FEDERATION OF INDIAN CHAMBERS OF COMMERCE AND INDUSTRY

POINTS FOR DISCUSSION ON "FDI POLICY – ISSUES IN REAL ESTATE"
11 MAY, 2011, FEDERATION HOUSE, FICCI, NEW DELHI

1. Minimum area development and minimum capitalization norms for FDI in real estate

- It has been observed that 80% of real estate FDI has gone into the tier-1 cities. Little have gone to the tier 2 or 3 cites. The existing minimum area development norms for real estate development is blocking the foreign capital from going to smaller cities. It is therefore suggested that the minimum area development conditions of 10 hectares or 50,000 sq mts should be reduced to enable greater flow of foreign capital into India especially to the tier 2 or 3 cities which are otherwise starved of capital and expertise in real estate development.

- Similarly, the minimum capitalization norms also need to be rationalized as it blocks foreign capital from investing in small projects. The minimum capitalization norms of US$ 10 million for a wholly owned subsidiary and US$ 5 million for joint ventures with Indian partner/s should be relooked.

- The minimum capitalization norms should apply at the entity level and not at project level as it is proposed now. FDI policy relates to equity investment in Indian companies but it is now proposed to extend this to the project level.

2. Lack of consistency in interpreting the three year lock-in period condition

- Press Note 2 of 2005 announced a minimum lock in period of 3 years from completion of minimum capitalisation for repatriation of original investment, except with the prior approval of the Foreign Investment Promotion Board ("FIPB").

- Circular No. 02 of 2010 has clarified that "original investment" refers to the entire amount brought in as FDI and not just the minimum capitalization. It has further clarified that the lock-in period of three years would apply from the date of receipt of each tranche of FDI, or from the date of completion of minimum capitalization, whichever is later.

- DIPP has in the past provided several clarifications stating that the lock in applies only to the minimum capitalization amount of US$ 5 million or US$ 10 million. The lack of consistency in the lock-in period has created confusion and fear among the foreign investors. As a consequence, the risk weightage for real estate projects is going to go up, leading to an increased cost of capital which would ultimately result in increased pricing.

- It is therefore suggested that the condition of each tranche being locked-in for 3 years should be removed from the guidelines. Lock-in condition should either be completely removed or it should apply only to the minimum capitalisation as was set out in the original guidelines of 2005.

3. Allow FDI in both Greenfield & Brownfield Real Estate Projects

- Presently FDI is allowed only in greenfield real estate projects. But there is a need for clarity on what constitutes a green field project. Under the existing policy, the extent of development up to which FDI is permissible is not clear. FDI in greenfield projects is fraught with challenges and difficulties which a foreigner investor is typically ill equipped to handle (eg. sanctions and approvals).

- FDI investors are already being questioned by regulators on whether acquisition of land and seeking clearance to do development thereon is a permitted activity (agricultural land issue). An "existing" project could very well mean projects which have already been approved by the local authority. Therefore if acquisition of land and conversion of its end use is not permitted and projects already approved are not permitted, then the spectrum of projects which can be undertaken with FDI is negligible. India can encourage more FDI if foreign investors are permitted to invest in brownfield and completed projects.

4. Exit Clause for Foreign investors in FDI policy

The FDI policy must state few conditions that will enable easy exits to foreign investors in cases which are beyond the control of the investors/developers;

- Enable early exit of capital in case of failure to obtain regulatory approvals
- Enable early exits in the event of idle projects, litigation among joint venture/fund partners, mutual decision to end development of a project or completion of certain percentage of the project
- Relax criteria for sale of land to enable liquidation of assets in case of abortion of project

5. **Removal of prohibition on sale of undeveloped land**

Currently, there is a prohibition on sale of undeveloped land under the FDI policy. When a company tries to acquire land privately it does not necessarily get all contiguous land. It gets smaller non-contiguous pieces of land which are sometimes in excess and need to be exchanged or sold. The rule regarding the sale of undeveloped plots should be relaxed by having a provision in the policy that allows sale of undeveloped land at a “No Profit No Loss” basis to recover the amount invested.