

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

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. SEBI had notified InvIT and REIT Regulations on September 26, 2014. Government of India has in the budget of 2014-15 introduced a separate chapter on the InvITs and REITs defining them together as "Business Trusts". Further, various tax related exemptions/clarifications have been provided to Business Trusts, in the budgets of 2014-15, 2015-16 and 2016-17.

2.2. InvIT and REIT Regulations were also amended and notified on November 30, 2016, giving effect to the amendments approved by the Board in its meeting held on September 23, 2016, which inter-alia included following:

2.2.1. Changes made to both REIT and InvIT Regulations

- i. Allowing REITs/InvITs to invest in two level holding structures with, inter-alia, following conditions:
 - a. REIT/InvIT shall hold or proposes 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.

- b. majority of the Board of SPV and Holdco to be appointed by Investment Manager, in consultation with the trustee.
 - c. ultimate holding interest of the REIT/InvIT in the underlying SPV(s) is not less than twenty six per cent
- ii. Rationalising the definition of associates and related parties and aligning them in line with the SEBI (Listing Obligations and Disclosure Requirement) Regulations.
 - iii. Aligning minimum public holding requirement with SCRR.

2.2.2. Changes made to REIT Regulations

- i. Allowing REITs to invest upto 20% in under construction assets
- ii. Removing the cap on the number of sponsors and allowing concept of sponsor group

2.2.3. Changes made to InvIT Regulations

- i. Reducing the mandatory sponsor holding in InvITs to 15% from 25%
- ii. Allowing InvIT to lend to underlying SPVs
- iii. Removing the cap on the number of sponsors

3. Current Status of InvITs and REITs

3.1. As on date, six InvITs and one REIT are registered with SEBI.

3.2. Two InvITs have got their units listed on Stock Exchanges, details of which are as under:

| S. No. | Name | Amount Raised (Rs Crore) |
|---------------|----------------|---------------------------------|
| 1. | IRB InvIT Fund | 5,032.9 |
| 2. | Indigrid Trust | 2,250 |

4. Market Representation

4.1. Subsequent to the last amendment SEBI has received various representations from the industry and market participants for making amendments to/providing clarity on REIT and InvIT Regulations.

4.2. The requested amendments are aimed towards providing structuring and operational ease to the InvITs and REITs. The said amendments will help in smoothen the process of registration of InvIT and REIT with SEBI and launching of the offer.

5. Proposal to the Board:

In light of the recommendations received from the market participants, the amendments/clarification proposed in the InvIT and REIT Regulations, along with the rationale, are as under:

A. Amendments proposed to both REIT and InvIT Regulations

5.1. (Details have been excised for reasons of confidentiality)

5.2. Allowing REITs and InvITs to raise debt capital by issuing Bonds

5.2.1. Current regulatory requirement:

Regulation 20(1) of the REIT and InvIT Regulations state as under:

"The aggregate consolidated borrowings and deferred payments of the REIT/InvIT, the Holdco and the SPV(s), net of cash and cash equivalents, shall never exceed forty nine per cent. of the value of the REIT/InvIT assets."

5.2.2. Representations received:

- i. It has been represented that the REIT and InvIT Regulations, though allow REITs/InvITs to leverage upto 49% of the value of its assets, but these Regulations do not clearly provide for the REIT/InvIT to raise debt capital through issuance of

debt securities, whether listed or unlisted. It is therefore, been requested to clarify the same in the REIT Regulations and the InvIT Regulations.

- ii. Further, RBI, vide circular number RBI/FED/2015-16/15 FED Master Direction No.5/2015-16, updated as on June 09, 2017, has allowed REITs and InvITs to issue rupee denominated bonds in overseas jurisdictions.

5.2.3. Changes proposed and rationale:

- i. In view of the representation as received at para 5.2.2 above, it is proposed that a clarification may be provided that one of the modes for undertaking leverage by REITs and InvITs may be by issuance of debt securities.
- ii. REITs and InvITs, as per regulations, are required to be set up as trust. However, currently the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (ILDS regulations), which governs the public issue and listing of debt securities and listing of privately placed debt securities, is silent on whether a trust can be identified as an issuer. It is therefore proposed that the ILDS Regulation be amended so as to clarify that a trust, registered with SEBI as REIT or InvIT and whose units are listed in nationwide stock exchanges, can issue debt securities.

5.3. Definition of the Valuer in case of both REITs and InvITs

5.3.1. Current regulatory requirement:

- i. Regulation 2(1)(zz) of the REIT regulations defines Valuer as under:

“valuer” means any person who is a "registered valuer" under section 247 of the Companies Act, 2013 or as defined hereunder and who has/have been appointed by the manager to undertake both financial and technical valuation of the REIT assets:

(a) a valuer in respect of financial valuation, means,-

- (i) a chartered accountant, company secretary or cost accountant who is in whole-time practice, or retired member of Indian Corporate Law Service or any person

holding equivalent Indian or foreign qualification as the Ministry of Corporate Affairs may recognize by an order:

Provided that such foreign qualification is acquired by Indian citizen.

- (ii) a Merchant Banker registered with the Securities and Exchange Board of India, and who has in his employment person(s) having qualifications prescribed under (i) above to carry out valuation by such qualified persons;

(b) a valuer in respect of technical asset valuation, means members of the following institutions for specific asset categories,-

- (i) Institution of Valuers;
- (ii) Institution of Surveyors (Valuation Branch);
- (iii) Institution of Government Approved Valuers;
- (iv) Practicing Valuers Association of India;
- (v) Centre for Valuation Studies, Research and Training;
- (vi) Royal Institution of Chartered Surveyors, UK;
- (vii) American Society of Appraisers, United States;
- (viii) Appraisal Institute, United States;
- (ix) Institute of Engineers;
- (x) Council of Architecture or the Indian Institute of Architects:

Provided that, the persons referred to in sub-sub-clause (i) and qualified person referred to in sub-sub-clause (ii) of sub-clause (a) above, shall have not less than five years continuous experience after acquiring membership of respective institutions:

Provided further that, the persons referred to in sub-sub-clauses (i) to (x) of sub-clause (b) above, shall have a minimum working experience of five years in relevant areas of valuation practice and in relation to relevant asset value and categories; and be citizens of India;"

- ii. Further, similar requirements are also provided under InvIT Regulations.

5.3.2. Representations received:

- i. SEBI is in receipt of various representations from various market participants requesting to modify the aforementioned list.

5.3.3. Changes proposed and rationale:

- i. The definition of the valuer, as provided in the InvIT Regulations and the REIT Regulations, was expanded in November 30, 2016. It was done so as to allow other classes of valuers including members of other professional bodies such as Institute of Government Approved Valuers, Institution of Valuers, Royal Institute of Chartered Surveyors (RICS), Practicing Valuers Association of India etc. which were recognized as per Indian Banks Association - National Housing Board handbook for the purpose of empanelment of valuers by the bank for the valuation of assets (IBA-NHB handbook), as referred at Regulation 2(1)(zz)(b) of the REIT regulations.
- ii. Thus, the definition of the valuer was amended to bring it in line with the requirements under the then draft rules under the Companies Act, 2013 and the IBA- NHB handbook.
- iii. Subsequently, following developments have happened:
 - a. IBA, vide circular no. OPR/CIR/2043 dated February 04, 2017, has revised its guidelines for Empanelment of Valuers by Banks. In the revised guidelines, the names of the professional bodies have been deleted and it now states that "every valuer empanelled by the banks or financial institutions in India be a member in good standing of any one of the associations of the valuers".
 - b. MCA, in this regard, has come out with the Companies (Registered Valuers and Valuation) Rules, 2017 which, inter-alia, provides the definition of registered valuers, requires registration of such registered valuers with the Registration authority, valuation standards to be followed etc. The rules are however currently in the draft stage and are yet to be notified.

- iv. In view of the developments as highlighted at point no. 5.3.3 (iii) above and in view of the evolving nature of this area, it is proposed to amend the definition of Valuers in the regulations as under:

(Excised, as the amendment is yet to be finalised)

5.4. Role of strategic investors in InvITs and REITs

5.4.1. Current regulatory requirement:

- iii. Regulation 2(1)(zza) of InvIT Regulations define Strategic Investors as under:

“strategic investor” means, -

- a. an infrastructure finance company registered with Reserve Bank of India as a Non Banking Financial Company;
- b. a Scheduled Commercial Bank;
- c. an international multilateral financial institution;
- d. a systemically important Non Banking Financial Companies registered with Reserve Bank of India;
- e. a foreign portfolio investors.

who together invest not less than five per cent of the total offer size of the InvIT or such amount as may be specified by the Board from time to time;

- iv. Further, the concept of strategic investor is not provided under REIT Regulations.

5.4.2. Representations received:

Representations have been received that the role of strategic investor be expanded and clarified in the InvIT regulations; and the concept of strategic investors be brought in case of REIT Regulations.

5.4.3. Changes proposed and rationale:

- i. The concept of Strategic Investors was built in InvIT Regulations so as to enable an InvIT to have Strategic investors in the issue, prior to making an offer of units and the intent behind having such category of investors was to instill confidence in the other set of investors.
- ii. As has now been represented we may allow Strategic Investor(s) to participate in REITs as well. Further, it is proposed that the role of Strategic investor be as under:
 - a) Strategic Investors, may be allowed to invest in the public issues of InvITs/REITs.
 - b) Other operational guidelines, with respect to the participation by strategic investors, shall be separately specified by SEBI.

B. Amendments proposed in REIT Regulations

5.5. Allowing Single asset REITs.

5.5.1. Current regulatory requirement:

- i. Regulation 14(2)(b) of the REIT Regulations require that the value of all the assets owned by REIT shall not be less than five hundred crore rupees.
- ii. Regulation 18(8) of the REIT regulations requires that a REIT shall hold at-least two projects, directly or through Holdco and/or SPV, with one project not more than 60% of the value of the REIT assets.

5.5.2. Representations received:

- i. Representations have been received that there are developers/private equity players which own/hold single large sized real estate asset which cannot fold into REITs because of the requirements as under Regulation 18(8), stated above.

- ii. It has therefore been requested that either the requirement of atleast two assets may be dispensed with or the percentage cap on one single asset forming part of REIT may be raised.

5.5.3. Changes proposed and rationale:

- i. The extant requirement of having atleast two assets in the REIT regulations have been put in place to so as to ensure diversification and risk mitigation for the investors in such REIT. However, there may be certain scenarios where both assets are placed in the same vicinity thus defying the very purpose of diversification. Further, specifying higher percentage for a single asset in a REIT may also not lead to any meaningful diversification.
- ii. On the contrary, as per the InvIT Regulations, an InvIT can hold single asset and there are no percentage holding restrictions in an asset.
- iii. It is therefore proposed that the extant regulatory requirement of atleast two assets and the percentage restriction on a single asset, in case of REITs, be done away with and we may allow REITs to be floated with one single asset, where the value of such asset shall comply with requirement of minimum size of assets as referred at point 5.5.1(i) above.

5.6. Allowing REITs to lend to underlying Holdco/SPV(s).

5.6.1. Current regulatory requirement:

Regulation 18(13) of the REIT regulation, inter-alia, doesn't allow the REIT to undertake lending to any person.

5.6.2. Representations received:

- i. It has been represented that real estate assets are normally financed by a mix of equity and debt (loan) from the financial institutions. Hence, in case of transfer of such assets from sponsor to a REIT, such transaction may require financing/

retiring the debt (loan) of such projects. Therefore, there is a need for allowing the REITs to lend to the underlying Holdcos/SPVs.

- ii. Notably, such lending to HoldCos/SPVs is allowed in case of InvIT Regulations. However, the same at present is not allowed in the REIT Regulations.
- iii. Further, at present, the REIT regulations allow the REITs to invest in debt securities and thus, a REIT can lend to an SPV through investment in the debt securities of the underlying SPVs. It has therefore been represented that direct lending may also be allowed under the REIT Regulations.

5.6.3. Changes proposed and rationale:

- i. InvIT Regulations allow InvITs to lend, however the same is restricted to the holdcos/SPVs in which the InvIT has invested in.
 - ii. It is therefore proposed that the REIT Regulations may be amended, in line with the InvIT Regulations, so as to allow lending to the Holdcos/SPVs in which the REIT has invested in.
6. The Board is requested to consider and approve the proposed amendments, as referred at paragraph no. 5 above, and authorize the Chairman to take necessary steps to implement the proposals by 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.

(The Board Memorandum must be read in conjunction with the minutes of the meeting, the press release issued on September 18, 2016 and the amended regulations, as may be notified.)