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SEBI INTRODUCES NEW GUIDELINES FOR THE PREFERENTIAL ISSUE AND INSTITUTIONAL PLACEMENT OF UNITS BY REAL ESTATE INVESTMENT TRUSTS

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Under the Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2014 and relevant guidelines and circulars issued thereunder (REIT Regulations), a real estate investment trust (REIT) is required to list its units on a recognised stock exchange only through an initial public offer. Subsequently, further issue of units can be undertaken by way of a public issue (follow-on offering), preferential issue, qualified institutional placement, rights issue or bonus issue, in the manner specified by Securities and Exchange Board of India (SEBI).

Recently, SEBI issued a circular on 27 November 2019 (Circular), notifying the framework for preferential issue and institutional placement of units by a listed REIT. The Circular details the manner in which preferential issues and institutional placements are to be undertaken by a REIT and also lists out the respective disclosure requirements. In this regard, an institutional placement refers to a preferential issue of units by a listed REIT only to 'institutional investors', as defined under the REIT Regulations.

Salient Feature of the Circular

- **Conditions for preferential issuance/institutional placement** - A REIT is required to comply with the following conditions to undertake a preferential issue or an institutional placement:
 - **Resolution of unitholders:** Approval of unitholders is required, where votes cast in favour of the resolution shall be at least one and half times the votes cast against the resolution i.e. at least 60% of the valid votes would be needed in the favour of the resolution;
 - **Minimum listing period:** (a) For a preferential issue, the same class of units of the REIT should have been listed for at least 6 months prior to the date of issuance of notice to unitholders for convening the meeting to pass the resolution recording their approval;
(b) for institutional placement, the same class of units of the REIT should have been listed for at least 12 months;
 - **Compliance with continuous obligations:** Compliance with continuous listing and disclosure obligations under the REIT Regulations;
 - **Other Conditions:** The promoters, partners or directors of the sponsor(s) or investment manager or trustee of the REIT should not have been declared a 'fugitive economic offender'; and

- **Additional condition for institutional placement:** A gap of 6 months should be maintained between two institutional placements.
- **Manner of issuance** – A REIT is required to adhere to the following guidelines while undertaking the issue:
 - The new units shall be listed on those stock exchanges where the existing units of the REIT are listed;
 - The offer through private placement shall not be made to more than 200 investors (excluding institutional investors) in a financial year;
 - The cash consideration for the units shall be paid in full by the allottees prior to the allotment of units. The consideration is required to be kept in a separate bank account by the trustee of the REIT and shall be only utilised after listing of the units;
 - Post allotment, the Units are required to be listed within a period of 7 days;
 - The REIT is required to file an allotment report (with details of allottees and allotment made) with SEBI within a period of 7 days from allotment; and
 - **Additional requirement for institutional placements:** In case of institutional placements, a SEBI registered merchant banker shall be appointed as the lead manager, who is required to submit a due diligence certificate. Further, an institutional placement shall be made on the basis of a placement document which must be filed with SEBI.
- **Pricing and lock-in requirements:**

Preferential Issue	Institutional Placement
Pricing for frequently traded units*	
<p>The price shall be the higher of - the average of the weekly high and low of the volume weighted average price of the related units quoted on the stock exchange during:</p> <ul style="list-style-type: none"> the 26 weeks preceding the Relevant Date; or the 2 weeks preceding the Relevant Date. <p>“Relevant Date” shall mean the date thirty days prior to the date on which the meeting of unitholders is held to consider the preferential issue.</p>	<p>The floor price shall be the higher of the average of the weekly high and low of the closing prices of the units of the same class quoted on the stock exchange during the two weeks preceding the Relevant Date. The REIT may offer a discount of not more than 5% on the floor price, subject to approval of the unitholders.</p> <p>“Relevant Date” shall mean the date of meeting on which board of the manager decides to open the issue.</p>
Pricing for infrequently traded units	
<p>The price shall take into account the net asset value (NAV) of the REIT based on a full valuation of all existing REIT assets conducted in terms of the REIT Regulations.</p>	<p>The price shall take into account the NAV of the REIT based on a full valuation of all existing REIT assets conducted in terms of the REIT Regulations.</p>

Lock-in requirements	
<p>Units allotted to sponsors shall be locked-in for a period of 3 years from the date of receipt of trading approval. For computing such lock-in requirement, units locked-in as per the requirement under the REIT Regulations shall also be taken into account.</p> <p>Units allotted to persons other than the sponsor(s) shall be locked-in for a period of 1 year from the date of trading approval.</p> <p>The entire pre-preferential issue unitholding of allottees shall be locked-in from the relevant date up to a period of 6 months from the date of trading approval.</p>	<p>There is no lock-in requirement applicable in case of an institutional placement, however, the units allotted shall not be sold by the allottee for a period of 1 year from the date of allotment, except on a recognised stock exchange.</p>

**Frequently traded units mean the units of the REIT, in which the traded turnover on any recognised stock exchange during the 12 calendar months preceding the relevant date, is at least 10% of the total number of issued and outstanding units (or the weighted average number of total units) of such class of units of the REIT.*

- **Disclosure requirements:** The key difference in the disclosure norms for both modes of issuances is that in case of a preferential issue, the disclosures are required to be made as part of the explanatory statement to be annexed to the notice sent to the unitholders proposing the issuance of units. The disclosures prescribed are similar to disclosures prescribed in case of a preferential issue under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 including, inter alia, objects of the preferential issue, NAV of the REIT, the maximum number of units to be issued, etc.

In case of an institutional placement, the REIT is required to prepare a detailed placement memorandum, akin to a placement document in case of a qualified institutions placement under the SEBI ICDR Regulations. The Circular allows disclosures to be included by reference to any earlier offer document, placement memorandum, annual report, financials along with the links to such documents which are available on the websites of the REIT, the stock exchanges or SEBI. The REIT is required to appoint one or more merchant bankers as lead manager(s) to the institutional placement who are required to submit a due diligence certificate and furnish a copy of the placement memorandum along with any other document required by the stock exchange(s). The format of such due diligence certificate has not been specified in the Circular.

Comments

While the REIT Regulations allowed issuance of units by listed REITs through various mechanisms such as follow-on offer, preferential allotment, qualified institutional placement, rights issue, bonus issue etc., the manner was not specifically laid out for the same. The Circular is a welcome step in this direction. There are also certain points which may need further clarity from SEBI.

The Circular requires that the explanatory statement to the notice for the general meeting of the unitholders, shall disclose the NAV of the REIT. Further, with respect to the pricing of infrequently traded units, the Circular states that *"the price determined by the REIT shall take into account the NAV of the REIT based on a full valuation of all*

existing REIT assets conducted in terms of the REIT Regulations". Using the NAV to form the basis of calculation of issue price for infrequently traded units is indeed a pragmatic benchmark.

Regulation 21(7) of the REIT Regulations lays down that prior to any public offer or issue of units, the valuer shall undertake a full valuation of the assets. The valuation report should not be more than 6 months old at the time of the offer. Fresh valuation would be required in case 6 months have passed, or any material changes have occurred. Therefore, it may be inferred that the annual full valuation report prepared by the REIT (under Regulation 21(4)) may be used to reach the NAV required above, and a fresh valuation would not be required unless such valuation is more than 6 months old or there is a change in the asset portfolio of the REIT.

The definition of 'frequently traded units' considers units in which traded turnover, on any of the recognised stock exchanges, during the last 12 months preceding the relevant date is at least 10% of the total number of issued and outstanding units. This does not align with the minimum period of listing required for preferential issues (i.e., 6 months) as mentioned above. However, it may be noted that, Embassy Office Parks REIT, which has been listed for the past 8 months will be classified as infrequently traded as its trading turnover percentage vis a vis total units on the BSE was 1.42% and on the NSE was 9.58%, for the period between 1 April 2019 and 30 November 2019.

It should be noted that under the institutional placement mechanism, allotment to sponsors or managers or certain related entities, is not permitted. Regulation 11(3) of the REIT Regulations require the sponsors along with the sponsor group, to hold a minimum percentage of outstanding units post-listing (25% for 3 years post-listing, and 15% at all times). Further, each sponsor is individually required to hold not less than 5% of the total outstanding units at all times. In case an institutional placement results in dilution of a sponsor's unitholding below the required threshold, the REIT will simultaneously need to conduct a preferential issue to sponsors.

The Circular has broadened the avenues for fund raising by REITs with procedural ease. For example, in case of institutional placements, SEBI has permitted disclosures to be included by reference to any earlier offer document, annual report, financial statements, valuation reports along with the links to such documents which are available on the websites of the REIT, the stock exchanges or SEBI. This is a refreshing change from the approach followed by SEBI traditionally in case of offer documents and will make the drafting of the placement memorandum time and cost efficient. SEBI's intention to align the various requirements under the REIT Regulations to those available to companies under the SEBI ICDR Regulations appears to be a very pragmatic approach and will definitely help listed REITs raise funds in a much more effective manner.

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