Grant Thornton

#GTBharat
SHAPING VIBRANT INDIA

Infrastructure Investment Trust

An overview

May 2024

Contents

Introduction

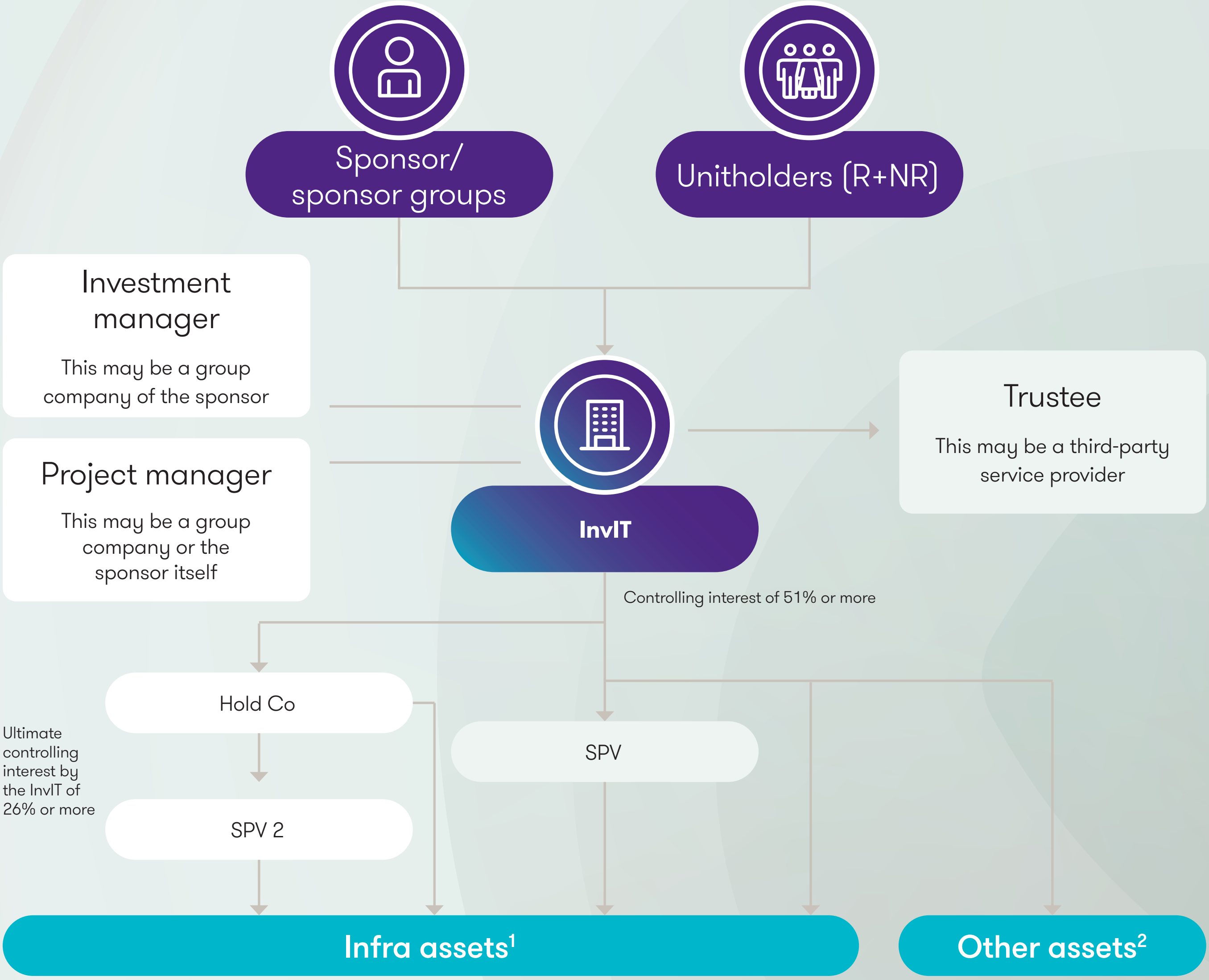
In the investment landscape, innovation goes beyond diversification; it is crucial for enhancing national infrastructure and ensuring economic stability. Since their inception under the Securities and Exchange Board of India (SEBI) Infrastructure Investment Trust (InvIT) Regulations in 2014, InvITs have exemplified innovation. They have established themselves as pivotal instruments in India's financial sector, channelling investments into robust, revenue-generating infrastructure assets.

InvITs stand out as models of financial innovation aimed at sustainable development. Designed with a tiered structure where a sponsor sets up the InvIT, which then invests in various eligible projects directly or through special purpose vehicles (SPVs), these trusts offer a unique blend of stability and profitability. The amendment of tax laws to confer pass-through status to InvITs enhances their appeal, allowing income to be taxed directly in the hands of investors and providing a tax-efficient investment structure. This arrangement not only facilitates the raising of long-term funds by infrastructure companies but also assures investors of regular returns, liquidity, transparency and accountability.

As of now, 25 InvITs have been registered with SEBI, having raised approximately INR 1.11 lakh crore. This underscores their effectiveness and the confidence they have built among investors. These InvITs encompass a diverse portfolio of infrastructure assets, including roads, highways, power plants, pipelines and warehouses, highlighting their integral role in shaping India's infrastructure development. Their ability to attract foreign direct investment without prior governmental approval has significantly broadened their investor base, enhancing their capacity to fund large-scale infrastructure projects. Although retail involvement is increasing gradually, international investors have shown strong confidence in India's InvIT framework.

This thought leadership piece explores the tax and regulatory frameworks for InvITs, as well as key considerations for establishing or transitioning into this investment structure.

Structure overview



1. Not less than 80% in completed and revenue-generating projects for public InvITs and eligible infra projects for privately-placed InvITs
2. Not more than 20% in other specified assets, including under-construction assets for public InvITs (investment in under-construction assets cannot exceed 10% of the value of InvIT assets)

Parties to InvIT

Sponsor[3]

- Can be a company, limited liability partnership (LLP) or body corporate
- Responsible for the formation of the InvIT and transfer of assets to the InvIT
- **Qualifying criteria**
  - Net worth/net tangible assets of at least INR 100 crore
  - Minimum five years of experience in infra development/ fund management in the infra sector (track record of at least two completed projects if the sponsor is a developer)
- Minimum lock-in[4] - 15% stake in the InvIT locked in for a minimum of three years; balance in excess of 15% for one-year post-initial public offering (IPO)
- Staggered lock-in introduced for additional units issued after 18 August 2023 with an initial lock-in of 5% stake for up to five years up to INR 500 crore

Investment manager[5]

- Can be a company, LLP or body corporate with an office in India
- Responsible for investment-related decisions of the InvIT
- Sponsor cannot act as the investment manager
- **Qualifying criteria**
  - Net worth/net tangible assets of at least INR 10 crore
  - Minimum five years of experience in fund management/ advisory services/development in the infra sector ('infra experience') or the combined infra experience of the directors/partners/employees of the investment manager of not less than 30 years
  - Other prescribed employee and director-related conditions

Trustee

- Registered with SEBI under SEBI (Debenture Trustees) Regulations, 1993
- Should not be related to the sponsor or investment manager
- Responsible for holding InvIT assets for the benefit of unitholders
- Shall oversee activities of the investment manager and project manager
- Cannot invest in the units of the InvIT for which it is a trustee

Project manager

- Can be a company, LLP or body corporate with an office in India
- Sponsor can act as the project manager
- Responsible for managing the InvIT projects
- Project manager of the InvIT shall be the sponsor or an associate of the sponsor and shall continue to act in such capacity for a period of minimum three years from the date of listing of the InvIT units unless a suitable replacement is appointed by the unitholders through the trustee[6]

3. InvIT (Second Amendment) Regulations, 2023 have inserted a sponsor group which can be considered for the fulfilment of conditions. Sponsor group includes (i) Sponsor(s), (ii) Entities or person(s) which are controlled by such sponsor, (iii) Entities or person(s) who control such body corporate, (iv) Entities or person(s) which are controlled by entities or person(s) as specified in (iii)
4. Separate lock-in conditions are prescribed for public-private partnership (PPP) projects; no encumbrance permitted on units held under lock-in
5. InvIT (Second Amendment) Regulations, 2023 have inserted the concept of 'self-sponsored investment manager' w.e.f. 18 August 2023. Key conditions to be fulfilled:
   - InvIT to be listed for a minimum period of five years and has undertaken not less than 12 continuous distributions and has complied with the regulations for the preceding five years
   - Investment manager to satisfy net worth criteria and minimum unit holding requirement specified for the sponsor
   - The sponsor(s) or its associate(s) are not the project manager and do not own or control the project manager or investment manager of the InvIT on or after the date of conversion to a self-sponsored investment manager
   - No transfer/sale of assets by the sponsor to the InvIT three years before and one year after the date of conversion to a self-sponsored investment manager
   - At least one of the sponsor(s) proposing to disassociate should have been a sponsor of the InvIT for a minimum period of five years
   - InvIT shall not have any under-construction assets acquired from the sponsor that have not commenced commercial operations
6. This regulation shall not be applicable where the sponsor(s) and sponsor group(s) together hold not less than twenty-five percent of the total outstanding units of the InvIT after the initial offer of units, at all times, during a period of first three years from the date of the listing of units issued in the initial offer

Key advantages to stakeholders

Developers

Liquidity

- Alternate way to monetise assets
- Easy entry and exit from infrastructure assets

Funding

- Raise funds by monetising completed projects
- Reduction in debt exposure

Business

- Transition from an asset-heavy to an asset-light model
- Focus on core competencies
- Segregation of operations and infrastructure

Investors

Entry and exit

Easier entry and exit from investment in the infrastructure sector

Transparency

Greater transparency as regulated under the SEBI Regulations

Returns

- Income stability
- Diversification of investment portfolio
- Income at regular intervals

Types of InvITs

An overview

Publicly-placed listed InvIT | Privately-placed listed InvIT

Parameters/ types of InvITs	Eligible assets (min 80% of the total assets)	Eligible investors	No. of investors	Single investor limit	Minimum investment	Borrowing limit
Publicly-placed listed InvIT	Assets need to be completed and revenue-generating	Any person – resident/foreign[7]	At least 20 investors	25% of the units[8] (other than related parties/ associates of the sponsor)	INR 10,000 to INR 15,000	Borrowing[9] cannot exceed 70% of the value of the InvIT assets
Privately-placed listed InvIT	Eligible infrastructure assets	Institutional investors and body corporates (Indian/foreign[7])	At least five investors[10] and up to 1,000 investors		INR 1 crore or INR 25 crore[11]	

Notes:
7. In the case of foreign investors, such investment shall be subject to the Reserve Bank of India (RBI) guidelines
8. Investment in excess of 25% is obtained only on approval from 75% of the unitholders by value (excluding units held by investors along with associates)
9. The 70% limit is computed for aggregate consolidated borrowings and deferred payments of the InvIT, Hold Co and SPV (net of cash and cash equivalents) – this is subject to the credit rating and other conditions/requirements
10. Other than the sponsor or its associates
11. If the InvIT proposes to invest not less than 80% of the value of the InvIT assets in completed and revenue-generating assets

Tax implications

InvIT

Transaction	Tax implications
Interest received from SPVs	Exempt in the hands of InvIT
Dividends from SPVs (where SPVs have not opted for the concessional tax regime)	Exempt in the hands of InvIT
Income from directly-held assets/other income	Taxable at the maximum marginal rate
Capital gains on the sale of assets/shares of SPVs	Taxable at applicable rates (under Sections 111A and 112) depending on the period of holding
Withholding tax (WHT) obligations	**Distribution to unitholders subject to WHT** • Interest to a resident at 10% and to a non-resident at 5%[12] • Dividend to a resident at 10% and to a non-resident at 10%[12] (only if the SPV has opted for the concessional tax regime under Section 115BAA)

Unit holders[13]

Transaction	Tax implications
Interest income from the SPV distributed by the InvIT	• Resident investor – at applicable rates (credit for taxes withheld at 10%) • Non-resident investor (other than foreign portfolio investors (FPIs) – 5%[12] (subject to the beneficial provision under the applicable tax treaty) • FPIs – may be taxed at 20%[12] (subject to the beneficial provision under the applicable tax treaty)
Dividend income (if SPV has opted for the concessional tax regime under Section 115BAA)	• Resident investor – at applicable rates (credit for taxes withheld at 10%) – benefit of Section 80M extended to domestic unitholder being a company, provided such dividend is distributed within the prescribed timeline • Non-resident investor (including FPIs) – 20%[12] (subject to the beneficial provision under the applicable tax treaty)
Dividend income (if SPV has opted for the old regime)	• Exempt for unitholders
Distribution of any proceeds other than interest and dividend; not taxable in the hands of InvIT	**Distribution in excess of the issue price shall be taxable as income from other sources at applicable rates** • Resident investor – at applicable rates • Non-resident investor (other than FPIs) – taxable at applicable rates (subject to the beneficial provision under the applicable tax treaty, credit available for taxes withheld) • FPIs – 20%[12] (subject to the beneficial provision under the applicable tax treaty)
Sale of listed units (on stock exchanges)	• Long-term capital gains beyond INR 0.1 million taxable at 10%[12] • Short-term capital gains taxable at a concessional rate of 15%[12] • For non-residents, provisions and rates under applicable tax treaties to be considered

12. Increased by applicable surcharge and cess
13. Income of unitholders is exempt in certain situations:
    - Income of specified sovereign wealth funds (SWFs)/pension funds from investments in InvITs subject to certain conditions
    - Capital gains from the transfer of InvIT units listed on a recognised stock exchange by a non-resident in an international financial services centre (IFSC) in India if consideration for such transfer is paid in foreign currency
    - Dividend income, if such dividend is from an SPV which has not opted for the concessional tax regime under Section 115BAA

Sponsor

Transaction	Tax implications
Swapping of shares of SPVs with units of InvITs	• Transaction not regarded as 'transfer' and no tax implication on exchange/swap of shares for units • Deferral of minimum alternate tax (MAT) implications
Swapping of assets with units of InvITs	• No specific exemption under the tax law • Taxable under normal provisions and under MAT
Sale of units listed on the stock exchange	• Long-term capital gains beyond INR 0.1 million taxable at 10%[14] • Short-term capital gains taxable at a concessional rate of 15%[14] • For non-residents, provisions and rates under applicable tax treaties if eligible to access tax treaty

SPV

Transaction	Tax implications
Interest paid to the InvIT	• Deduction available to SPV
Capital gains on the sale of assets	Taxable at applicable rates depending on the period of holding
Income from an infrastructure asset	Taxable as business income
WHT obligations	• No withholding required for dividend • No withholding required for interest

14. Increased by applicable surcharge and cess

Migration of assets to InvITs: Key considerations

01 Restriction on multi-layer holding

If the existing structure for holding InvIT assets includes more than two layers, the sponsor group may need to restructure its holdings.

02 Capital structure and leverage

InvIT regulations impose a limit on total debt levels; therefore, it is essential to streamline external borrowings and examine the methods of transfer and capital structure.

03 Lock-in requirement for the sponsor

InvIT regulations mandate a staggered lock-in requirement for the sponsor of 5% for five years, including 1% to be held till perpetuity. A structure needs to be ensured that enables continuity for the sponsor or a plan to migrate to a self-sponsored investment manager.

04 Disinvestment of non-core assets

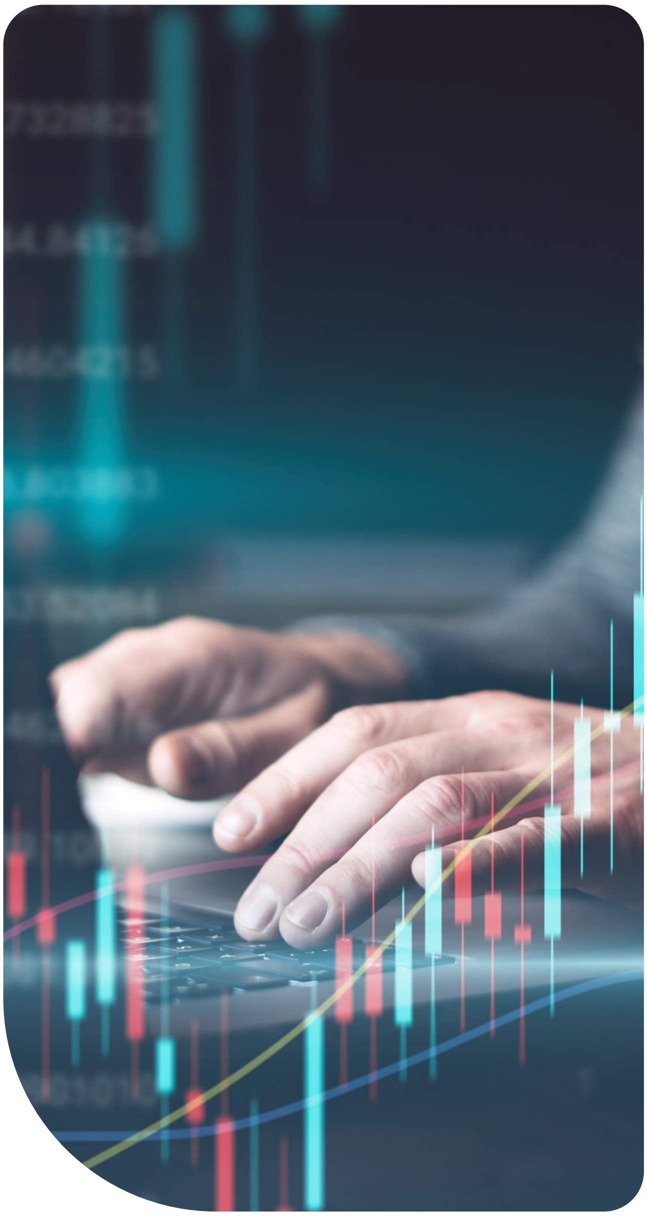
Since InvITs are allowed to hold only infrastructure assets, any non-infrastructure assets must be divested or separated.

05 Sponsor and investment manager eligibility

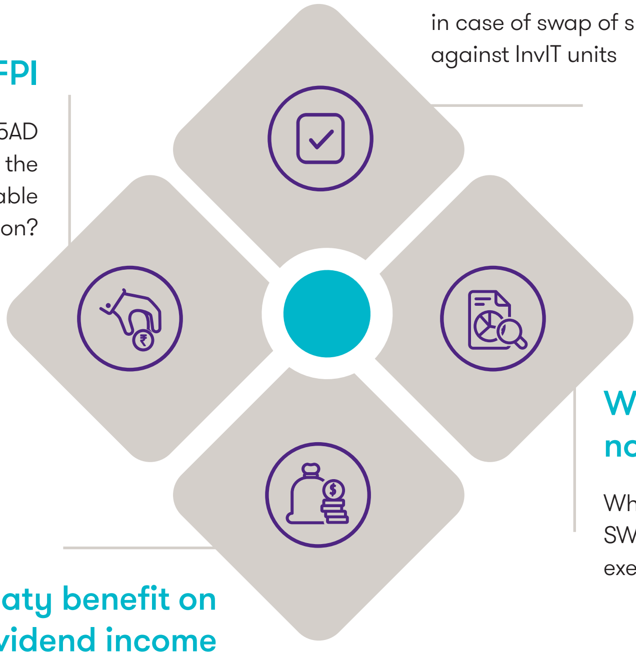
It is important to identify the key parties involved in the InvIT to ensure they meet the required experience criteria in the infrastructure sector.

06 Transfer of assets to InvIT for a limited period

The structural setup should consider the potential need to transfer certain assets to the sponsor.



Key tax issues



Swap by non-sponsor

Whether tax benefit is available in case of swap of shares of SPV against InvIT units

FPI

Taxability under Section 115AD or any other section of the Act; what is the applicable withholding tax provision?

WHT on payment to notified SWFs

While the income earned by SWF is exempt, no specific exemption from WHT

Treaty benefit on dividend income

Whether the dividend from an SPV would be covered under provisions of a tax treaty

Annexure

List of infrastructure assets

Transport

- Roads and bridges
- Ports
- Shipyards
- Inland waterways
- Airport
- Railway track, rolling stock along with workshop and associated maintenance facilities, and terminal infrastructure, including stations
- Urban public transport
- Logistics infrastructure
- Bulk material transportation pipelines

Energy

- Electricity generation/transmission/distribution
- Oil pipelines
- Oil/gas/liquefied natural gas (LNG) storage facility (including strategic storing of crude)
- Energy storage systems

Water and sanitation

- Solid waste management
- Water treatment plants
- Sewage collection, treatment and disposal system
- Irrigation (dams, channels, embankments, etc.)
- Storm water drainage system

Communication

- Telecommunication (fixed network)
- Telecommunication towers
- Telecommunication and telecom services
- Data centres

Social and commercial infra

- Educational institutions
- Sports infrastructure and hospitals
- Tourism infrastructure – three-star or above hotels/ ropeways and cable cars
- Common infrastructure for industrial parks and other parks with industrial activity, such as food parks, textile parks, special economic zones (SEZs), tourism facilities and agriculture markets
- Post-harvest storage infrastructure for agriculture and horticultural produce, including cold storage
- Soil-testing laboratories
- Cold chain
- Affordable housing, rental housing complex and exhibition cum convention centre

Acknowledgements

Authors

Shabala Shinde
Partner and Real Estate & REITs Industry Leader
Grant Thornton Bharat
shabala.shinde@in.gt.com

Contributors

Janhvi Shah
Yash Davda

Editorial review

Sonali Lingwal

Design

Ashwani Kumar

For media enquiries, write to

media@in.gt.com

Great Place To Work® Certified DEC 2023 – DEC 2024 INDIA

Best Workplaces™ in Professional Services Great Place To Work® INDIA 2023

We are
Shaping Vibrant Bharat

A member of Grant Thornton International Ltd., Grant Thornton Bharat is at the forefront of helping reshape the values in the profession. We are helping shape various industry ecosystems through our work across Assurance, Tax, Risk, Transactions, Technology and Consulting, and are going beyond to shape a more **#VibrantBharat.**

Our offices in India

- Ahmedabad
- Bengaluru
- Chandigarh
- Chennai
- Dehradun
- Delhi
- Goa
- Gurgaon
- Hyderabad
- Kochi
- Kolkata
- Mumbai
- Noida
- Pune

Scan QR code to see our office addresses

www.grantthornton.in

Connect with us on

@Grant-Thornton-Bharat-LLP

@GrantThorntonBharat

@GrantThornton_Bharat

@GrantThorntonIN

@GrantThorntonBharatLLP

GTBharat@in.gt.com

6727 | SL | AK2