will be issued against the securities already held by the investors. In such a case, if the value of securities already held by the investors is not in multiples of rupees ten lakhs, how will the issue of units of scheme of SM REIT happen i.e. how to deal with odd value of securities?

- REIT Regulations do not contain any provision to deal with odd value of securities (i.e. which is not in the multiple of rupees ten lakhs) held by investors of existing structures. Hence, existing structures proposing to get migrated to the listed space shall have to align their investment value in multiples of rupees ten lakhs before migration into SM REIT. Towards this end, the following methods may, *inter-alia*, be explored –
 - Holders of such securities may consider inter-se sale/purchase of securities;
 - The SPV may undertake buy-back or redemption of a portion of existing securities in compliance with applicable laws; OR
 - The SPV may consider establishing a trust for holding of the odd-value of securities, which can consolidate the units issued in lieu thereof into lots of rupees ten lakhs and dispose such units in the market within one year from migration to the SM REIT scheme and distribute the proceeds net of expenses, to the person/s to whom the odd-value of securities pertained.

37. With regard to migration of existing SPV to the SM REIT, what will be the treatment of convertible debentures issued by such SPV to the existing investors at the time of migration. Also, will it be included for the purpose of computation of leverage as per Regulation 26U(5)?

- With regard to convertible debentures issued by an existing SPV which is proposed to be migrated to the SM REIT, the applicant may consider conversion of such debentures into equity shares of the SPV before migrating under the SM REIT.
- However, if the conversion is not done before migration to SM REIT then following will apply –
 - convertible debentures issued by existing SPV prior to migration into the SM REIT, may be swapped for units of the scheme of SM REIT and the scheme

of SM REIT will hold such convertible debentures. The existing debenture holders will receive units of the scheme of SM REIT against the convertible debentures held by them.

- Further, the ceiling limit for leverage prescribed under Regulation 26U(5) is applicable at the scheme level and accordingly borrowings made by the SPV by issuance of convertible debentures which are held by the scheme of SM REIT will not be included in the leverage limits under Regulation 26U(5).

38. Use of Certain Words/Expressions in the Proposed Name of SM REIT.

The Applicant seeking registration as a SM REIT from SEBI, may apply for registration under a name which is not suggestive of patronage from Govt. of India. The proposed name of SM REIT shall not contain the words "India", "Indian", "National" or "Bharat" etc.