

Proposed Amendments to SEBI (Infrastructure Investment Trusts) Regulations, 2014 and the SEBI (Real Estate Investment Trusts) Regulations, 2014

1. Objective

- 1.1. This Board Memorandum proposes amendments to the SEBI (Infrastructure Investment Trusts) Regulations, 2014 (hereinafter referred to as "InvIT Regulations") and SEBI (Real Estate Investment Trusts) Regulations, 2014 (hereinafter referred to as "REIT Regulations") and seeks approval of the Board for the same.

2. Background

- 2.1. A few amendments were proposed to the InvIT and REIT Regulations to the Board, in its meeting held on September 18, 2017. Of the proposals made in the memorandum, following were approved by the Board:
 - 2.1.1. Allowing REITs and InvITs to raise debt capital by issuing debt securities
 - 2.1.2. Introducing the concept of Strategic Investor for REITs on similar lines of InvITs
 - 2.1.3. Allowing single asset REIT on similar lines of InvIT
 - 2.1.4. Allowing REITs to lend to underlying Holdco/SPV
 - 2.1.5. Amending the definition of valuer for both REITs and InvITs
- 2.2. However, on the proposal of allowing REITs and InvITs to invest in Holdco/SPVs with 50% stake, Board took following decision (Board minutes placed at **Annexure A**):
 - 2.2.1. No changes in the InvIT Regulations on the captioned matter.
 - 2.2.2. SEBI to have further consultation with the stakeholders on the proposal of allowing REITs to invest with at least 50% of the equity share capital or interest in the underlying Holdco/SPVs, and similarly allowing Holdco to invest with at least 50% of the equity share capital or interest in the underlying SPVs.
- 2.3. Subsequently, consultations were held with various market participants viz. industry association i.e. Asia Pacific Real Estate Association (APREA), merchant bankers, issuers, private equity players, , law firms, etc. and the issue was discussed.

3. Amendments proposed in REIT and InvIT Regulations:

In light of the discussions held with the market participants on the aforesaid matter and inputs received thereafter, following is proposed:

3.1. **Allowing REITs to invest in Holdco/SPVs with 50% stake**

3.1.1. **Current regulatory requirement:**

- i. Regulation 2(1)(qa) and Regulation 2(1)(zs) of the REIT Regulations, inter-alia, require that a REIT shall hold or propose to hold controlling interest and not less than 51% of the equity share capital or interest in the underlying Holdco/SPVs. Further, a Holdco, as well, shall hold controlling interest and not less than 51% of the equity share capital or interest in the underlying SPVs.
- ii. Regulation 18(3A)(a) of REIT Regulations mandates that the ultimate holding interest of the REIT in the underlying SPV(s) is not less than 26 %.
- iii. Also, Regulation 18(3)(b) and Regulation 18(3A)(c) of the REIT require that the manager of the REIT/InvIT, in consultation with the trustee, shall appoint the majority of the Board of directors or governing board of such holdco/SPVs.

3.1.2. **Genesis of current regulatory structure**

- i. At the time of notification of REIT Regulations, in September 2014, only one level SPV structure was allowed for investment i.e. REIT were allowed to invest in assets either directly or through a SPV. Further, if investment is made through a SPV, REIT was required to hold atleast 50% of the equity share capital or interest and appoint atleast one director on the board of SPV.
- ii. Subsequently, amendments to REIT Regulations were proposed to Board in its meeting held on September 23, 2016. One of the amendment proposed was to allow REIT to invest in real estate assets through a two level holding structure as well i.e. REIT invests in a Holding Company and that Holding company in turn holds stake in SPVs, which hold assets. The amendment was proposed, keeping in view the industry representation that the real estate assets are usually held through multiple layers of investments. The proposal, inter-alia, included following:
 - a) The REIT shall hold controlling interest and not less than 50% of the equity share capital or interest in the HoldCo. The Holdco shall in turn hold controlling interest and not less than 50% of the equity share capital or interest in underlying SPV(s).
 - b) The manager, in consultation with the Trustee, shall ensure that the REIT or the HoldCo appoints the majority of the Board of directors or governing board of the underlying SPV(s).

- iii. Proposal was approved by the board with following requirements:
- a) REIT shall hold controlling interest and not less than 51% of the equity share capital or interest in the underlying Holdco/SPVs. Further, a Holdco, as well, shall hold controlling interest and not less than 51% of the equity share capital or interest in the underlying SPVs.
 - b) Ultimate holding interest of the REIT in the underlying SPV(s) is not less than 26%.
 - c) The manager of the REIT, in consultation with the trustee, shall appoint the majority of the Board of directors or governing board of such holdco/SPVs.

Board instructed the inclusion of abovesaid requirements so as to ensure that various requirements and compliances cast upon REIT under the Regulations, are complied with.

3.1.3. Request for change and rationale:

- i. Subsequent to the amendment, SEBI received representations that in Indian context, the joint venture is a model followed by many developers, where such JV partners are landowners or financials investors. Further, based on market practices, many real estate assets in India are owned and developed through 50:50 partnership structures / joint ventures.
- ii. Thus, ensuring a minimum of 51% shareholding in such situations could be challenging when the joint venture partner is not willing to roll over its interest into the REIT.
- iii. Further, mandating the REIT to hold at least 51% in the underlying SPVs would potentially rule out the inclusion of several economically viable assets within the REIT portfolio which are held as 50:50 joint ventures with other parties.
- iv. A few illustrations of jointly developed and/or jointly owned assets in India are as under:

S.No.	Project	Location	Developer	50% JV Partner
North				
1.	Capital Greens	Delhi	DLF	GIC
West				
2.	Equinox Business Park	Mumbai	Essar Group	RMZ
3.	R-City Mall	Mumbai	Runwal Group	GIC

4.	Eon Business Park	Pune	Panchshil Realty	Blackstone
5	Viviana Mall	Thane	Sheth Group	GIC
South				
6.	Hotel Project	Bengaluru	Salarpuria	Merrill Lynch
8.	Office Park	Hyderabad	Divyasree	NSL Infratech
9.	Development Project	Hyderabad	Salarpuria	Blackstone
10	Commercial Development	Hyderabad	My Home	RMZ
11	Waverock Office Development Project	Hyderabad	Tishman Speyer	GIC

- v. In this reference, the industry participants have brought out the key contours of a Joint Venture partnership, which are as under:
- a) **Similar rights, responsibilities and obligations:** Joint ventures by their very nature confer on both joint venture partners similar rights, responsibilities and obligations, which are essentially outlined in the JV agreement. Thus, each joint venture partner is entitled to its respective share in the entity and proportionate board seats but both parties are in joint control of the SPV (be it 50:50 or 51:49 structure).
 - b) **Unanimous consent of both parties required:** Given the equal distribution of rights, neither joint venture partner has the sole decision making ability for key decisions irrespective of the shareholding split (be it 50:50 or 51:49). Thus, unanimous consent of both parties is required in order to take any decision in the SPV. Therefore, decisions required to be taken at shareholders meetings including in relation to matters such as appointment of directors, alteration of share capital, amendments to charter documents, allotment of securities etc. cannot be taken without the concurrence of the other party.
 - c) **Limited Role of the Board:** Given that the unanimous consent of both parties is required to take key decisions; neither joint venture partner has the required strength or rights to take unilateral decisions, if any, on the Board. Therefore, a majority board in case of 51:49 scenario does not give the 51% shareholder the sole decision making ability, and unanimous consent of both parties will be required in order to take any decision in the SPV.

- vi. Thus, in light of above a unanimous consent of both parties is required to take key decisions in the SPV. Therefore any decision, by the other 50% holder(s) in SPV can be blocked by the REIT, which REIT believes is prejudicial to the interest of its unitholders.
- vii. However, any commercial decision in the underlying SPV, which REIT thinks is beneficial to unitholders, can effectively be passed only if both the JV partners agree to it, irrespective of REIT holding 51% or 50 % in the underlying SPV. Thus, in so far as it pertains to commercial decisions, consent of both the partners is required and a REIT whether holding 51% or 50% in the JV, may not be able to drive the agenda on its own.
- viii. Industry participants have therefore represented that in a REIT, with 50% shareholding and equal board rights in underlying Holdco/SPV, it is possible to comply with all the provisions under the REIT Regulations and safeguard the rights of unitholders.

3.1.4. Changes proposed:

- i. In view of the representations made above, the following is proposed:

S. No.	Existing Requirement/clause	Proposed amendment
1.	REIT to hold controlling interest and not less than 51% of the equity share capital or interest in the underlying Holdco/SPVs and Holdco to hold controlling interest and not less than 51% of the equity share capital or interest in the underlying SPVs.	REIT shall hold not less than 50% of the equity share capital or interest in the underlying Holdco/SPVs. Further, Holdco shall hold not less than 50% of the equity share capital or interest in the underlying SPVs.
2.	REIT to have ultimate holding interest of not less than 26% in the underlying SPV(s).	Existing clause to be retained.
3.	Manager of the REIT, in consultation with the Trustee, shall appoint the majority of the Board of directors or governing board of the holdco and/or SPV(s)	Manager of the REIT in consultation with the trustee, shall appoint at least such number of directors on the Board of Holdco/SPVs, in proportion to its shareholding in the Holdco and/or SPV

4.	No other shareholder or partner of the Holdco or the SPV(s) shall have any rights that prevent the REIT, the Holdco or the SPV(s) from complying with the provisions of these regulations and an agreement shall be entered into with such shareholders or partners to that effect prior to investment in the Holdco and/or SPVs	No other shareholder or partner of the Holdco or the SPV(s) shall exercise any rights that prevent the REIT, the Holdco or the SPV(s) from complying with the provisions of these regulations and an agreement has been entered into with such shareholders or partners to that effect prior to investment in the Holdco and/or SPVs.
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- ii. Further, following clauses be built in the regulations for the purpose of bringing more clarity and enforcement of the regulations:
 - a) in case of any inconsistencies between the shareholder/partnership agreement and the obligations cast upon REIT in the Regulations, the provisions of the REIT Regulations shall prevail.
 - b) an appropriate mechanism for resolution of disputes between the REIT and the other shareholders or partners in the SPV shall be agreed to.

3.2. **Rationalising the definition of Sponsor group in case of REITs**

3.2.1. **Current regulatory requirement:**

- i. Regulation 2(1)(zta) of the REIT Regulations defines sponsor group as

“sponsor group” – includes:

- (i) the sponsor(s);
- (ii) 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.
- (iii) in case sponsor is an individual:
 - a. 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
 - b. entities or person(s) which are controlled by such individual;

- ii. Regulation 4(2)(j) requires the declaration for fit and proper for all the sponsor group entities. Further, Para 7 of Schedule I of the Regulations require disclosures in regards for

any litigation connected with the securities market, history of any disciplinary action and refusal of certificate to, inter-alia, entities of sponsor group entities and their directors.

3.2.2. Request for change and rationale:

- i. Representations have been received that the current definition of the sponsor group is wide and given the way the ownership patterns are in Real Estate industry this may lead to numerous entities and SPVs, which are not controlled by the Sponsor or persons/entities controlling the Sponsor or are not connected in any manner with the business of the REIT or its assets, being categorised as part of sponsor group.
- ii. Hence, it has been requested that the regulations be amended so as to provide flexibility in identification of the sponsor group, such that the entities forming part of sponsor group shall be those which have a relationship with the business and operations of the REIT and which are enabling the sponsor to meet the eligibility criteria.

3.2.3. Changes proposed:

In view of the above, following is proposed:

- i. The existing definition of sponsor group, as provided in the REIT Regulations, shall remain as it is.
- ii. However, for the purposes of registration and disclosures, only those entities/individuals shall be required which satisfies any of the below mentioned criterions:
 - a. An individual/entity who is directly/indirectly holding a stake (interest/shareholding) in any of the assets/SPVs/HoldCos proposed to be transferred to REIT,
 - b. An individual/entity who is directly/indirectly holding units of the REIT on post issue basis
 - c. An individual/entity whose experience is being utilised by the sponsor for meeting with the eligibility conditions required under Regulation 4 of the REIT Regulations.

3.3. Enabling investment in unlisted shares under the 20% investment category

3.3.1. Current regulatory requirement:

- i. Regulation 18(5) of REIT Regulations provides as under:

"Not more than twenty per cent of value of the REIT assets shall be invested in assets other than as provided in sub-regulation (4) and such other investment shall only be in,-

(a) properties, which are:

- i. under-construction properties which shall be held by the REIT for not less than three years after completion;
- ii. under-construction properties which are a part of the existing income generating properties owned by the REIT which shall be held by the REIT for not less than three years after completion;
- iii. completed and not rent generating properties which shall be held by the REIT for not less than three years from date of purchase;

(b) listed or unlisted debt of companies or body corporate in real estate sector:

Provided that this shall not include any investment made in debt of the holdco and/or SPVs;

(c) mortgage backed securities;

(d) equity shares of companies listed on a recognized stock exchange in India which derive not less than seventy five per cent. of their operating income from real estate activity as per the audited accounts of the previous financial year;

(e) government securities;

(f) unutilized FSI of a project where it has already made investment;

(g) TDR acquired for the purpose of utilization with respect to a project where it has already made investment;

(h) money market instruments or cash equivalents."

3.3.2. Request for change and rationale:

- i. Request has been received to permit investment by REITs in unlisted equity shares of companies or body corporate in real estate sector within the limits prescribed under Regulation 18 (5) of REIT Regulations.
- ii. It has been represented that current REIT regulations permit REITs to invest in listed/unlisted debt and listed equity shares of companies in real estate sector within the limits prescribed by Regulation 18 (5). Further, the regulation also permits investment in more illiquid assets classes such as under construction assets and unutilized FSI. Such investments were permitted to allow REITs to make investments, within a limited band, in assets that could be valuable and allow flexibility over and above investing 80% of the REIT assets in completed and rent generating properties.

- iii. It has further been represented that, while REITs are allowed to invest in listed/unlisted debt and listed equity shares of companies in real estate sector, investment in unlisted equity shares of companies in real estate sector has been left out. Allowing such investment would be a natural extension of permitting investment in companies in real estate sector and would provide flexibility to REITs to invest in broad based investments without diluting the REIT regulations.
- iv. Further, it proposed that to safeguard the interest of unitholders and to ensure appropriate value of such unlisted shares are accurately reflected in the value of REIT assets, a mechanism can be introduced whereby such investments are required to be independently valued every quarter.

3.3.3. **Changes proposed and rationale:**

In view of the representation received, following is proposed:

- i. Existing Regulation 18(5)(a), which allows investment by REIT in under-construction properties and completed but non-rent generating properties, be amended so as to allow such investments both through companies/LLPs as well as directly.
- ii. In Regulation 18(5)(d), which allows investment in equity shares of listed companies which derive not less than seventy five per cent. of their operating income from real estate activity, amendment may be made so as to allow investments in unlisted equity shares of the companies which derive not less than seventy five per cent. of their operating income from real estate activity.

3.4. **Clarification or minor amendments to REIT and InvIT Regulations**

In the course of discussions with the market participants and in view of the experiences gained of the two public issues of the InvITs, it has come to notice that there are certain clarifications/minor amendments to be provided in the REIT and InvIT Regulations. The proposed amendments are aimed towards providing more clarity and coherent reading of the Regulations. The amendments proposed for REIT Regulations are placed at **Annexure-B** and for InvIT Regulations are placed at **Annexure -C (Both the annexures excised for the reason of confidentiality)**.

4. **Proposal to the Board**

- 4.1. The Board is requested to consider and approve the draft amendments to the SEBI (Real Estate Investment Trusts) Regulations, 2014 and SEBI (Infrastructure Investment Trusts) Regulations, 2014 as referred at point no. 3 above.

4.2. The Board is also requested to authorize the Chairman to make necessary amendments in SEBI (Infrastructure Investment Trusts) Regulations, 2014 and SEBI (Real Estate Investment Trusts) Regulations, 2014 and issuing circulars, wherever necessary with consequential and appropriate changes, as may be required.

4.3. The Board is also requested to authorize the Chairman to make amendments in the REIT and InvIT Regulations, which are either clarificatory in nature or are minor amendments.

(The Board Memorandum must be read in conjunction with the press release issued on December 28, 2017, minutes of the meeting and the amended regulations, as may be notified.)

Annexure-A

1. The Board deliberated on the proposals contained in the captioned agenda item and took note of the comments received from DEA (vide letter no. F. No. 11/09/2017-PM dated September 18, 2017) and MCA (vide letter no. F.No. 11/15/2017-CL V dated September 15, 2017) on the proposals. After deliberations, the Board decided as under on the following proposals:
 - a. Proposal of allowing REITs and InvITs to invest in Holdco/SPVs with 50% stake
 - (i) The Board decided that there need not be any changes in the InvIT Regulations on the captioned matter.
 - (ii) The Board decided to have further consultation with the stakeholders on the proposal of allowing REITs to invest with at least 50% of the equity share capital or interest in the underlying Holdco/SPVs, and similarly allowing Holdco to invest with at least 50% of the equity share capital or interest in the underlying SPVs.
 - b. Other proposals

The following proposals were approved by the Board:

 - (i) Allowing REITs and InvITs to raise debt capital by issuing debt securities, which would be necessarily listed and will be governed under SEBI ILDS and LODR Regulations, to the extent applicable
 - (ii) Amending the definition of valuer for both REITs and InvITs
 - (iii) Allowing single asset REIT in similar lines of InvIT
 - (iv) Introducing the concept of Strategic Investor for REITs on similar lines of InvITs
 - (v) Allowing REITs to lend to underlying Holdco/SPV

However, with regard to the proposal mentioned at point (iv) above, the Board felt that the proposal may be implemented subject to compliance with the provisions of FEMA, if applicable.

As regards the proposal mentioned at point (v) above, the Board approved the proposal subject to adequate disclosures and compliance with the provisions of the Related Party Transactions in the REIT Regulations. Further, the said disclosures and compliances shall be applicable for InvITs as well.
2. The Board also authorised the Chairman to take necessary steps to implement the aforesaid proposals by, inter-alia, amending the SEBI (REIT) Regulations, 2014, SEBI (InvIT) Regulations, 2014 and SEBI (ILDS) Regulations, 2008, and issuing circulars, wherever necessary with consequential and appropriate changes, as may be required.

