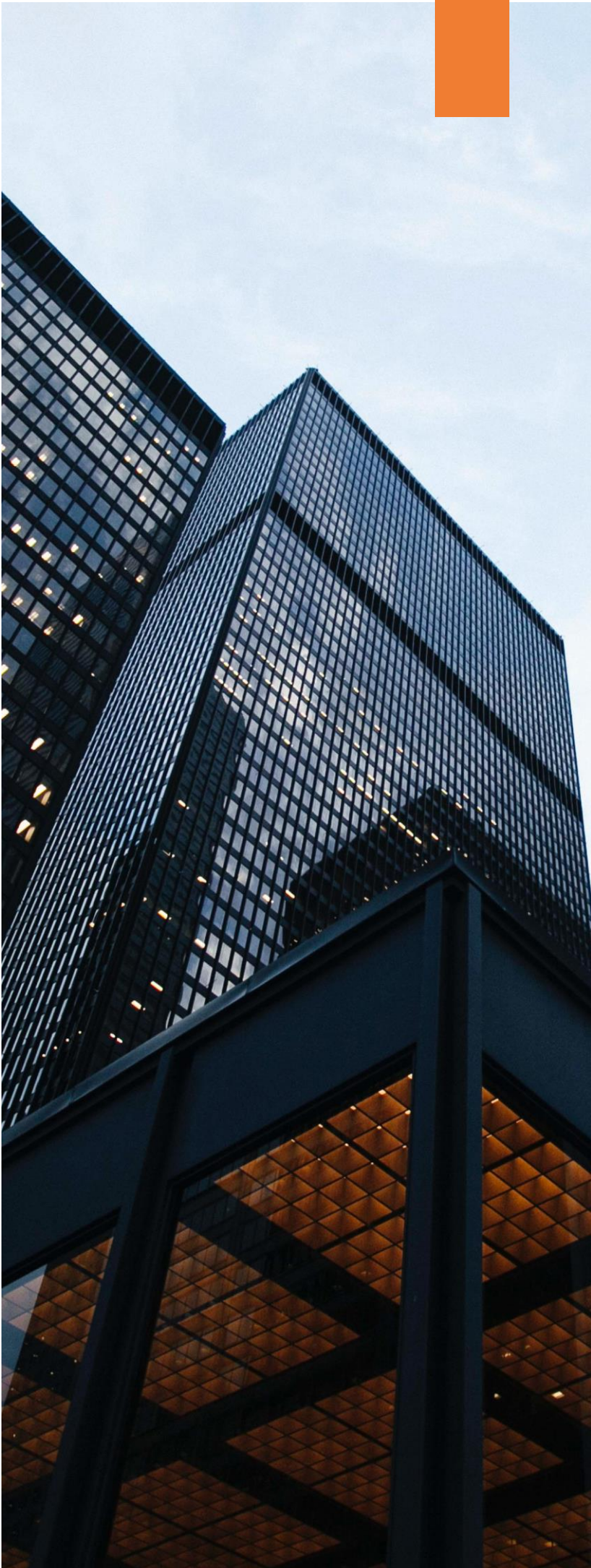


## FRACTIONAL OWNERSHIP

August 2023

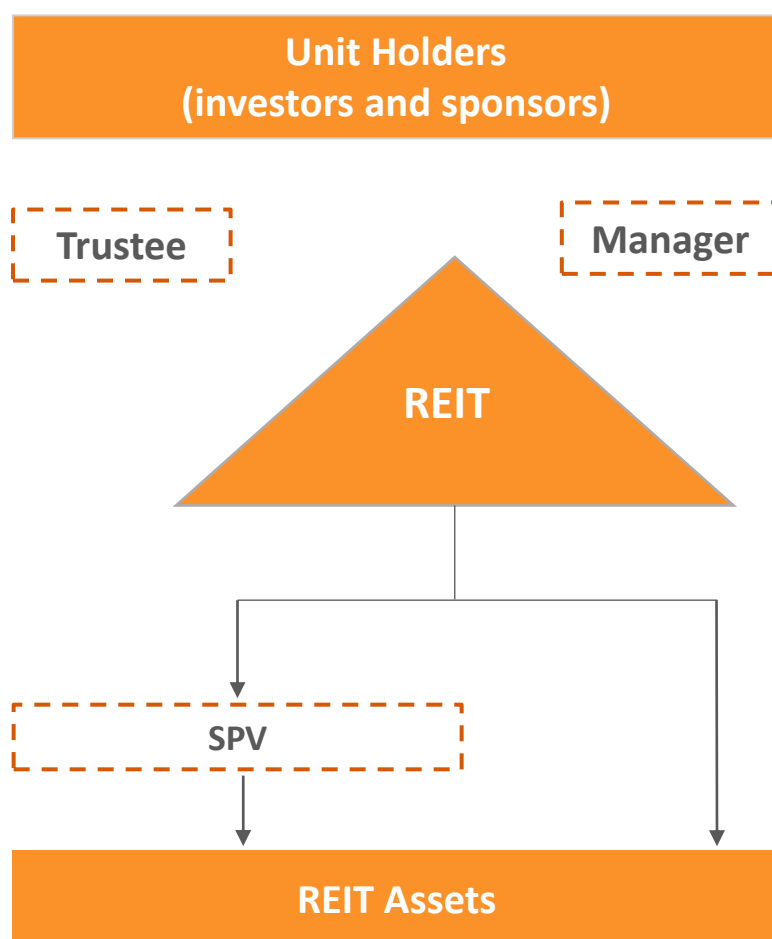


Real estate investing has historically been capital-intensive, requiring deep-pockets and long gestation periods for capital appreciation. Moreover, investing has been in the form of purchasing property or land through real estate developers and property brokers. The return generated on these investments is in the form of a rental yield and the long-term value appreciation of the property. This mode of investing limited the participation to institutional investors or individuals with considerable amount of financial resources at their disposal, given high capital requirements and illiquidity. However, new investment platforms – REITs and Fractional Ownership Platforms (FOPs) have changed the game for real estate investment.

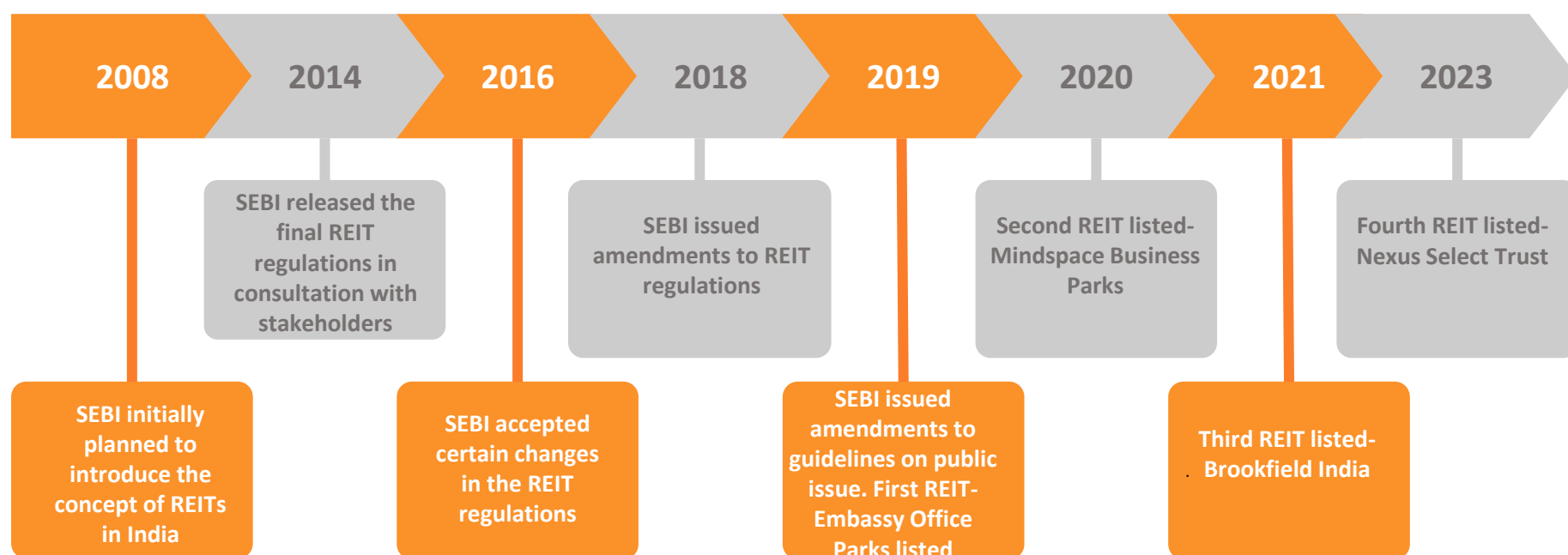
## REITs

REITs were introduced in India in 2007. These trusts democratized the participation of individual investors in real estate by allowing them to reap benefits of an appreciation in the underlying value of real estate assets without buying these assets.

A typical REIT structure is as follows:

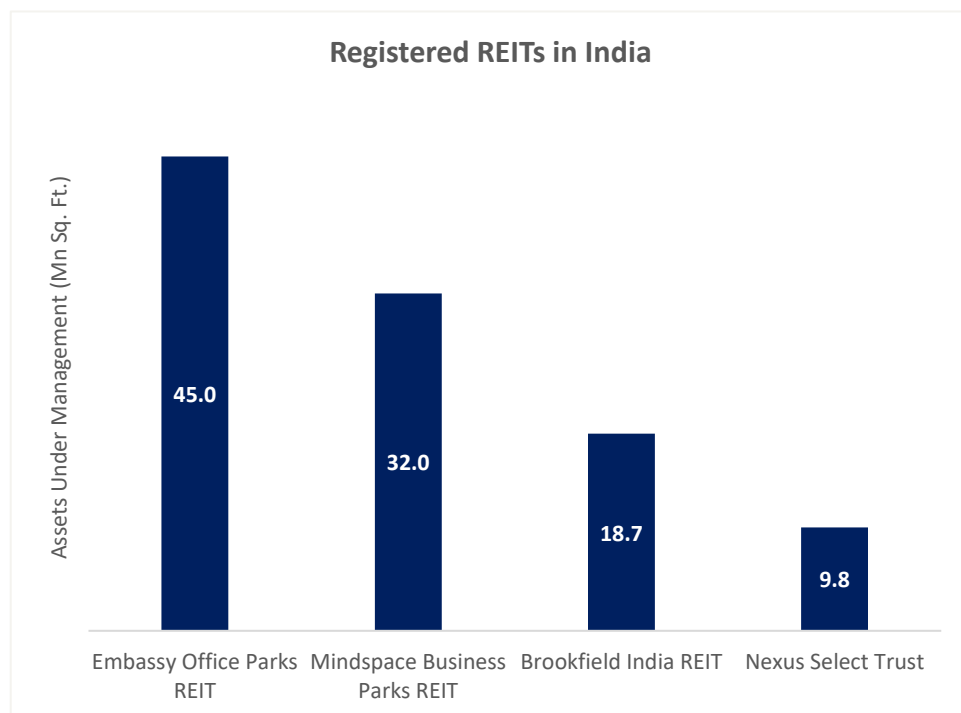


## Evolution of REITs in India



## REITs in India

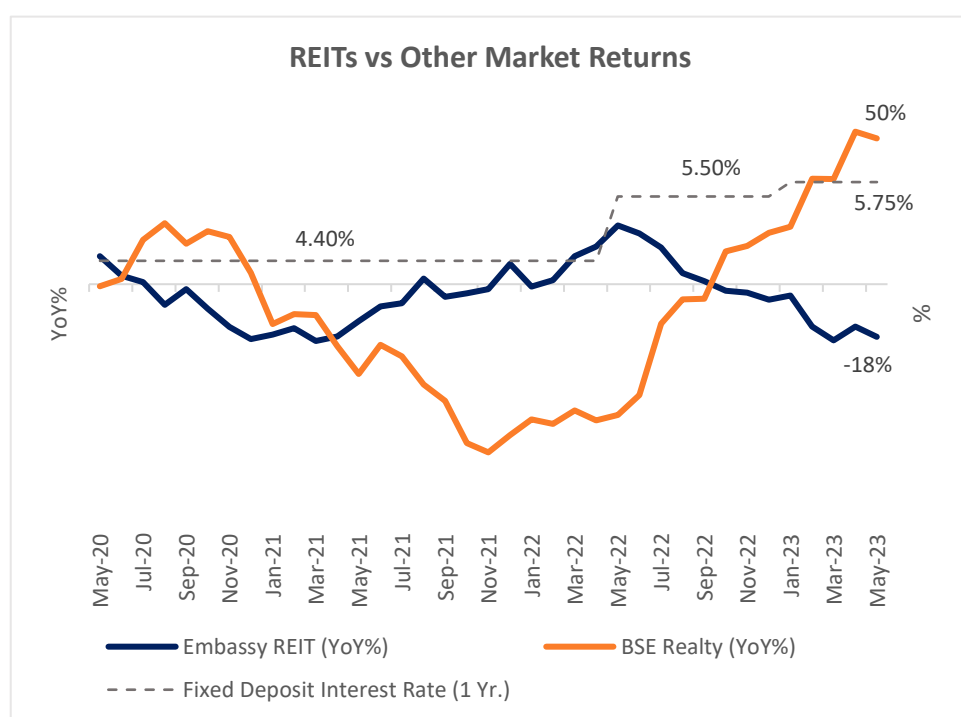
As of Jun 22, 2023, five REITs are registered with SEBI, of which four REITs have issued units which are listed on the stock exchange platforms (NSE/BSE).



Source : Company Presentations

Company	Rating	Outlook	Rating Agency	Year
Embassy Office Parks REIT	AAA	Stable	CRISIL	May, 2023
Mindspace Business Parks REIT	AAA	Stable	CRISIL	Feb, 2023
Brookfield India REIT	AAA	Negative	CRISIL	May, 2023
Nexus Select Trust	AAA	Stable	CRISIL	Apr, 2023

Source : Credit Rating Agencies' Rating Rationale



Source : NSE, BSE, SBI

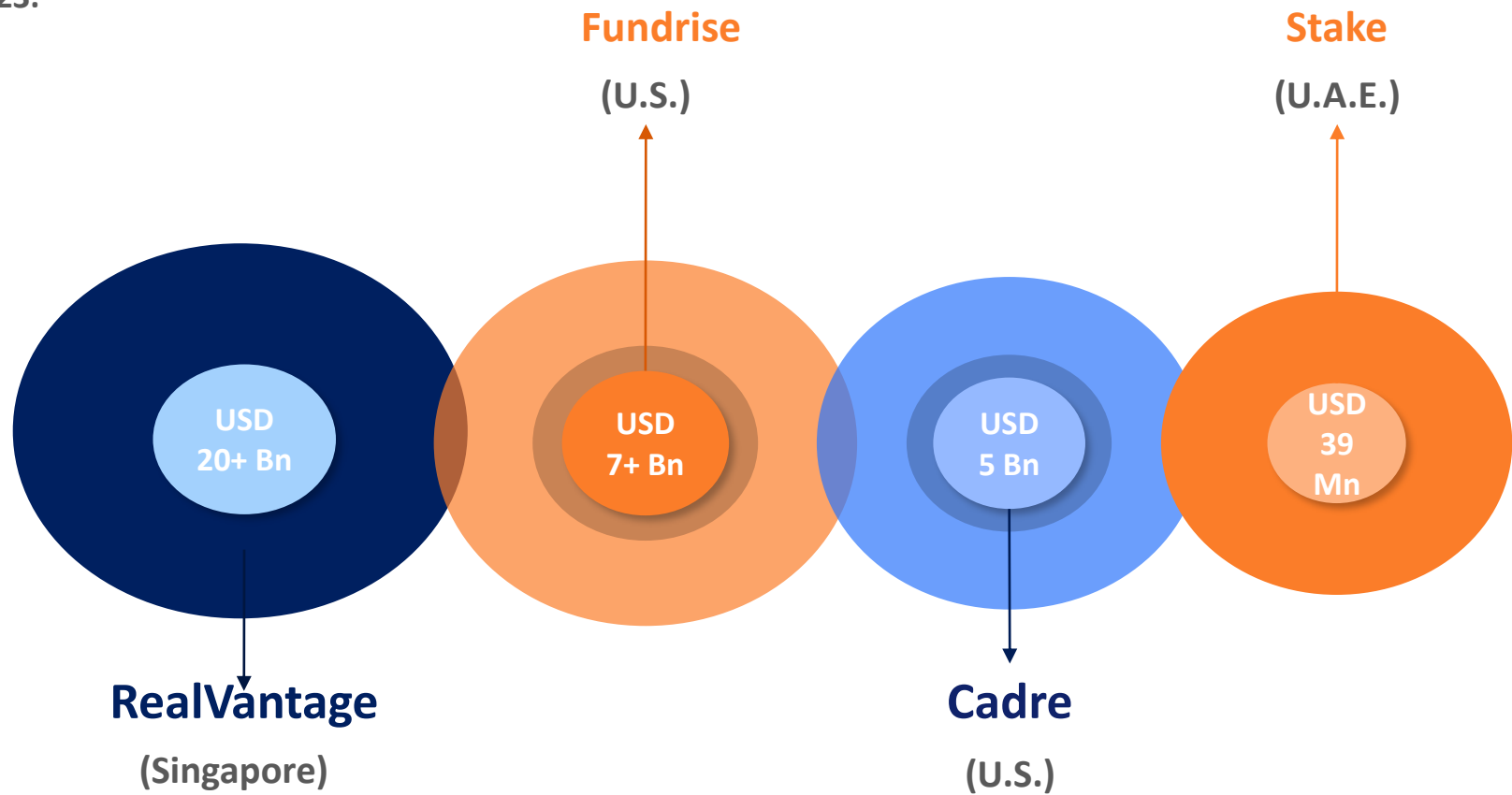
IPO	Listing Date	Total Issue Size (Rs. Cr.)
Embassy Office Parks REIT	Apr 1, 2019	4,750
Mindspace Business Parks REIT	Jul 8, 2020	4,500
Brookfield India REIT	Feb 16, 2021	3,800
Nexus Select Trust	May 19, 2023	3,200

Source : SEBI

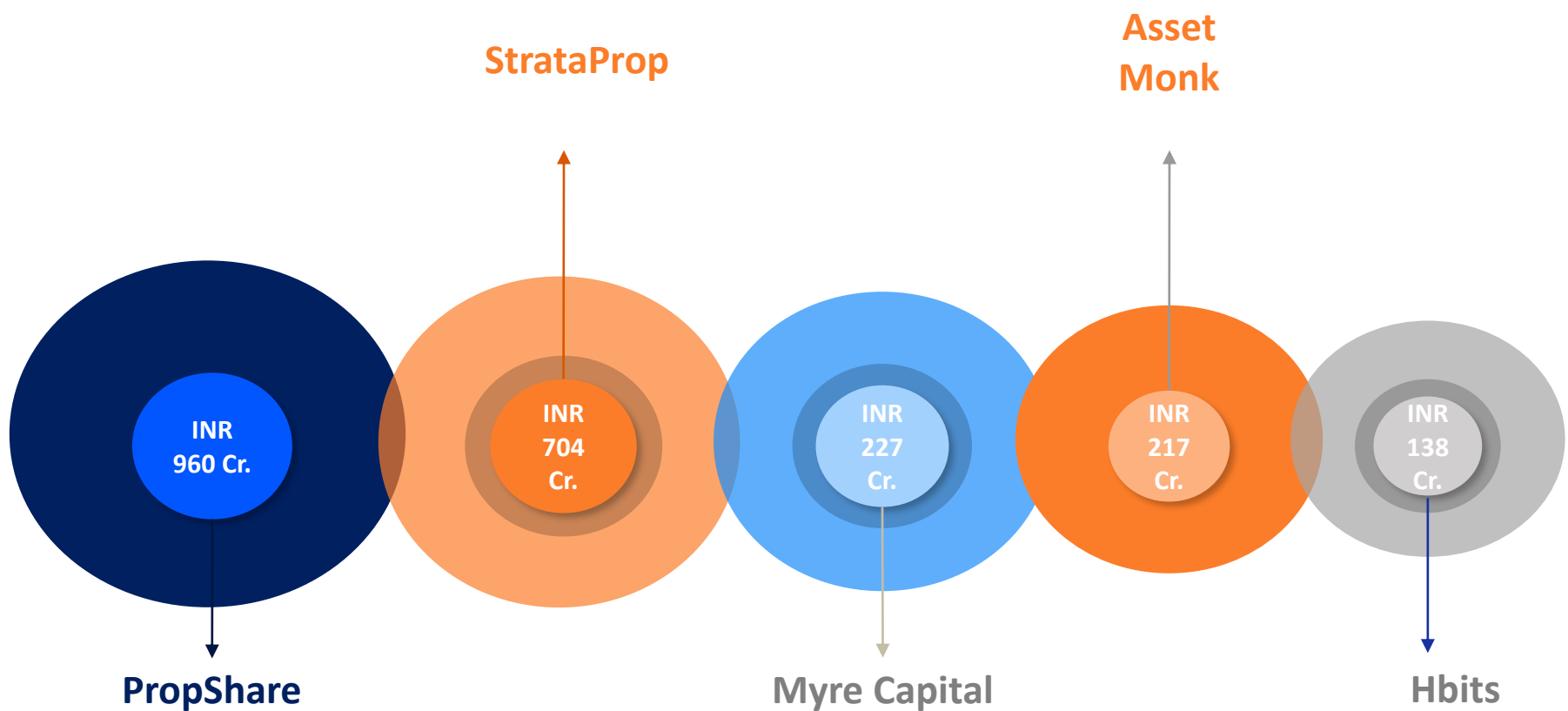
## Fractional Ownership Platforms

Fractional Ownership Platforms allow investors to own a fraction of assets. Fractional ownership typically involves the ownership of an underlying real estate asset among multiple investors. This lowers capital requirements and facilitates participation of a larger set of players in real estate asset ownership. The cost of acquisition of real estate is split among several investors, who invest in securities issued by a Special Purpose Vehicle (SPV) established by the FOP. FOPs provide a formal channel that enables a group of people to pool in money and jointly own real estate.

The chart below represents some of the leading global fractional ownership platforms based on assets under management as of 2023.



The chart below represents fractional ownership platforms in India and their respective AUMs.



**REITs Vs Fractional Ownership**

Parameter	REIT	Fractional Ownership (SEBI Proposal)
Property Type	At least 80% of assets should be completed and revenue-generating	At least 95% of assets shall be completed and revenue-generating
Cashflow Distribution	Must distribute not less than 90% of the net distributable cashflows	Must distribute 100% of net distributable cashflows
Asset selection	Investors do not have freedom of choice regarding asset selection	Investors can choose among various investment classes
Minimum subscription size/add asset value	INR 10,000-15,000	INR 10 lakh
Minimum asset size	INR 500 crore	INR 25 crore
Nature of investments	REITs can raise capital through issuance of debt securities	FOPs are not allowed to raise debt

Source : Company Reports, SEBI

Although the concept of fractional ownership of real estate is at a nascent stage in India, it is expected to grow in the next few years aided by tech-driven platforms. Estimates suggest that fractional ownership market in India jumped from INR 1,500 Cr. in 2019 to INR 4,000 Cr. in 2023.

Given the recent rise in FOPs in the country, SEBI has highlighted a few concerns and come out with proposals to regulate the industry.

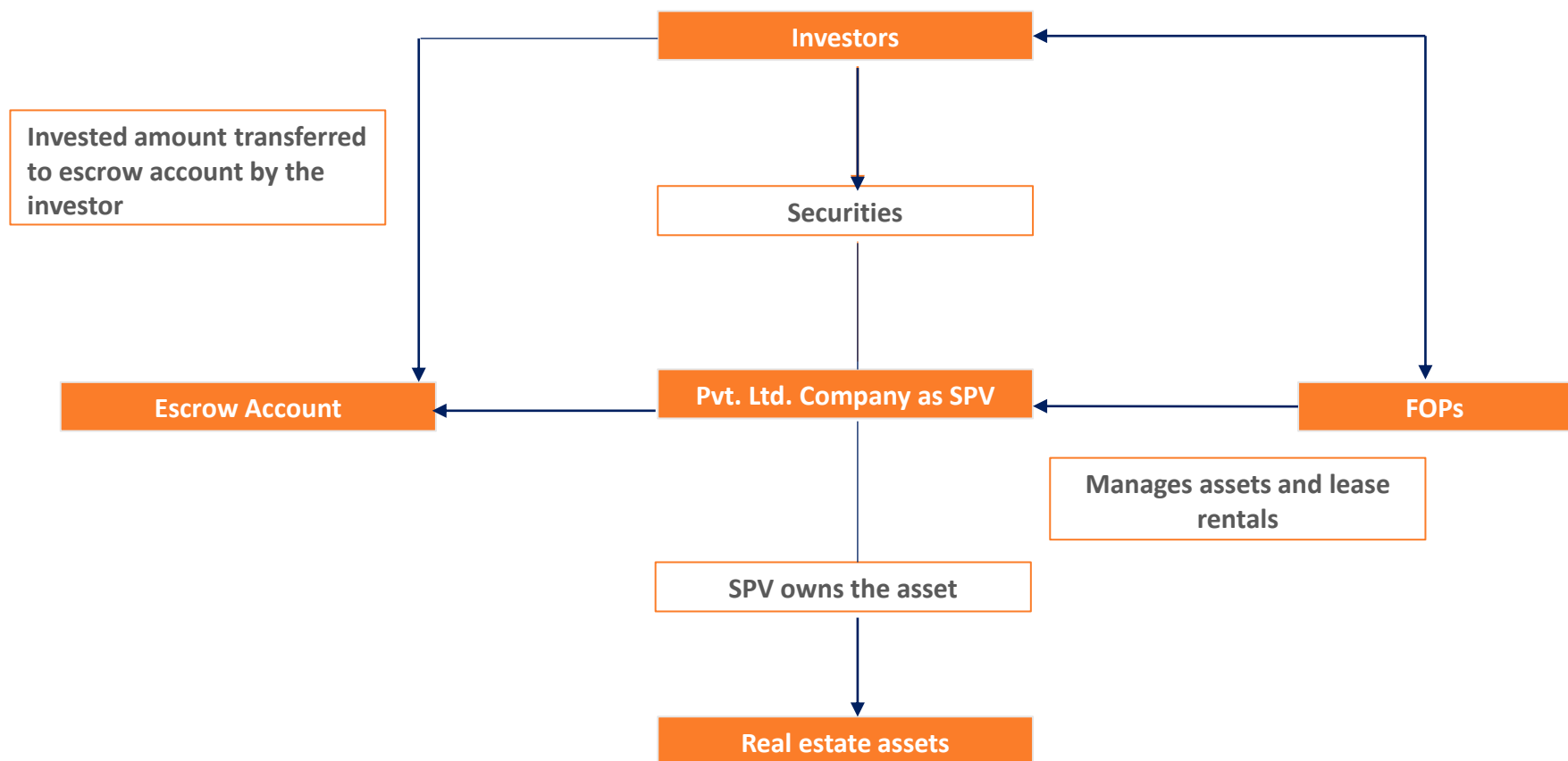
## Concerns

- Some of the FOPs are operated by real estate agents/brokers registered under RERA. The full extent and nature of operations of the FOP may not fall under the regulatory purview of RERA. Further, there is ambiguity around the structure of FOPs given the fact that they invite money from the public.
- The mode and manner of completion of the purchase/acquisition of the real estate and of issuance of the securities or confirmations may be ambiguous, opaque or not subject to independent review or oversight. *This creates a risk for investors and makes it difficult to resort to legal remedies.*
- Unlisted securities are issued to investors. This restricts the ability of the investor to exit the position in case he/she wishes to do so. *The investor is left at the mercy of the FOP.*
- KYC/AML norms are not applicable to activities of FOPs. *This creates a risk of misuse of identity credentials and money laundering.*
- Lack of uniformity for disclosures by FOPs. *This can lead to asymmetric information, which can be used by market participants to make illegal gains.*
- Lack of uniformity in addressing investor grievances and its handling. *This creates issues for investor protection.*
- There is no prescribed way of due diligence or valuations for the underlying real estate assets. *This can lead to mis-selling to potential investors.*

## Proposals

- SEBI has proposed FOPs to be registered as MSM REIT. SEBI has also proposed a minimum level of ownership of the Sponsor in the MSM REIT along with a minimum holding period. Sponsor shall have a net worth of at least INR 20 crores. Out of the same, an amount of INR 10 crores shall be in the form of positive liquid net worth. *This will ensure that the Sponsor of the REIT has some skin in the game and will lead to serious real estate players entering the FOP market.*
- Units of MSM REIT shall be mandatorily listed on stock exchanges. *This will lead to efficient price discovery and provide easy exit opportunities to investors. This will also deepen the FOP market and enhance liquidity.*
- The size of the asset proposed to be acquired should be at least INR 25 crores and should not exceed INR 499 crores. *This will ensure that the pooled money is invested in quality real estate assets.*
- At least 95% of the AUM shall be invested in completed and rent generating real estate properties. The balance 5% can be deployed in liquid assets which are unencumbered. *This will ensure better cashflows and liquidity for the REIT.*
- The MSM REIT Scheme shall raise funds from at least 20 investors that are unrelated to the Sponsor. The minimum subscription size to the units of an MSM REIT Scheme shall be INR 10 lakhs and the unit size shall be INR 10 lakhs. The maximum subscription to an MSM REIT Scheme from any investor (other than sponsor(s), its related parties, and its associates) shall not be more than 25% of the total unit capital. *This will ensure proper democratization of the ownership of the underlying real asset in the hands of genuine and serious investors. This will also ensure that no vested interests are entertained.*
- Independent and accurate valuation of real estate assets. Disclosures and reporting as per SEBI guidelines. Power to investors to change the investment manager. A cap on the expense ratio as specified by SEBI. *This will ensure that investors rights and interests are safeguarded.*

The chart below represents the operating structure currently followed by most FOPs in India



## Role of independent asset managers in MSM REITs

SEBI has laid down proposals to have regulatory oversight over FOPs and protect investor interest. However, proper implementation of the proposed guidelines and compliance with the same will be critical. Independent third-party asset managers can help FOPs identify and mitigate various risks, including operational, financial, and regulatory risks.

- **Objective Monitoring and Evaluation:** Independent asset managers bring an unbiased perspective to the monitoring and evaluation process. Independent asset managers are not affiliated with the FOPs they monitor, making them impartial observers. They can evaluate the FOPs' activities objectively and hold them accountable for adhering to SEBI's regulations without any conflicts of interest.
- **Specialized Expertise:** Third-party asset managers are often highly specialized in risk management, compliance, and investment analysis. Their expertise can help identify potential risks and violations of SEBI's guidelines, ensuring timely corrective actions. They can also help in keeping the expense ratio in check and help improve IRR for investors.
- **Transparency and Due Diligence:** Independent asset managers can conduct thorough due diligence on the FOPs' operations and investment practices. This involves scrutinizing financial statements, investment portfolios, risk management procedures, and internal controls. By ensuring transparency and accountability, these managers help maintain trust between FOPs, regulators, and investors.
- **Auditing and Reporting:** Independent asset managers can perform regular audits of FOPs' operations. These audits provide a comprehensive assessment of compliance with SEBI's guidelines and help uncover any potential issues early on. Detailed audit reports offer a clear picture of FOPs' adherence to regulations, which can be shared with SEBI, investors, and other stakeholders.

- Risk Management: Independent asset managers are skilled at identifying various types of risks that FOPs might face. They can work with FOPs to develop and implement effective risk management strategies, ensuring the stability and sustainability of the financial ecosystem. The involvement of credible third-party oversight can instill confidence in investors, reassuring them that their investments are being managed according to established regulations and industry best practices.
- Mitigating Conflicts of Interest: FOPs may sometimes struggle with conflicts of interest, where their business goals could conflict with the interests of investors. Independent asset managers, being separate entities, can prioritize investors' interests above all else and help minimize any such conflicts within FOPs' decision-making processes.
- Timely Remediation: In cases where non-compliance or issues are identified, independent asset managers can work with FOPs to develop corrective action plans. This proactive approach helps prevent minor issues from escalating into major problems, benefiting both investors and the overall market integrity.
- Investor Protection: By monitoring FOPs and ensuring adherence to regulatory guidelines, independent asset managers contribute to safeguarding investor interests. This helps prevent potential frauds or mismanagement, which can have a significant impact on investors.

Collaboration with independent third-party asset managers is one of the potential strategies to achieve SEBI's goals. The selection process for independent asset managers, as well as the mechanisms for their oversight, can be carefully structured by SEBI to ensure their effectiveness in upholding regulatory standards and protecting investor interests.

# TruBoard Partners

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Our platforms utilize Data and AI to help Capital Providers maximize their Portfolio returns. By integrating technology into the post-investment performance cycle, we enable informed decision-making in both equity and debt investment categories. Our solutions are tailored to enhance IRRs, assess asset integrity, and measure the ESG impact, offering a comprehensive perspective on investments.

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## TruGenie

A platform for Real Estate and Infrastructure Monitoring which is a comprehensive solution designed to monitor both under-construction and operational projects.

## TruCollect

A platform for retail loan portfolios will enable lenders and investors to manage their financial asset portfolios on a real-time basis.

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