REIT AT THE END OF THE TUNNEL

From 2008 to now in 2016, REIT has been a budget focus. Will it see traction now? Nirupa Shankar of Brigade Group, tries to explain the concept

ing topic of discussion over the past couple of years but the REIT market is yet to see traction. The Securities Exchange Board of India (SEBI) first attempted to create the regulatory framework for REIT's in 2008. When developers didn't bite the bait a revised framework was created in August 2014, with the Finance Minister, Arun Jaitley briefly mentioning REITs in his Union Budget of 2015. Still, developers did not create REIT's, mainly due to the tax inefficiencies in the framework. The two major issues were related to stamp duty and the dividend distribution tax (DDT). The framework required

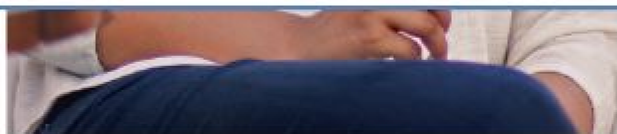
- Stamp Duty: to be paid on the market value of the asset when the Developer transfers the physical asset to the REIT, even though Developer is the Sponsor of REIT at the time of transfer of Asset
- Dividend Distribution Tax (DDT): any dividend distributed to the REIT by the SPV (which holds the physical assets and earns income) is subject to DDT.

However, there was a big breakthrough in the Union Budget of 2016, with the announcement that REIT's would have pass-through status, meaning that REIT's would be exempt from paying DDT. This would mean removing the biggest inefficiency in the current framework and the possibility of India seeing its first REIT this year. While the budget did not mention any other incentives or plans for the hospitality and tourism sector, the pass-through status given to REIT's is a light that shines for the industry as a whole.

The creation of hospitality REIT's is a massive game changer for the industry. Some of the advantages are.

I. Accessibility

REIT's create liquidity for an asset that is otherwise fairly intangible. REIT's make investment into hotels more accessible to the common investor by reducing the investment size from many crores to a few lakhs.



Nirupa Shankar, director, hospitality, Brigade Group

II. Alleviation of risk

One of the biggest fears for hotel investors who don't control the construction of a hotel is that the hotel might never come up. It's why a majority of hotel investors don't invest in green field hotel projects. Hotels are the riskiest real estate product because

a) They are capital intensive, requiring funds upfront
b) They are a specialised product with a longer construction phase (typically 3-5 years)
c) Need more than a hundred odd approvals
d) Have variable income (occupancy, ARR, F&B income is volatile and cannot be fixed like commercial office rentals)

The riskiness is not unfounded as many times, developers do run out of funds during the construction phase. The length of the construction phase also does not make sense to most financial investors who have a 5 year horizon to exit from their investment.

REIT's alleviate this fear because in a REIT scenario, at least 80% of the REIT's assets have to be revenue generating. If an asset is already revenue generating it means (in most cases) that the asset is complete, up and running and with approvals in place. SEBI guidelines are quite stringent on the criteria for assets to