Indian real estate sector is going through a phase of changeover in the process of its development. From being an unorganized sector traditionally, the Indian real estate sector is gradually moving to become a more organized one. Financial crisis in 2008 impacted the Indian economy at large and the real estate sector in particular. The industry in India faced the heat of the global crisis in terms of a demand slowdown and more specifically severe liquidity crunch. An underdeveloped capital and debt market, coupled with limited options for raising funds further dampen cash blockage for the developers specially those who are owning or developing commercial assets. After 2008, there was a major transformation of the investment sentiment for this sector. In addition to traditional source of funding, the policy changed by Government of India (GOI) has opened up the floodgates for funds from global Real Estate Funds, Private Equity Funds, hedge funds, and strategic investors or foreign developers. Real Estate Investment Trusts (REITs) is a recent development in the area of investment vehicle of real estate sector. REITs markets first emerged in the 1960s in the US, followed by Australia in the early 1970s. From the late 1990s, and particularly the early 2000s, various Asian governments have been passing legislation which allows the establishment of REITs. In India, the Securities and Exchange Board of India (SEBI) notified the SEBI (Real Estate Investment Trusts) Regulations, 2014 on 26th September 2014 and laid down a framework for REITs and its registration and regulation in India. This paper is an empirical study on the basis of secondary data which examines various issues related with REITs in India besides highlighting its’ genesis and development.
1. BACKDROP

The real estate sector has been at the forefront of the Government of India’s (GoI’s) agenda on account of its potential to drive economic growth significantly. The contribution of the real estate sector to India’s gross domestic product (GDP) has been estimated at 7.3% in 2015 and expected to augment to 13% by 2028; and this sector also generate 7.6 million jobs during the same period (the second largest employer after agriculture in India). It is also expected to generate more than 17 million employment opportunities across the country by 2025. While housing contributes approximately 5%–6% of the country’s GDP, the retail, hospitality and commercial sub sectors have also grown at the same time, meeting the growing infrastructural needs. Due to rapid urbanization, positive demographics and rising income levels, the Indian real estate sector (including housing) during the period January 2000 to December 2015 has attracted FDI to the tune of US $ 20.42 billion (8.70% of the total FDI inflows). Again, total inflows by way of private equity (PE) funds in real estate sector during the year 2015 were INR 23,500 crores which is increased by 72% as compare to the previous year.

To attract more domestic and foreign investment in real estate and infrastructure sector, the Finance Bill, 2014 has introduced a new concept of “Business Trusts” and this type of entity have been given the pass through status. Business trusts are not a separate legal entity, but a combination of elements of company and trust. It runs a business enterprise, invests in sectors and assets, but trustees are the legal owners of the trust's properties and they manage these assets for the benefit of the unit holders. Such business trusts include new category of investment vehicles i.e. Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs). REITs have been successfully used as an instrument for pooling of investment in real estate sector in several countries.

In India real estate assets are kept out of the financial market since it is assumed that it is not a full- fledged investment option and as an asset class, it is significantly differing from any other assets prevailing in the capital market. It is considered as a natural hedge against inflation, having low volatility in prices and generates positive long- term return. Therefore, the common investors should be allowed with an opportunity to share in the gains of this asset class through an investment by Systematic investment plan (SIP) route.

2. OBJECTIVES AND METHODOLOGY OF THE STUDY

The present study aspires to make an overall evaluation on REITs in the context its contribution in the real estate sector of India. To be very specific, the major objectives of the study are –

(i) To highlight the problems faced by the real estate sector during post financial crisis (2008) in India.

(ii) To describes the history and development of REITs in the world as well as in India.

(iii) To discuss on various conceptual issues related with REITs.

(iv) To highlight on the operational aspects of a REIT.
(v) To identify problems and point out some measures in the context of better progress of REIT in the real estate sector of India.

Accordingly, the remainder of the paper is organised as under –

Section three highlights the problems faced by the real estate sector in India. Section four narrates down the trends of funding in real estate sector of this region. Section five discuss on the conceptual issues related with REITs. Section six and seven describes the genesis and development of REITs in the world and particularly in India respectively. Section eight narrates down the reasons for introduction of REITs in India. Section nine highlight some of the key features of SEBI rules on REIT and the last section i.e. section ten is devoted for concluding observations.

The study is basically exploratory in nature and depends exclusively on secondary data. Secondary data are collected from various reports published by ASCI, GOI, KPMG, Price Water house and other research papers on REITs.

3. PROBLEMS FACED BY THE REAL ESTATE SECTOR IN INDIA

The average growth rate of India’s economy was approximately 6.77 % during the period 2006-2015 (the World Bank). The growth has been achieved on account of increased consumption, increased investment activity as well as productivity gains. However, on account of the prevailing global economic uncertainty and macro-economic factors the Indian economy recorded a growth of 7.26 % in 2015. This presents a sharp contrast from a growth rate of approximately 10.3% achieved in 2009-10. Successive reduction in key borrowing costs, poor availability of overseas credit, sluggish industrial output and weak private-sector investment were the key reasons behind this deceleration in the growth of the Indian economy.

As the economy shows signs of decreasing GDP growth, the real estate industry faces its own share of concerns. Several real estate developers are badly suffering from high debt due to increasing construction and labour costs. An underdeveloped debt and capital market, coupled with limited options for raising fund has resulted in a significant cash blockage for developers especially those who have commercial properties in their hands ready to dispose off. This sector witnessed a sluggish demand after the Global Financial Crisis in 2008. This sector is facing the following types of problems:

- Prolonged processes for obtaining permit is one of the major difficulties faced by the sector;
- In India, policies regarding land acquisitions are different in each states; which adds misery for investment plan of the developers;
- Rates of stamp duty are also too high and again subjected to state jurisdictions;
- Overall cost of borrowing is badly affected due to depreciation of rupee against dollar which results in lower bottom lines.
- A large portion of ready commercial assets are still owned by developers who were continuously finding out avenues to offload these assets.
4. TREND IN REAL ESTATE FUNDING

The introduction of SEZ policy in April 2000 has increased the demand for commercial and office spaces. In order to foster the growth of the real estate sector and to bridge the shortage of ever increasing demand for housing and real estate business, the Government of India vide press note no. 2 of 2005, permitted FDI up to 100%, under the “automatic route” in townships, housing, built-up infrastructure and construction development projects. After foreign direct investment (FDI) was allowed in the real estate sector in 2005, there was a major change of the investment sentiment for the sector. In addition to the traditional source of funding, the policy change opened up the floodgates for funds from global Real Estate Funds, Private Equity Funds, hedge funds, and strategic investors or foreign developers. During 2000 to 2008, a number of investments by both domestic and foreign funds took place at entity and project levels. Along with this, there were successful listings of many real estate developers in India as well as in overseas market. However, the global financial crisis of 2008 resulted in a significant shift in the funding scenario within the real estate sector in India. While the availability of capital continues to be there, albeit at a reduced level, the nature and sources of capital have changed over the years. After 2008, the sector has been experiencing a substantial decline in FDI inflows due to more cautious approach from the investors in a volatile market.

Figure 1: Trend In Real estate funding

Trend in real estate funding

Pre FDI (Before 2005)
- Bank lending
- Private lending

Post FDI and before global financial meltdown (2005 to 2008)
- Offshore listing
- Initial Public Offer (IPO)
- Private Equity (PE) funds
- External Commercial Borrowings (ECB)
- Non-Banking Financial Companies (NBFCs) lending
- Bank lending
- Private lending

- Offshore listing
- Qualified Institutional Placement (QIP)
- Initial Public Offer (IPO)
- Private Equity (PE) funds
- Non-Convertible Debentures (NCDs)
- External Commercial Borrowings (ECB)
- Non-Banking Financial Companies (NBFCs) lending
- Bank lending
- Private lending
- Real Estate Investment Trusts (REITs)/ Real Estate Mutual Funds (REMFs)/ Asset Investment Fund (AIF)
During last couple of years the real estate sector is witnessing a sign of recovery with the help of some private equity firms who have shown their increasing interest to acquire commercial assets on the back of decreasing vacancies, somewhat stabilization of rentals and depreciated Indian currencies. Several new investors such as Qatar Investment Authority, Canada Pension Plan Investment Board, Abu Dhabi Investment Authority, Blackstone, Standard Chartered Bank, Proprium capital partner, Hayat Invest and Clear water Capital have committed major investment in the Indian real estate sector, especially in commercial properties. These firms have taken advantage of the liquidity crunch and have acquired assets at an attractive price.

Actually, private equity funding is peaked in 2007 with several deals at the entity level. Following the financial crisis in 2008, the availability of funding is much more at a project level than at the entity level. Within the sector, funds have been cautiously looking at residential projects due to their self-liquidating nature and also commercial leased assets that provide attractive rental yields along with capital appreciation.

Banks’ credit exposure to the real estate and housing sector declined from 10% (as a percentage of Gross Bank Credit) in FY10 to 5.8% in FY15 (Reserve Bank of India, 2015). While bank construction finance continues to be the cheapest source of funding, end-use restrictions and close monitoring of proceeds for construction has hinders the ability to utilise these funds for growth capital such as land acquisition.

With several equity investments in real estate projects going resentful, investors have shifted focus to mezzanine and structured equity instruments. With relaxed regulatory
norms governing non-convertible debentures, this has become the instrument of choice for foreign investors after 2008. The major benefits of using these instruments are the flexibility of tenure, alignment of returns to the project cash flows and the ability to get real security over assets. Reflecting this trend non-convertible debentures (NCDs) worth c. US $ 8.2 billion were issued in 2015 as compared to c. US $ 6.8 billion in (www.nseindia.com and www.bseindia.com ) In the domestic market, there has been a growing dependence on non-banking finance companies (NBFCs) for funding in the real estate sector. In particular, NBFCs have been actively looking at “last mile funding” opportunities, where projects in which substantial investments have been made are not getting completed due to lack of “last mile funding.”

During post financial crisis, divestment of non-core assets and leased assets is another very strong theme that has been visible. With several developers dealing with unmanageable debt levels, asset disposal is being taken to deleverage their balance sheets. Non-core assets (projects or land) not under development or outside the core geographical region are at the top of the sell-off list in order to reduce the debt burden on the company. Apart from real estate companies, several industrial groups have been trying to monetize the value of real estate assets (specifically leased assets) lying hidden in their balance sheets; and this action has accelerated significantly in the last couple of years. Apart from lease rental discounting facility by banks, some of the private equity funds are looking for Grade A office space assets that have been leased or near completion and hence, do not have any residual development risk.

Raising funds from the capital markets continues to remain an unviable option for the sector during both pre and post financial crisis. Nevertheless, in 2013 one of the largest real estate companies in India was able to successfully place a large US$345 million follow-on public offer (FPO) in line with Securities and Exchange Board of India (SEBI) requirements to bring the promoter holding down to 75%.

After 2009, development of portfolio of project with the help of global funds is becoming an emerging trend for funding in the real estate developer. In these type of “platform deals”, the real estate developer will be the exclusive development manager of the projects to be pursued through such equity commitments for which they will enjoy a development management fee. Several large pension funds and sovereign wealth funds have shown their positive response to the real estate sector in India through this route. GOI, on its part, is also re-evaluating policy measures for boosting the real estate sector. Recent changes to the SEZ policy, in terms of reduced area requirements, easing of external commercial borrowing (ECB) norms for affordable housing and enhancement of limits for listed NCDs for all are the glimpses of positive steps for the sector. Game changers e.g. FDI in multi brand retail, can provide the necessary support to revitalize investor interest in the sector.

In the light of the above discussion, Real Estate Investment Trusts (REITs) Regulations, 2013, should have a positive impact on the real estate industry and open another avenue for investment in the real estate sector.
5. CONCEPTUAL ISSUES ON REITS:

5.1 What is REITs?
Real Estate Investment Trusts (REITs) is a collective investment vehicle that invests in a diversified pool of professionally managed investment grade real estate. The assets are typically office, residential, retail, hospitality and industrial, logistics property or any other income-generating property. Some REITs specialise in one asset type, while others offer a mixed portfolio. But the real estate should provide investors with steady income generated from rent under lease contracts and potentially capital growth.
REIT usually offers the investors with high yields and a highly liquid method of investing in real estate. It is actually a real estate company that offers common shares to the public. Thus, a REIT stock is similar to any other stock that represents ownership in an operating business. A REIT has two unique features — its primary function is to manage income-producing properties and Generally, REITs are closed-ended or open-ended companies or trusts that hold, manage, lease, develop and/or maintain real estate for investment purposes. They tend to have a broad shareholder base and are often, but not always, traded on a public stock exchange. REITs receive special tax consideration and are characterized by low transaction costs. The US House of Representatives describes the primary motivation for introducing real estate investment trusts (REITs) as “to provide all investors with the same opportunity to invest in large-scale commercial real estate that previously was open only to large financial institutions and wealthy individuals through direct investment in such real estate”.

5.2 Common Features of REITs
REITs generally have the following characteristics
- They are corporatized vehicles that pool money from investors for investment in real estate assets.
- REITs can only be used to invest in completed properties and not under-construction (Work-in-progress) projects.
- They are listed and freely traded on stock exchanges.
- The revenue source for REITs involve regular lease rentals and asset sale proceeds.
- Usually, REITs are closed-ended funds. The UK, however, has open-ended REIT schemes.
- REITs are mandatorily required to distribute 90% of their net income to investors every year.
- Internationally, REITs are allowed to raise debt.
- REITs are required to publish the fair value of assets and net present values (NPVs) of schemes in accordance with prescribed norms and at regular intervals.
- A REIT has a “pass-through” status for tax purposes. There is a single point tax on the investor.
5.3 Types of REITs

REITs can be of various kinds, such as:

- **Equity REITs**: Equity REITs invest in and own properties. Their revenues come mainly from their properties’ rents.

- **Mortgage REITs**: Mortgage REITs engage in investment and ownership of property mortgages. These REITs extend loan for mortgages to owners of real estate, or invest in (purchase) existing mortgages or mortgage-backed securities. Their income is generated from the interest earned on mortgage loans.

- **Hybrid REITs**: Hybrid REITs comprise investment strategies of Equity REITs and Mortgage REITs by investing in both properties and mortgages.

- **Sector Specific types of REIT**: Some REITs invest specially in apartments, warehouses, and hotels. Such REITs include:
  - **Housing REITs**: Housing REITs acquire, renovate, lease and manage residential properties located in markets for generating rental income. They hold properties over the long period and generate virtually all revenue by leasing the properties. This revenue is used to pay operating costs and for distributing dividends among the shareholders. Most residential REITs are multifamily REITs, also called apartment REITs. An apartment REIT owns a portfolio of rental apartment properties, which may be large residential properties such as mid-rise and high-rise buildings, student housing, senior housing or social housing. This type of REIT can be seen in the Asian countries.
  - **Industrial REITs**: Industrial REITs acquire, own and manage industrial properties, such as warehouses, buildings, undeveloped land, business parks and high-tech space.
  - **Hotel REITs**: Hotel REITs own hotel, lodging or resort properties and could include various types of properties such as limited service, full service, resort, conference center, suite and airport properties. Hotel REITs accrue revenue from the underlying value of hotel properties it owns and from the income generated by those properties. This type of REIT can be seen in the US, Australia and UK.

5.4 REITs advantages to different stakeholders

- **To the Developers**
  - Improve liquidity of the sector
  - Capital raising opportunity for the mid-tier developers particularly for the small companies having lower or minimal credit worthiness.

- **To the Institutional Investors**
  - Provide an exit opportunity for the existing PE players, financial investors and developers.
  - Act as an alternative financing opportunity with increase depth of Indian real estate capital market.
  - Help attractive long term investors such as pension and insurance funds looking for moderate risk vs. return proposition.
To the Government
- Help to increase Government's revenue.
- REITs can ease in implementation of other key real estate policy initiative of the Government e.g. targeting 100 smart cities.

To the retail investors
- Reducing ticket size for investing in real estate sector.
- Transparent investment opportunity in real estate sector supported by experienced professionals and independent oversight.
- Easy entry and exit of the developers in real estate sector.

5.5 Structure of REITs:

Source: KPMG in India Analysis 2014

The following are the major parties involve in a REIT business
- Sponsor: The person who sets up the REIT and hold at least 25% of the units of the trust;
- Trustee: The person who holds the REIT assets in trust for the benefit of the unit holders;
REIT Manager: An Individual who is looking after identification of investment opportunity, managing the investment and controlling the day to day operation of REIT business; typically paid with management fees and part of upside (IRR).

Property Management Company: It is a facility management company for maintaining the standard and quality of assets. Generally their appointment is not mandatory as per regulation but for better management of the property they are involved into the system.

Special Purpose Vehicle (SPV): A body corporate in which REIT holds or proposes to hold controlling interest (i.e. 51%);

Principal Valuer: A person who is a registered valuer under Section 247 of the Companies Act, 2013 and assigned as such and who has been appointed by the manager to undertake valuation of real estate assets.

6. GENESIS AND DEVELOPMENT OF REITS IN THE WORLD:
REITs were emerged in the US during the mid-1960s as a means of providing small investors the opportunity to invest in commercial real estate or mortgage lending. After gaining popularity in the US market, REITs were introduced in Australia. From the late 1990s, and particularly the early 2000s, Asian governments have been passing legislation which allows the establishment of REITs, giving tax concessions which replicate the taxation treatment of REITs globally, particularly in the US and Australia. This reflects a better understanding of the benefits REITs which offer both as an investment class and in improving the built environment and promoting economic growth.

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Source: Legislative framework in place: India, China and Spain (2014)

7. GENESIS OF REIT S IN INDIA
The process of bringing the REITs structure in India began in 1996. The Security Exchange Board of India (Mutual Funds) Regulations, 1996, introduced chapter VIA, highlighting the guidelines for introduction of Real Estate Mutual Fund Schemes (REMFs). However, the mutual fund industry fails to launch REMFs due to lack of clarity, want of transparency and uncertainty prevailing in the real estate sector. Moreover, lack of
regulatory framework for the real estate sector refrained mutual fund houses from launching such funds.

In December, 1999, the Association of Mutual Funds in India (AMFI) appointed a committee headed by Mr. Deepak Satwalekar (known as the “Satwalekar Committee”), to explore the opportunities and possibilities of introducing real estate investment schemes for mutual funds in India. In its report (submitted in October, 2010) the committee recommended the introduction of Open ended mutual fund structure for Real Estate Investment. On receipt of report from the Satwalekar Committee, AMFI has established another sub-committee for further investigations and to devise a working plan for launching Real Estate Investment Schemes. The said committee submitted its report to AMFI in August 2002. The Sub-committee agreed with the suggestions of “Satwalekar Committee” and recommended the ‘Trust’ structure as appropriate for Real Estate investments; the committee also opined for a tax benefit to the stakeholders and close ended scheme instead of open ended scheme.

In order to bring the accruing benefits of REITs mechanism in Indian Economy, SEBI brought Draft Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2008, or “The Regulation” for public comments. Many suggestions were received in order to make “the Regulation” more prominent and sturdy e.g. Participation of Foreign Investments in REIT, minimisation of transaction cost, relevant amendment in the taxation area etc. However, the regulator realized that REIT guidelines may not work in Indian structure as the Indian property market lacks profundity and liquidity. Hence the SEBI vide Notification dated April 16, 2008 amended SEBI (Mutual Funds) Regulations, 1996 so as to permit mutual funds to launch REMFs. However, the initiative of the regulator to introduce the scheme could not be put on the reality as it failed to find any takers of the scheme. Some of the issues involves in establishment of the REMFs are as follows:

- The aftermath of Global Recession play a crucial role in liquidity issues;
- A sound market for mortgage backed securities is lacking in India;
- Implication of stamp duty, which varies from state to state in this continent;
- No clear cut guidelines for the valuation of the assets;
- There were also some issues related with the acquiring real estate properties on long term leases.

In the process of bringing the REITs regime in India, the market regulator SEBI, for the third time on October 10, 2013 tabled the draft consultation paper on Real Estate Investment Trust (REIT) Regulations, or “the Draft Regulation”. On 26th September, 2014, after getting positive feedback from all the stakeholders, SEBI notified the Real Estate Investment Trusts Regulations, 2014 and laid down a framework for its successful functioning. As per these regulations, REITs has to be registered as Trusts under the Indian Trusts Act, 1882. Further, the taxation structure of REITs was incorporated in the Income Tax Act, 1961 ("ITA") by the Finance Act 2014.
8. WHY REITS IN INDIA?

The liberal economic policies, aimed at improving private participation, adopted by the Government of India has helped in capitalising the strong fundamentals of the Indian economy which includes young population, rising urbanisation and a growing purchasing capacity of the middle class population. Globally, REITs have successfully demonstrated the ability to attract and effectively manage investments in the real estate sector. Besides other advantages, REITs also fetch increased transparency in the sector by adopting better corporate governance, disclosure and financial transparency practices. The demographic dynamics in India are shifting very fast, leading to an ever growing demand for quality real estate that continues to be higher than supply. REITs can help in bringing the essential investments for meeting this growing demand.

Following are some of the significant factors that bring out the need for introducing REITs in India:

(i) Rising demand due to changing demographics and growing urbanization:
According to UN estimates, India has the highest rate of shift in urban population among the BRIC nations. An estimated 843 million people will live in Indian cities by the year 2050, which is about the same as the combined population of the US, Brazil, Russia, Japan and Germany. Again, more than 300 million persons are expected to be included to India’s working age population by the year 2050. This will propel the growing urbanization and push the need for providing housing or accommodation facilities for this section, including the increasing number of women in the work force.

(ii) Investment gap: After the financial crisis in 2008, the capital intensive real estate sector faces a stern constraint in terms of adequate and structured financing options. According to EY estimates (2015) the investments required in the Indian real estate market by the year 2015 is approximately US $ 42 billion (excluding EWS housing) and approximately US $ 257 billion (including EWS housing). Residential real estate alone will require an investment of US $ 29 billion. The Indian economy is prepared to experiment with advanced funding options such as REITs and provide industry players with a globally competitive edge.

(iii) REITs bring transparency: REITs can help improve the much-needed transparency levels in the Indian real estate sphere in the following ways:

a) Availability of real estate financing from more structured, institutional sources helps in reducing the over dependence on a particular means of financing and therefore improve transparency. In this context, REIT’s will help in streamlining the real estate sector by developing a transparent mechanism for raising finance in the real estate market.

b) REITs are registered with the concerned regulatory body of the country, for instance the Securities and Exchange Commission in the case of the US. Therefore, they are always subject to stringent regulation and monitoring by the regulator.
c) REITs are required to comply with corporate governance, information disclosure and financial reporting standards laid down by the Regulator. Therefore, there is a regular information exchange and accessibility of information by the public domain.

d) REITs bring more professionalism. There is a definite emphasis on issues such as reducing risks attached to title in property and minimizing transaction costs.

(iv) Improvement in debt-equity balance: Being a pure equity capital, the introduction of REITs will definitely assist in improving the debt-equity balance in the real estate market through provision of equity financing; thereby assisting in the growth of a more steady and mature real estate market.

(v) Vehicle for addressing non-performing assets (NPAs): Specifically in the context of the Indian real estate market, the introduction of the REITs can be used as a capable investment vehicle to wipe out NPAs i.e. sick or defunct companies holding large values of real estate mostly in the form of land. Disposal of such NPAs (i.e. companies) to REIT’s will have a two-fold effect — realization of actual value for the real estate and relieve in liquidating the sick company after removal of the high value of real estate from its books. This will help the financial institutions in regaining their strong profitability positions, which is currently being damaged through large NPAs being booked by them.

(vi) Opportunity for common investors to share in the gains of this asset class: REITs provide a more liquid module to the current range of property investment vehicle and improve investor’s investment profile through diversification of investment base and improving stability of income sources. REITs usually offer a good hedge against the rentals i.e. the underlying income and adjust themselves in line with the cost of living. In REITs, usually more than 90 % of the profits are distributed to investors as dividends. In India, the returns from this source are not only expected to be high due to an increase in demand, the REITs also provide protection against inflation. In its recent consultative paper on Draft REITs Regulations, 2013 SEBI has recognized the need for REITs as an investment vehicle to meet the investment demands for the real estate sector. SEBI observed that — “By the very nature of REIT, it is beneficial to both the investors and the industry in different ways. On one hand, REITs provide the investors with an investment avenue, which is comparatively less risky than investing in under construction properties and also provides regular income. On the other hand, REITs provide the sponsor (usually a developer or a private equity fund) avenues of exit thus providing an opportunity of liquidity and enable them to invest in other projects.”

9. SEBI RULES FOR REITS

Recently, SEBI has approved basic rules for REITs called SEBI (Real Estate Investment Trusts) Regulations, 2014. These rules, in brief, are:
Dr. Manas Chakrabarti :: Real Estate Investment Trusts (REITS)--
A New Concept Of Real Estate Funding In India

(i) REITs shall be set up as a trust and registered with SEBI with the parties such as Trustee, Sponsor(s) and Manager.

(ii) The trustee of a REIT shall be a SEBI registered debenture trustee who should not be an associate of the Sponsor/Manager.

(iii) REIT shall invest in commercial real estate assets, either directly or through SPVs. In such SPVs, the REIT shall hold or proposes to hold controlling interest and not less than 50 % of the equity share capital or interest. Further, such SPVs shall hold a minimum of 80 % of its assets directly in properties and shall not invest in other SPVs.

(iv) Once registered, the REIT can raise funds through an initial offer. Subsequent arranging of funds may be made through follow-on offer, rights issue, qualified institutional placement, etc. The minimum subscription size for units of REIT shall be INR 2 lakhs. The units offered to the public in initial offer should be minimum 25 % of the number of units in the REIT on post-issue basis.

(v) Units of REITs should be listed on a recognised stock exchange and a continuous disclosure in terms of the listing agreement is required. Trading lot for such units shall be INR 1 lakh.

(vi) Value of the assets owned or proposed to be owned by REIT should be a minimum of INR 500 crore to qualify for an IPO and minimum issue size for initial offer shall be INR 250 crore.

(vii) The role of the trustee is to watch the activity of the REIT and the manager assumes operational responsibilities relating to the REIT. Responsibilities of the parties involved are given in the Regulations.

(viii) An REIT may have multiple sponsors, not more than three, subject to each holding at least 5 % of the units of the REIT. Such sponsors shall collectively hold not less than 25 % of the units of the REIT for a period of minimum three years from the date of listing. After three years, the sponsors, collectively, shall hold at least 15 % of the units of REIT for the rest of life of REIT.

(ix) 80 % of the value of the REIT assets should be consist of ‘completed and revenue generating properties’ and a maximum of 20 % of the value of REIT assets may be invested in the followings:

- developmental properties;
- mortgage backed securities;
- listed or unlisted debt of companies or body corporate in real estate sector;
- equity shares of companies listed on a recognised stock exchange in India who’s’ 75 % of operating income consist of revenue from real estate activity;
- Government securities, money market instruments or cash equivalents. However, investments in developmental properties shall be limited to 10 % of the value of the REIT assets.

(x) An REIT shall invest in at least two projects with a maximum allotment of 60 % of value of assets in one project.
(xi) REIT shall allocate a minimum of 90% of the net distributable cash flows on a half yearly basis to its investors, subject to the applicable laws.

(xii) REIT, through a valuer, shall undertake full valuation on a yearly basis and updation of the same on a half yearly basis; it should declare NAV within 15 days from the date of such valuation or updation.

(xiii) The borrowings and deferred payments of the REIT shall not exceed 49% of the value of the REIT assets at a consolidated level. In case such borrowings or deferred payments exceed 25% of the value of the REIT assets, approval from unit holders and also a credit rating is required.

(xiv) Detailed provisions for related party transactions, valuation of assets, disclosure requirements, rights of unit holders, etc. are provided in the Regulations. However, for any issue demanding unit holders’ approval, voting by a person who is a related party in such transaction as well as its associates shall not be considered.

10. Conclusion

Urbanisation is a trend which probably cannot be reversed or avoided in India. Having realised the potential and need for an adequate urban development strategy, the GOI has taken significant steps by allocating significant amount of funds towards urban infrastructure. As a growth carrier, it is essential to develop the real estate sector to support the growth of over 300 other sectors and employment. However, the key challenge is the lack of technology and funding, where a massive gap exists. Realising the challenges at hand, several key reforms have been introduced recently and many more are lined up to improve global inflow of funds and promote growth of the sector. Launch of REITs in current times is expected to be a major relief for developers and can be an important reform in the real estate sector. REITs could be a game changer for commercial real estate sector in India, which is beginning to see a renewed interest from global investors. However there are some taxation and regulatory aspects with respect to pricing and asset quality, which needs detailed planning on behalf of GOI.

11. References


[12] www.sebi.org.in