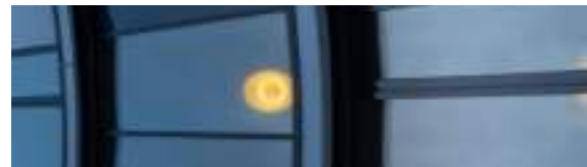




# Taxation of REIT / InvIT

[CA] Gautam Mehra  
June 2021



# Agenda

- 1 The What...
- 2 The Why...
- 3 The How...
- 4 Case study



# 1

## The What...?

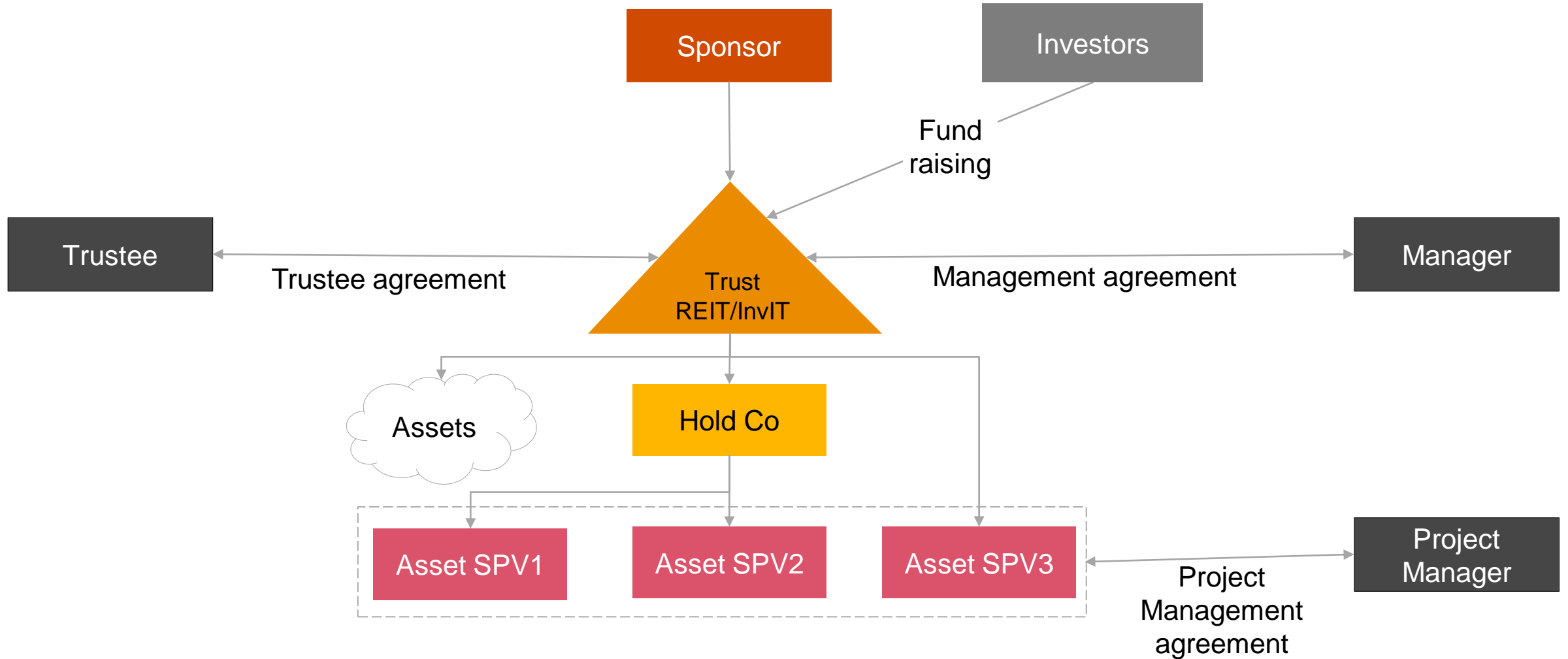
- *In Simple Terms*
- *Typical Structure*
- *The India Journey*
- *SEBI Regulations*

# In Simple Terms

***A regulated collective investment vehicle, listed or unlisted, which pools money with the purpose of investing it primarily in developed and predefined real estate/ infrastructure assets, and which is required by law to periodically distribute the income to investors***

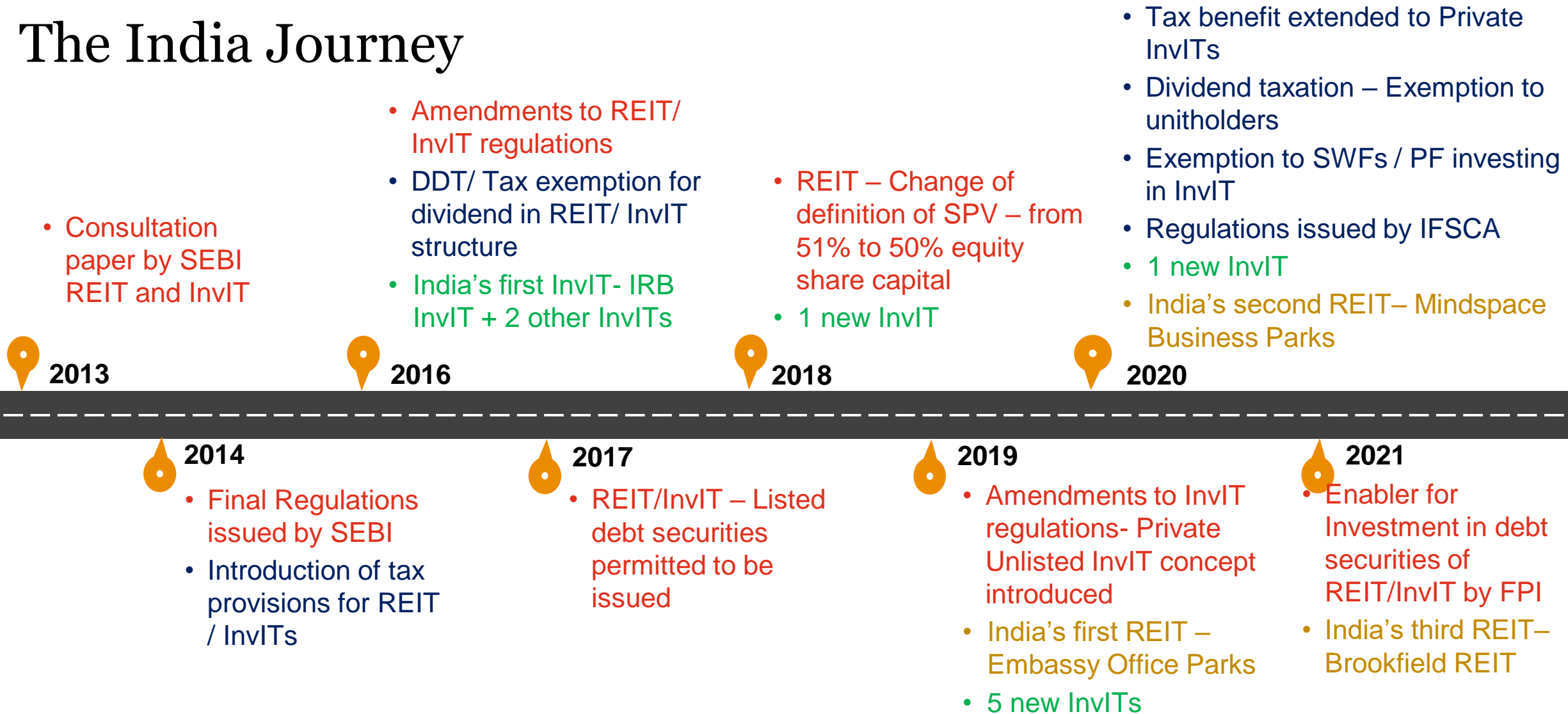


# Typical Structure



*Note: In case of InvIT - SPV to enter into a separate O&M contract with a Project Manager*

# The India Journey



Market capitalisation of listed REITs is *INR 49,256 crores*, listed InvITs is *INR 22,471 crores*

# SEBI Regulations : Permitted Investments

## Real Estate

Land, building, warehouses, sheds, garages etc. whether leasehold or freehold, excluding mortgage

Assets falling under infrastructure are excluded except for:

- Hotels, hospitals, convention centers, forming part of real estate projects
- Common infrastructure for composite real estate projects, industrial parks and SEZs

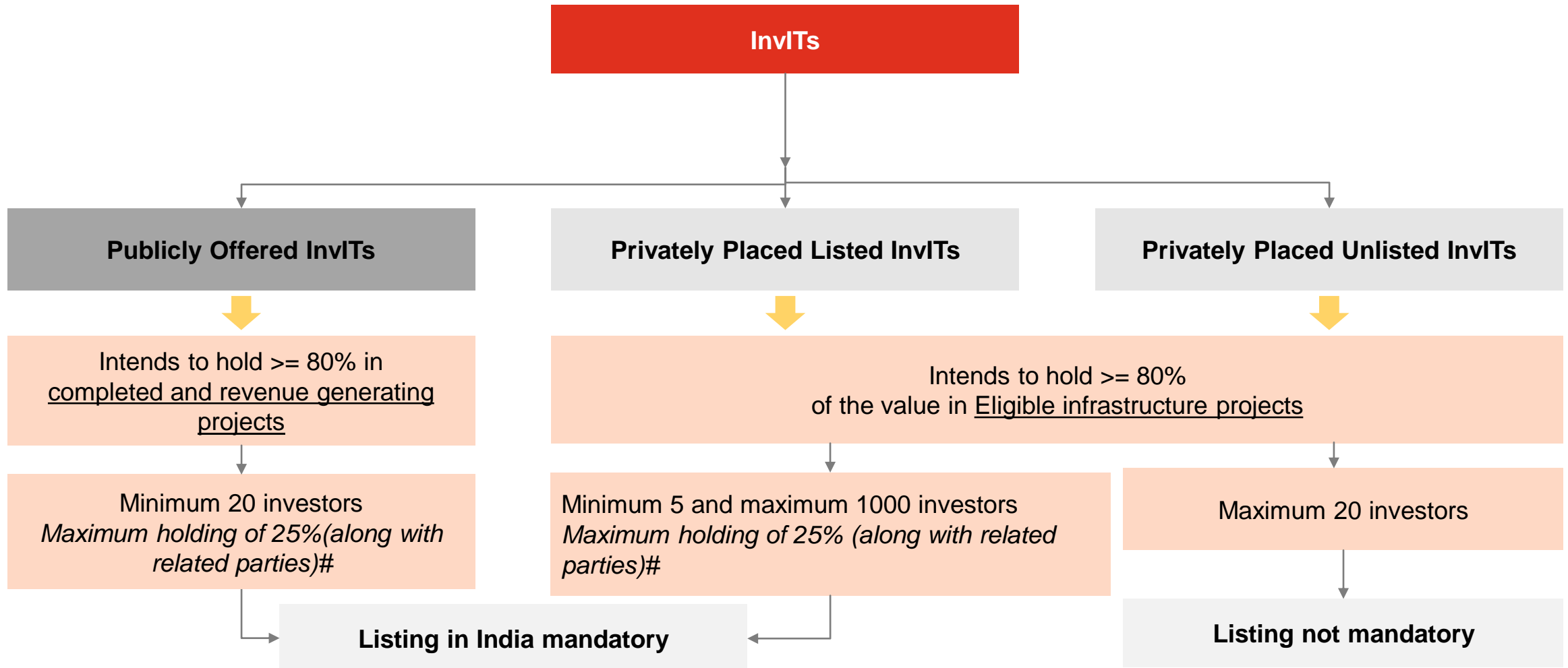
As least 80% investments in completed assets and at least 51% revenue from rentals

## 'Eligible' Infrastructure

Sub-sectors defined in Ministry of Finance notification (dated 7 October 2013/24 August 2020):

- **Transport and Logistics** – roads, bridges, ports, airports, inland waterways, railways, logistics infra etc.
- **Energy** – electricity generation/ transmission/ distribution, gas and oil storage facility
- **Water and sanitation** – solid waste management, water treatment plants, irrigation etc.
- **Communication** – Telecommunication fixed network, towers and services
- **Social and commercial infra** – affordable housing, affordable rental complexes, education institutions, sports infrastructure, hospitals, hotels, storage for horticulture / agriculture produce etc.
- **Eligibility** as per SEBI Regulations – PPP/Non-PPP

# SEBI Regulations: Types of InvITs



*#Except with approval of more than 75% of the unitholders (in value), excluding the value of units held by parties related to the transaction)*



# SEBI Regulations : Public Issue and other points

Fund Raising method	Publicly offered InvITs	Privately placed InvITs	Privately placed InvITs (Unlisted)	REITs
Asset size	INR 500 crores			
Minimum subscription	INR 1 lakh; 90% of the overall issue size	INR 1 crore; (INR 25 crore if $\geq 80\%$ InvIT assets in completed/revenue generating assets)	INR 1 crore	INR 50,000, 100 units 200 unrelated unitholders
Minimum public float	<b>Post issue capital - at offer price to be held by public:</b> 1. < INR 1600 crore: Higher of 25% or INR 250 crore 2. > INR 1600 < INR 4000 crore: INR 400 crore; 3. $\geq$ INR 4000 crore : Min 10%: 4. Public float to be increased to 25% within 3 years		Not Applicable	25% Minimum public float [10% permitted for 3 years where post issue capital is $\geq$ INR 4,000 crores]
Distributions	Once every 6 months - Min 90% of net distributable cash flows			
Leverage	Not to exceed 70% of assets		No restriction	Not to exceed 49% of assets
% Holding in Holdco/SPV	$\geq 51\%$			$\geq 50\%$

# SEBI Regulations: Sponsor, Trustee and Manager

Sponsor	Manager	Trustee
<ul style="list-style-type: none"> <li>• Net worth : Collectively <math>\geq</math> 100 cr and Standalone <math>\geq</math> 20 crs</li> <li>• Minimum 5 years experience in development of real estate or fund management/ 2 completed projects</li> <li>• Sponsor holding:               <ul style="list-style-type: none"> <li>- Lock-in – REITs: Collectively hold at least 25% for at least 3 years post listing. Unit holding exceeding 25% to be held for at least 1 year post listing</li> <li>- Post 3 Years, Sponsors to hold not less than 5% individually</li> <li>- Lock-in – InvITs: Collectively hold at least 15% for at least 3 years post listing. Unit holding exceeding 15% to be held for at least 1 year post listing</li> </ul> </li> </ul>	<ul style="list-style-type: none"> <li>• Company/ LLP or any body corporate - Manages assets/ investments of REIT</li> <li>• Net worth <math>\geq</math> INR 10 crs</li> <li>• Manager or its associate has minimum 5 years experience in fund management/ advisory services/ development in the sector (or combined experience of 30 years for InvITs)</li> <li>• Key personnel to also meet qualification criteria of 5 years experience in the sector</li> <li>• The investment manager has at least half of its directors / governing board as independent and not directors/members of an investment manager of another InvIT</li> </ul>	<ul style="list-style-type: none"> <li>• Should be registered with SEBI and should not be an associate of the sponsor(s) or manager</li> <li>• Execute investment management agreement with Manager</li> <li>• Oversees activities of Manager, protect interest of unit holders and ensure compliance with the Regulations</li> <li>• Inform SEBI on failure on manager to discharge its functions</li> </ul>

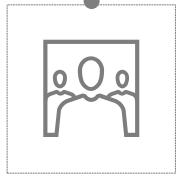
**Sponsor, Trustee and Manager to be separate entities; Valuer also to be mentioned in Offer Document**

# 2

## The Why...

- *Key Advantages*
- *International REIT Market*
- *Indian REITs Market*

# Why?...



## Nation/ Society

- Capital raise, and from a different investor class
- Mark of maturity of financial markets
- Regulation and governance
- Debt to equity



## Sponsors

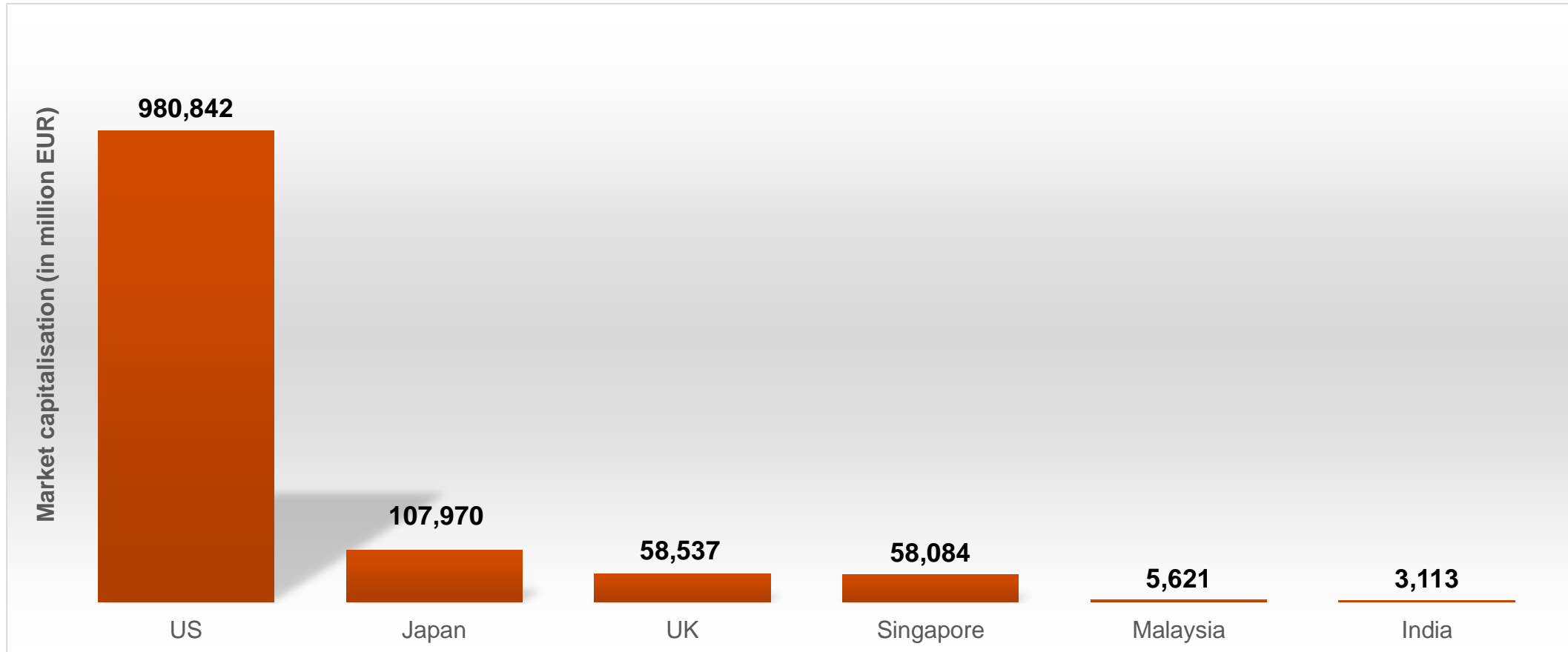
- Redeploy capital, refinance
- Unlock value – asset heavy
- Control vs liquidity
- Alternate funding source
- Future acquisitions through swap of units



## Investors

- Stable cash flow with limited risk
- Investment by retail investors
- Liquidity
- Diversification with new asset class

# Market capitalisation of REITs



Source: Global REIT survey 2020 by EPRA

# Listed India REITs performance

	<i>INR in crores</i>		
	Embassy	Mindspace	Brookfield
<b>Issue size</b>			
Primary	4750.00	1000.00	3800.00
Secondary	0.00	3500.00	600.00
Total	4750.00	4500.00	4400.00
<b>Yields</b>			
Dividends (A)	320.39	515.33	No distribution
Interest (B)	1,639.86	53.37	No distribution
Debt Amortisation (C)	2,387.74	-	No distribution
Cash yield (D=A+B+C)	4,347.99	568.70	
No. of units (in crores) (E)	94.79	59.30	
Yield per unit (F=D/E)	45.87	9.59	
Price on listing (per unit) (G)	300.00	275.00	
Yield % (F/G)	15.29%	3.49%	

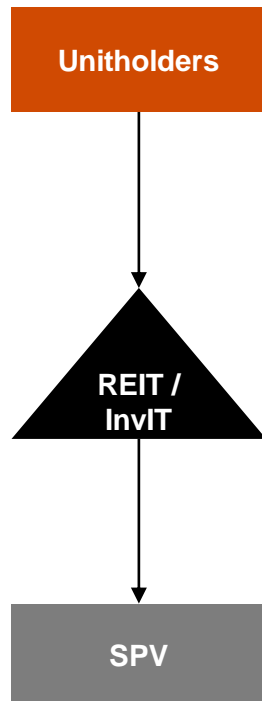
Source: <https://www.embassyofficeparks.com/investors/distribution-history/> and <https://www.mindspacereit.com/investor-relations/distribution#ir>

# 3

## The How...

- *Key direct tax implications*
- *Amendments and recommendations*

# Tax on a slide



Level	Capital Gains	Dividend		Interest	Rent (only for REITs)
		SPV under Old Regime	SPV under New Regime		
<b>Unitholders</b>	<ul style="list-style-type: none"> <li>Swap of units at time of set up</li> <li>Sale of units</li> </ul>	<ul style="list-style-type: none"> <li>Dividend distributed by REIT / InvIT to Resident/ Non-resident shareholders</li> </ul>		<ul style="list-style-type: none"> <li>Interest distributed by REIT to Resident/ Non-resident shareholders</li> </ul>	<ul style="list-style-type: none"> <li>Rent distributed by REIT/ InvIT to Resident / Non-resident shareholders</li> </ul>
<b>REIT / InvIT</b>	<ul style="list-style-type: none"> <li>Sale of shares of SPV</li> <li>Sale of property held directly</li> </ul>	<ul style="list-style-type: none"> <li>Dividend received from SPV</li> <li>Dividend distributed to Unitholders</li> </ul>		<ul style="list-style-type: none"> <li>Interest received from SPV</li> <li>Interest distributed to Unitholders</li> </ul>	<ul style="list-style-type: none"> <li>Rent received from Assets</li> <li>Rent distributed to unitholders</li> </ul>
<b>Asset SPV</b>		<ul style="list-style-type: none"> <li>Dividend distributed to REIT / InvIT</li> </ul>		<ul style="list-style-type: none"> <li>Interest paid to REIT / InvIT</li> </ul>	

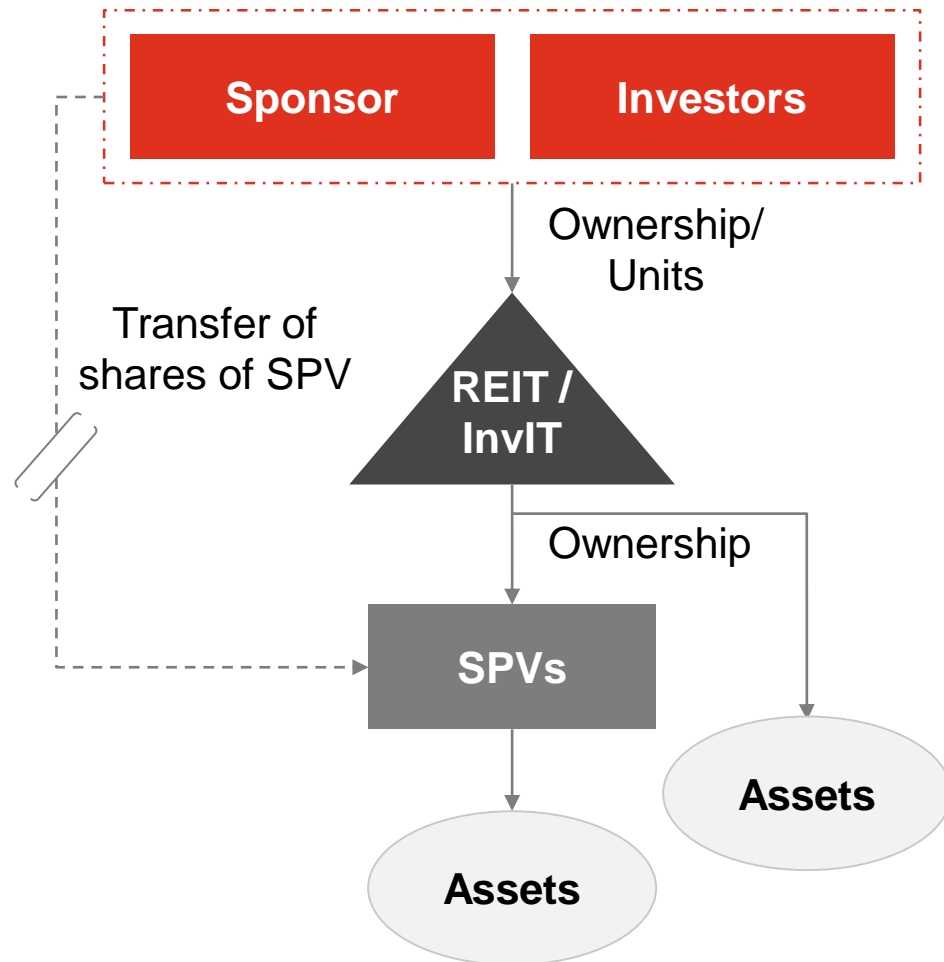
*SPV, Manager and PMC tax considerations excluded*



# Index of Sections

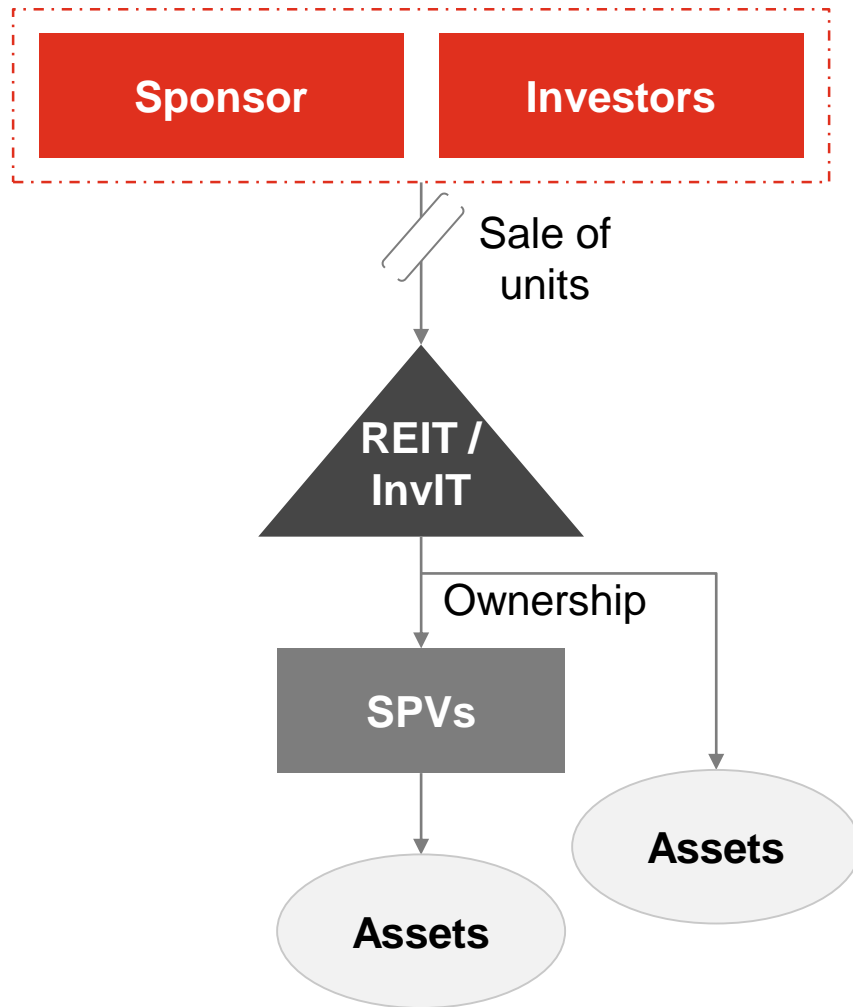
Section	Description	Legislative history
2(13A)	Definition of Business Trust	2014, 2015, 2021 (listed)
2(42A)(hc)	Period of holding of Units of a Business Trust in case of swap [r.w.47(xvii)]	2014
10(23FC)	Exemption to a Business Trust, of interest and dividend income from an “SPV”	2015, 2017, 2021
10(23FCA)	Exemption to a REIT, of rental income from directly owned RE assets	2016
10(23FD)	Exemption of income distributed to Unitholders, other than income exempt for a Business Trust, and exemption of dividends distributed by an SPV not covered by 115BAA	2015, 2016, 2017, 2021
10(23FE)	Exemption on investment in Infra Business Trust to ADIA, SWF and Pension Fund	2020, 2021
47(xvii)	Swap of shares in SPV to a Business Trust is not a transfer	2015
49(2AC)	Cost of acquisition of units received on swap [r.w.47(xvii)]	2015
115JB(2)(k)	No MAT on book profit arising on swap of shares for units of Business Trust	2016
115UA	Special provisions relating to Business Trust [Pass through], MMR s.t. 111A/112	2015, 2016, 2021
139(4E)	Requirement to file income-tax return	2015
194	SPV not required to deduct tax on Dividend distributed to Business Trust	2020
194A(3)(xi)	SPV not required to deduct tax on interest paid to Business Trust	2014
194-I	No TDS on rent paid to REIT	2015
194LBA	TDS provisions on distributions by Business Trust to Unitholder	2014, 2015, 2016, 2020
194LC	TDS on interest paid by Business Trust to a non-resident	2014
Rule 12CA	Statements in Form 64A and Form 64B	2015

# Swap of shares for units



- ❑ No capital gains tax on swap of shares of SPV for units
  - Exemption not available in case of other instruments (eg. Debt instruments)
- ❑ No MAT (in case of corporate sponsor) on swap of shares of SPV for units
- ❑ Cost of acquisition of above units = Cost of shares in SPV transferred
- ❑ Period of holding of shares to be included for determining period of holding of units, for future sale
- ❑ No exemption from capital gains tax on sale of assets to REIT / InvIT
- ❑ Lapse of losses (under section 79) on swap

# Sale of units



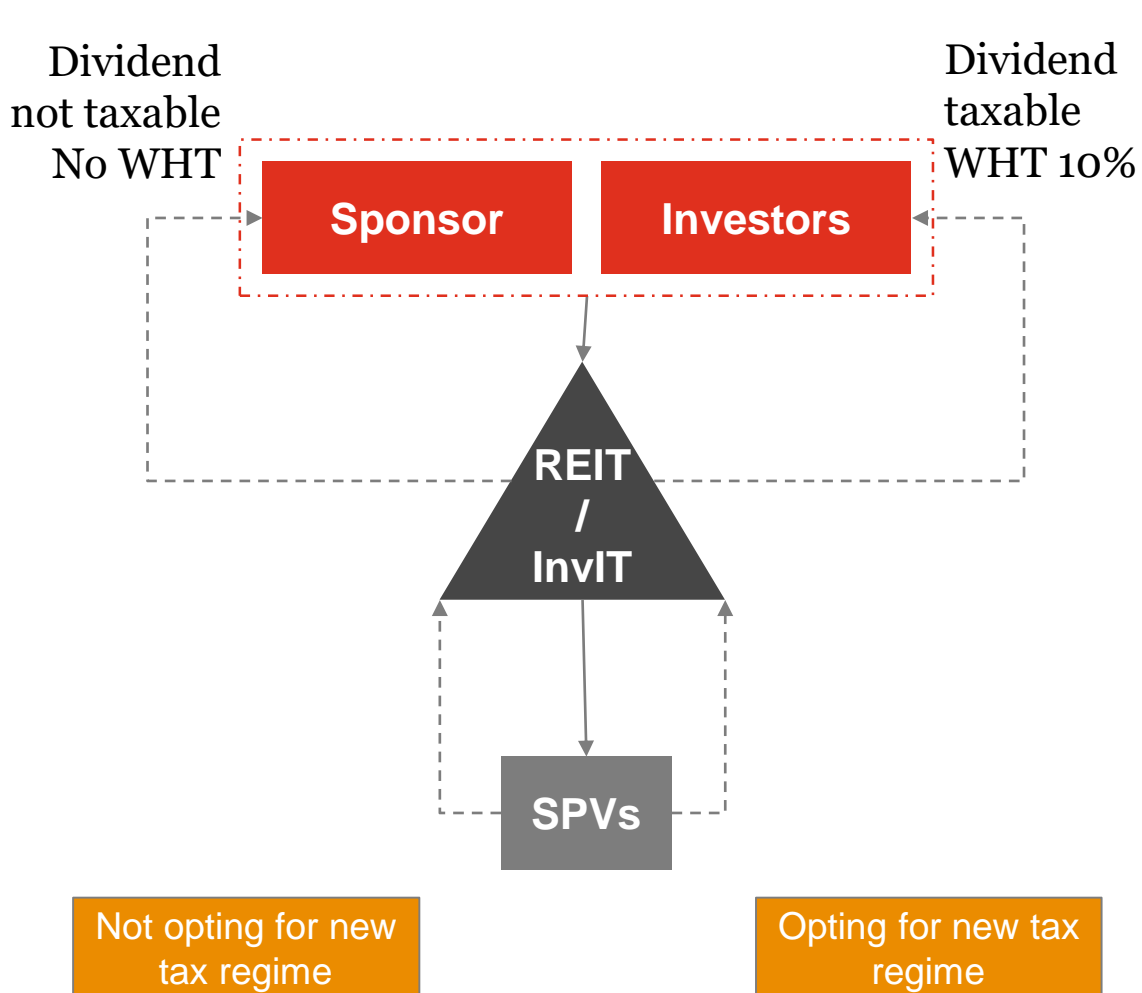
- LTCG (period of holding > 36 months)  
 STCG (period of holding ≤ 36 months)

	Listed units		Unlisted units*	
	Resident	Non-resident	Resident	Non-resident
<b>LTCG</b>	10%++	10%++	20%++	10%++
<b>STCG</b>	15%++	15%++	30%++	40%++

- For non-resident unit holders, subject to any beneficial rates applicable under respective tax treaties
- MAT applicable on sale of units by resident companies not opting for the new tax regime

\* Only in case of InvIT

# Dividend Distributions



- Dividend exempt, if received from SPV under old tax regime, else taxable
  - Residents – Applicable rates
  - Non-residents – 20%++

---

- No TDS if dividend received from SPV under old tax regime
- Else, TDS on distribution
  - Residents – 10%
  - Non-residents – 10%++

---

- Dividend - Exempt

---

- TDS – Nil

# Dividend Distributions

## Key assumptions:

- 1) Investment Amount = INR 1,000
- 2) Profit before interest and tax at SPV = INR 100

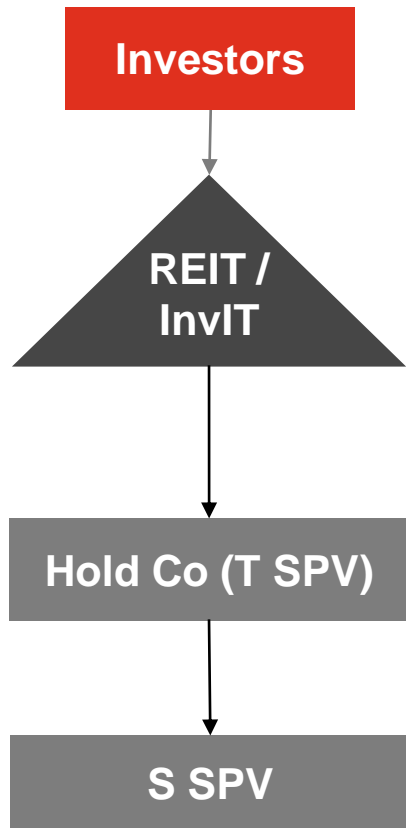
		RESIDENT	NON-RESIDENT	RESIDENT	NON-RESIDENT
		Old tax regime		New tax regime	
<b>SPV level</b>	PBT	100.00	100.00	100.00	100.00
	Tax	34.94	34.94	25.17	25.17
	Distributed	65.06	65.06	74.83	74.83
	TDS	Nil	Nil	Nil	Nil
<b>REIT level</b>	Dividend	65.06	65.06	74.83	74.83
	TDS	Nil	Nil	7.48	8.17
<b>Investor level</b>	Income	65.06	65.06	74.83	74.83
	Tax	Nil	Nil	26.15	16.34
	Net	65.06	65.06	48.68	58.49
<b>Total</b>	Tax	34.94	34.94	51.32	41.51

# Definition of ‘special purpose vehicle’

*“...an Indian company in which the business trust holds controlling interest and any specific percentage of shareholding or interest, as may be required by the regulations under which such trust is granted registration”*



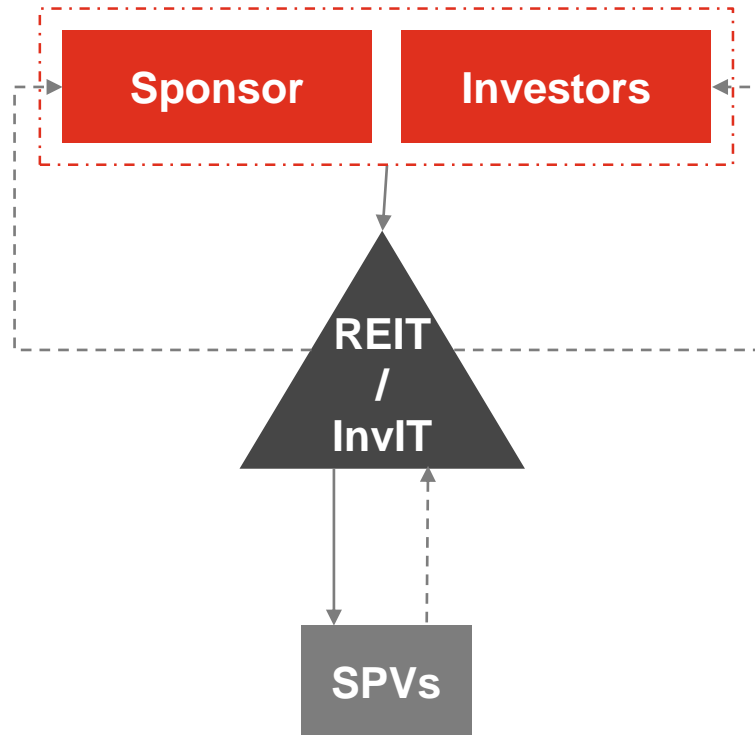
# Dividend Distributions : Multilayer structure



Parties	Scenario A	Scenario B	Scenario C	Scenario D
<b>Tax Regime</b>	S SPV – New Tax Hold Co – New Tax	S SPV – Old Tax Hold Co – New Tax	S SPV – New Tax Hold Co – Old Tax	S SPV – Old Tax Hold Co – Old Tax
<b>Investor</b>	Taxable at applicable rates	Taxable / Exempt?	Taxable / Exempt?	Exempt
<b>REIT / InvIT</b>	WHT: 10%	WHT: 10%	No WHT	No WHT
<b>Hold Co</b>	<ul style="list-style-type: none"> <li>• Tax: 22%++ (Subject to section 80M)</li> <li>• No MAT</li> <li>• No WHT</li> </ul>		<ul style="list-style-type: none"> <li>• Tax: 25% / 30% ++ (Subject to section 80M)</li> <li>• MAT</li> <li>• No WHT</li> </ul>	
<b>SPV</b>	<ul style="list-style-type: none"> <li>• Tax: 22%++</li> <li>• No MAT</li> <li>• WHT: 10%</li> </ul>	<ul style="list-style-type: none"> <li>• Tax: 25% / 30% ++</li> <li>• MAT</li> <li>• WHT: 10%</li> </ul>	<ul style="list-style-type: none"> <li>• Tax: 22%++</li> <li>• No MAT</li> <li>• WHT: 10%</li> </ul>	<ul style="list-style-type: none"> <li>• Tax: 25% / 30% ++</li> <li>• MAT</li> <li>• WHT: 10%</li> </ul>

*“...an Indian company in which the business trust holds controlling interest and any specific percentage of shareholding or interest, as may be required by the regulations under which such trust is granted registration”*

# Interest Distributions



- Interest Taxable
  - Residents – Applicable rates
  - Non- Residents – 5%++

- 
- TDS on interest payments
    - Residents – 10%
    - Non-Residents – 5%++

- 
- Interest income - Exempt

- 
- TDS – Nil (other than interest on securities)

Section 94B– not applicable on interest paid to REIT/  
InvIT – “...debt issued by a non-resident”



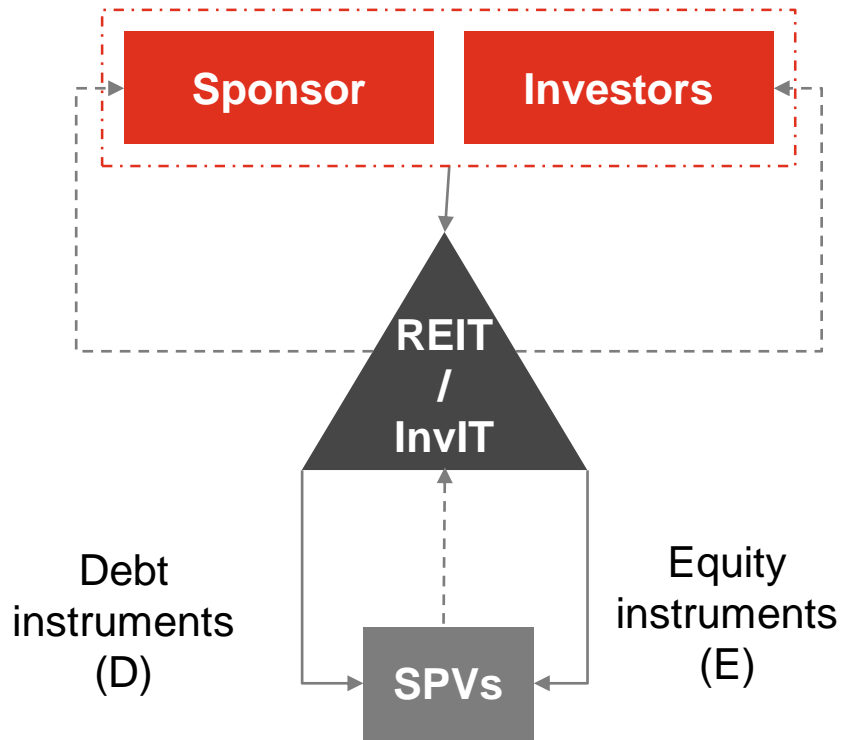
# Interest Distributions

## Key assumptions:

- 1) Investment Amount = INR 500  
(50% of INR 1,000)
- 2) Profit before interest and tax at  
SPV = INR 100
- 3) Interest rate = 10%

		Resident	Non-resident
<b>SPV level</b>	PBIT	100.00	100.00
	Interest	50.00	50.00
	PBT	50.00	50.00
	Tax	17.47	17.47
	Distributed	32.53	32.53
	TDS	Nil	Nil
<b>REIT level</b>	Interest	50.00	50.00
	TDS	5.00	2.73
<b>Investor level</b>	Income	50.00	50.00
	Tax	17.47	2.73
	Net	32.53	47.27
<b>Total</b>	Tax	17.47	2.73

# Debt: Equity ratio



$$\text{Debt / Equity Ratio} = \frac{D}{D+E}$$

Investor	Case 1	Case 2	Case 3	Case 4
<b>Equity</b>	100	75	50	25
<b>Debt</b>	0	25	50	75
<b>D/E</b>	0:1	1:3	1:1	3:1

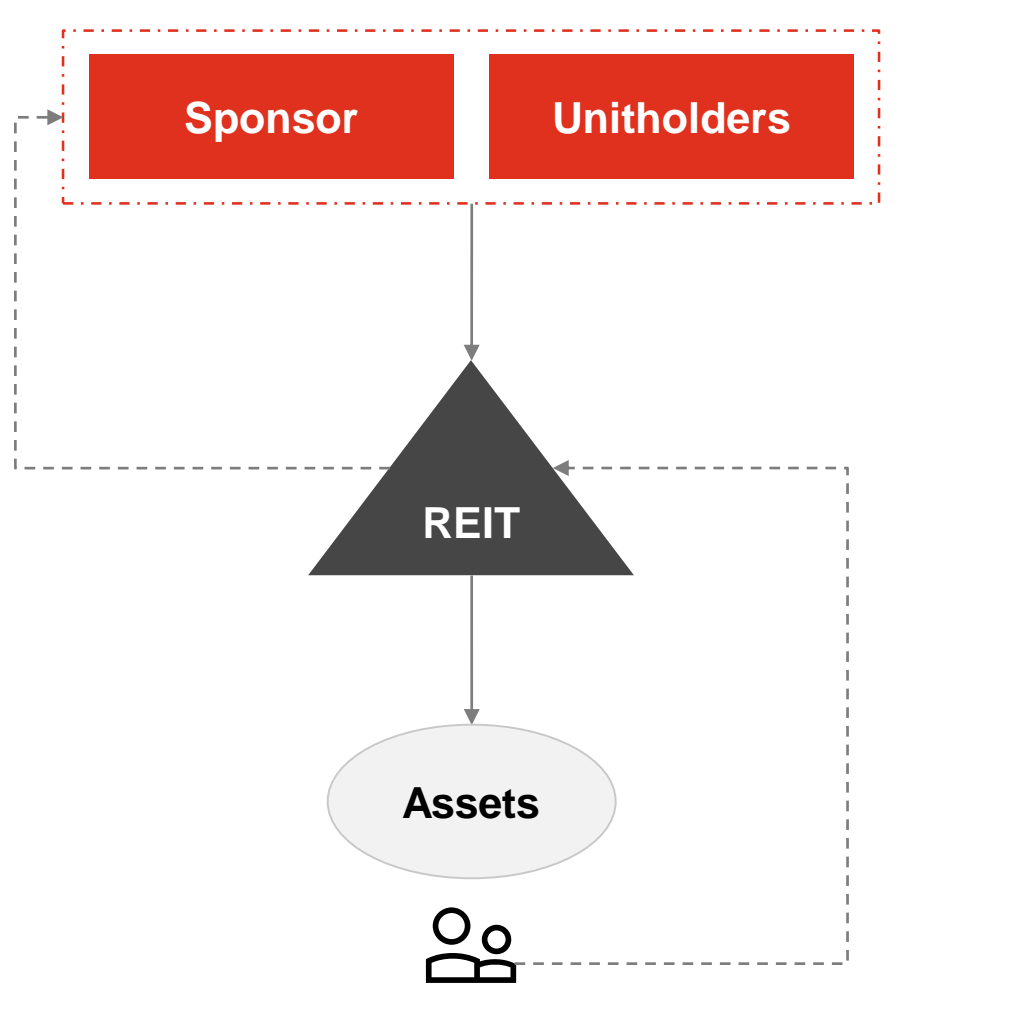
# Effective tax rates

Investor	Tax regime opted by the SPV	Case 1 0:1	Case 2 1:3	Case 3 1:1	Case 4 3:1
<b>Domestic</b>	Old Tax Regime	34.94%	34.94%	34.94%	34.94%
	New Tax Regime	51.32%	47.22%	43.13%	39.04%
<b>Foreign</b>	Old Tax Regime	34.94%	27.57%	20.20%	12.83%
	New Tax Regime	41.51%	32.50%	23.49%	14.47%

## Key assumptions:

- 1) Investment Amount = INR 1,000
- 2) Cap rate and interest rate = 10%

# Rental Distributions



- Rental Income Taxable:
  - Resident – Applicable rates
  - Non-resident – Applicable rates (subject to any beneficial rates applicable under any tax treaties )

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- TDS on payment to unitholders by REIT
  - Resident – 10%
  - Non-Resident – rates in force

---

- Rental Income exempt for REIT

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- TDS – Nil

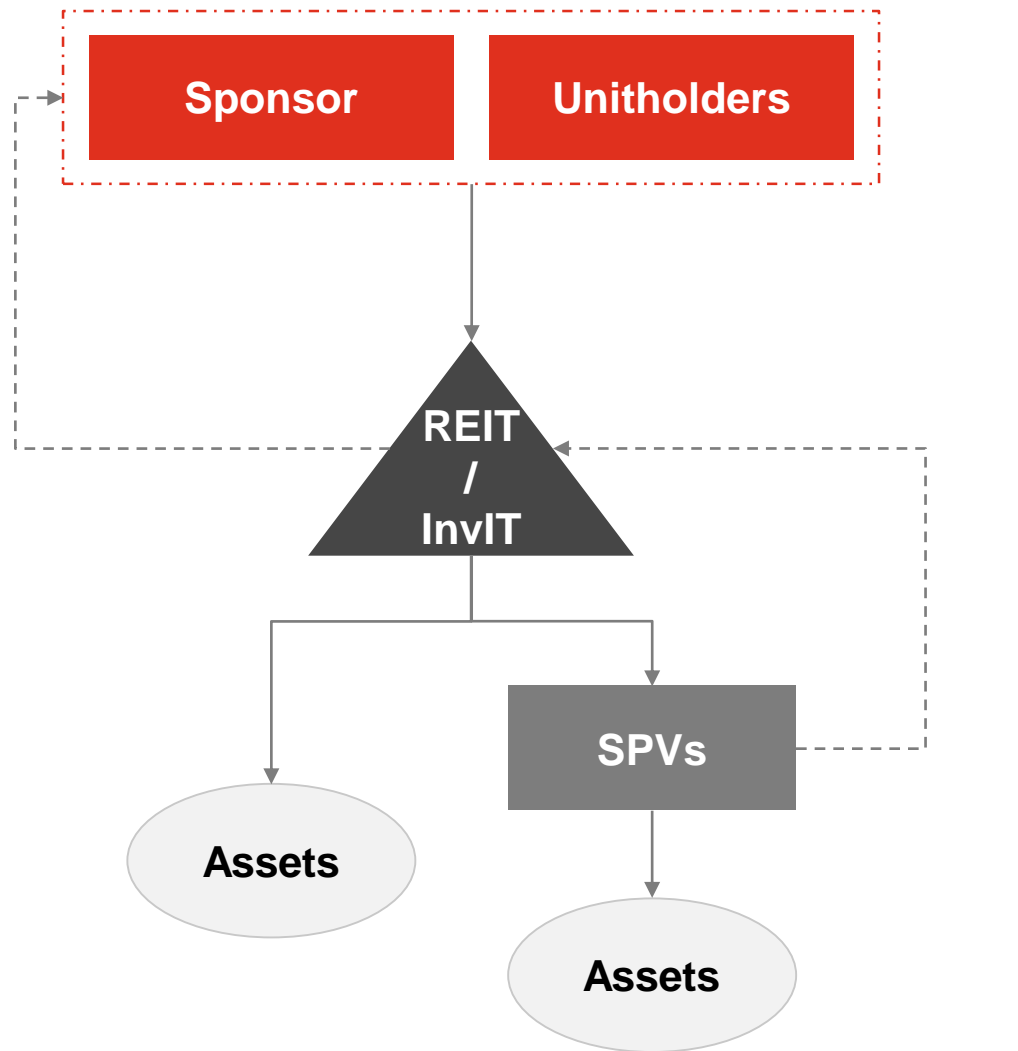
# Rent distributions

Key assumptions:

1) Rental income = INR 1,00

		RESIDENT	NON-RESIDENT
<b>REIT level</b>	Rent	100.00	100.00
	Tax	Nil	Nil
	TDS	10.00	43.68
<b>Investor level</b>	Income	100.00	100.00
	Tax	34.94	43.68
	Net	65.06	56.32
<b>Total</b>	Tax	34.94	43.68

# Gains and other income



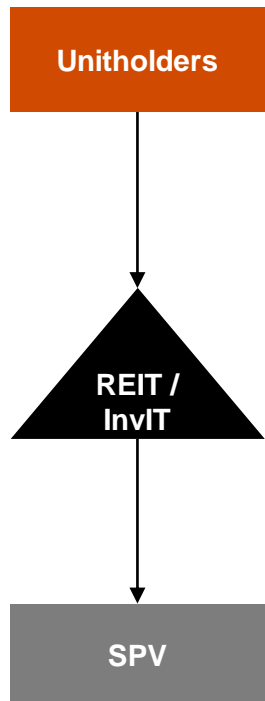
- Gains Exempt
- Other Income Exempt

- 
- TDS – Nil

- 
- Gains Taxable
  - Other Income Taxable at MMR (30%++)

Section 40A(2) –payments made to a business trust  
Chapter X – specified domestic transaction

# Tax on a slide



Level	Capital Gains	Dividend		Interest	Rent (Only for REITs)
		SPV under Old regime	SPV under new regime		
<b>Unitholders</b>	Swap of shares – Exempt		Domestic company @ 25.17% / 34.94%**	Domestic company @ 25.17% / 34.94%	Domestic company @ 25.17% / 34.94%
<b>Unitholders</b>	On transfer of units <ul style="list-style-type: none"> <li>• LTCG – 10%</li> <li>• STCG – 15%</li> </ul> (+ surcharge/cess)	<b>Exempt</b>	Resident individual @ 35.88%  NR @ 21.84% (subject to treaty benefit ?)	Resident individual @ 35.88%/ 39%/ 42.74%  NR @ 5.46%	Resident individual @ 35.88%/ 39%/ 42.74%  NR @ 43.68% (subject to treaty benefit ?)
<b>REIT</b>	<b>Sale of assets – Taxable</b>	<b>Exempt</b>	<b>Exempt TDS on payment to unitholders:</b> <ul style="list-style-type: none"> <li>• Resident @ 10%</li> <li>• NR @ 10%</li> </ul>	Exempt TDS on payment to unitholders: <ul style="list-style-type: none"> <li>• Resident @ 10%</li> <li>• NR @ 5%</li> </ul>	Exempt TDS on payment to unitholders: <ul style="list-style-type: none"> <li>• Resident @ 10%</li> <li>• NR @ rates in force</li> </ul>
<b>Asset SPV</b>	<b>Sale of assets – Taxable</b>	<b>No TDS</b>	<b>No TDS</b>	<b>No TDS</b>	<b>NA</b>

\*\* Section 80M provides for deduction on dividend received from a business trust

# Key tax compliances

- ✓ Form 64A and Form 64B
- ✓ SFT compliances
- ✓ Withholding tax compliances
- ✓ Income-tax returns
  - *No exemption to non-resident from filing returns*

	<i>REIT / InvIT</i>	<i>SPV</i>	<i>Investor</i>
Form 64A and Form 64B	✓	✗	✗
SFT compliances	✓	✗	✗
Withholding tax compliances	✓	✓	✗
Income-tax returns	✓	✓	✓





# Amendments and Recommendations

## Recent changes

- No taxes to be deducted on distribution of dividend to REIT/ InvIT
- Retaining single level tax for dividends
- 15% sponsor stake post 3 years relaxed
- Mutual Funds and Insurance Companies included in 'strategic' investor
- Private unlisted InvITs
- Enabler for Investment in debt securities of REIT/InvIT by FPI

- Capital gains deferral on swap of debentures, assets and LLP interest
- 2-tier [or more] holding structure
- Continuity of tax losses u/s 79
- Holding period for units - long term characterisation
- Deemed dividend – s 2(22)(e) exemption
- TDS - Interest on securities, distributions to SWF/PF
- Deemed income u/s 56(2)(x) on swap, proposed SPV
- Conversion of existing AIF into REIT / InvIT; Private REITs
- Lowering investment threshold
- Dividend distribution – the Companies Act
- Leverage from offshore

## Industry Asks



# 4

## Case study

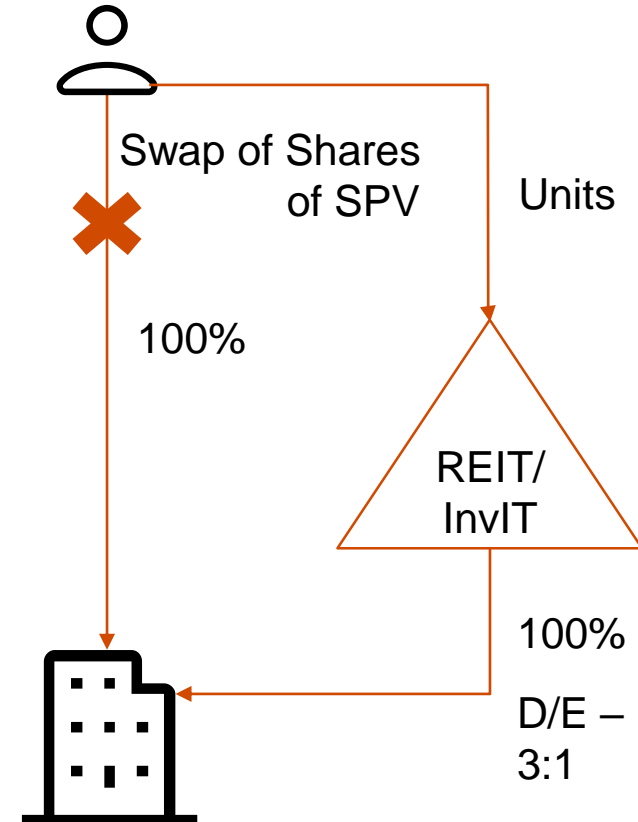
# Phase I

Year 0: Acquisition of SPV at INR 1,000

Year 1-2: Distribution of income

Particulars	Amount
Distribution of income	100.00
Tax in hands of shareholder	35.88

Year 2: Swap of shares of SPV for units of REIT / InvIT



# Phase II

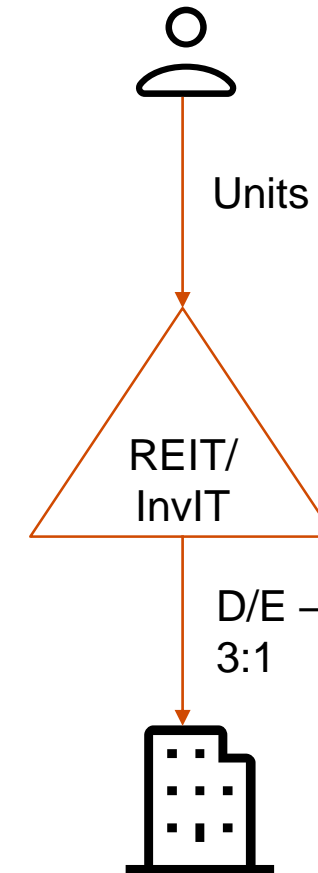
Year 0: Acquisition of SPV

Year 1-2: Distribution of income

Year 2: Swap of shares of SPV for units of REIT / InvIT

Year 3: Income distributed by REIT / InvIT

Particulars	Amount	
Distribution of dividend by SPV to REIT / InvIT	25.00	
Interest payment by SPV to REIT / InvIT	75.00	
Total Distributed Income	90.00	
	<b>Interest</b>	<b>Dividend</b>
Proportionate distributed income	67.50	22.50
Tax in hands of unitholder (resident)	24.22	0.00



# Phase III

Year 0: Acquisition of SPV

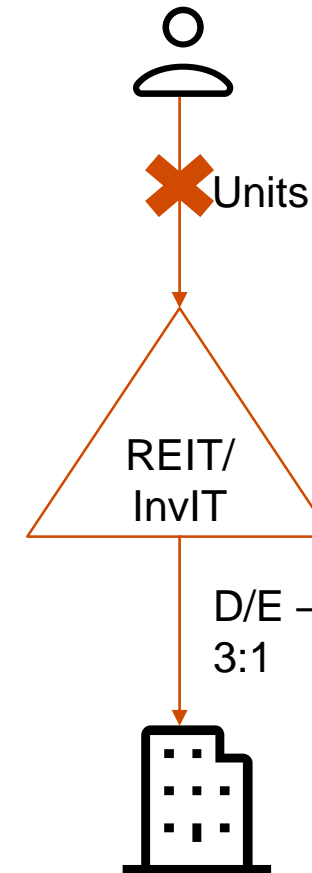
Year 1-2: Distribution of income

Year 2: Swap of shares of SPV for units of REIT / InvIT

Year 3: Income distributed by REIT / InvIT

Year 4: Sale of units of REIT / InvIT

Particulars	
Period of holding	48 months
Nature of holder	Long term
Particulars	Amount
Sale consideration	1500.00
Less: Cost of acquisition (purchase price of SPV)	1000.00
Capital Gains	500.00
Capital Gains tax (long term at 14.25%)	71.25



# Conclusions and Questions



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