

AUGUST 2020

ISSUE BRIEF

KNOWLEDGE

WEB-SERIES

SESSION V

**REAL ESTATE
SECTOR, IBC, THE
AFFORDABLE
RENTAL HOUSING
COMPLEXES
SCHEME**

Jointly Organised by



SUMMARY

On 29th August 2020, Hammurabi & Solomon Partners & the India Strategy Group jointly convened a knowledge web-series (“KWS”) to discuss the role of IBC in relation to the real estate sector, the potential avalanche of project delays post Covid-19 and affording housing targets for the real estate sector. This report tries to capture the discussions with the distinguished speakers and to highlight the dos and don’ts in this regard.

The KWS was convened with the aim to discuss, deliberate, and analyze implications of recent legal developments – legislative, regulatory/policy as well as judicial pronouncements.

DISTINGUISHED SPEAKERS



Hon'ble Mr. Justice S.J. Mukhopadhyaya
Former Chairperson, NCLAT &
Former Judge,
Hon'ble Supreme Court of India



Mr. Amrit Abhijat, IAS
Joint Secretary,
Ministry of Housing and Urban Affairs -
Government of India



Dr. Manoj Kumar
Founder & Managing Partner,
Hammurabi & Solomon Partners



Ms. Shweta Bharti
Senior Partner,
Hammurabi & Solomon Partners



Mr. Gopal Menghani
President - Legal
Lodha Group



Ms. Parveen Mahtani
Chief Legal Officer,
Mahindra Lifespace



Ms. Anjana Bali
Head of Legal,
DLF Home Developers Ltd.

KEY POINTS

Role of IBC in the Real Estate Sector

Given the circumstances which the pandemic has created, the IBC and the NCLT have a very unique position and role to play in the real estate industry especially in addressing the challenges being faced by various real estate sector stakeholders including developers, home buyers, and financial creditors.

The Central Government has introduced certain remarkable policies for affordable housing and addressing the challenges being faced by the real estate industry can be addressed by developing a very efficient understanding and working of the policies, the IBC and the workings of the NCLT to balance out the equation to serve sustainability.

As a background, housing for all has been a motto for the Central Government. It is estimated that the Real Estate sector will grow exponentially from Rs.5000 crore in 2019 to a Rs.12000 crore industry in 2040. The Real Estate market is estimated to contribute about 13% to India's GDP.

Prior to 2016, the real estate industry carried a perception of being hugely unregulated, however the said perception has considerably changed by the introduction of two key acts: RERA and IBC. This legal framework has completely changed the way in which the sector conducts its business.

Focusing on the functioning of IBC, the Real Estate Industry Insolvency Law Reforms Committee in November 2017 made recommendations for certain changes and since then we have seen certain key developments in the IBC specific to the real estate industry, such as treating allottees under Real Estate projects as Financial Creditors and affording them representations in the CoC. The reasoning behind this is that in many projects, allottees contribute more than the Financial Creditors.

Post Amendment, a plethora of CIRPs were filed against developers, and settlements were made out of fear. Pursuant thereto, the modalities by which homebuyers can file IBC petitions before the NCLT have also been conditioned.

Developments in IBC in the context of the Real Estate Sector

The developments in IBC in the context of the real estate sector can be understood by focusing on certain key developments: In the case of Nikhil Mehta and Sons v. AMR Infrastructures, NCLAT held that the allottees, flat-buyers, shop-buyers come within the scope of IBC Sections 5, 7 read with sub section 8. A clarification was made through an appeal about the status of the allottees.

Things changed with the advent of Essar Steel by NCLAT. Bankers had a delusion for being secured creditors. After the Essar Steel judgment, there was hue and cry among the bankers, as all of them had thought (law laid down in Swiss Ribbons) that they are all above operational creditors. A question that arises is that who will understand the viability and feasibility of a corporate? Is it the industries and the business houses or the banks? To answer this, it is operational creditors who will understand the place of business, type of business, feasibility, etc. Hence, operational creditors must be identified by the government as they know about the corporate debtor.

The second thing that has to be looked at is the principle of “Going Concern” and the Maximization of asset value of the corporate debtor in a time bound manner. While Essar Steel was under the guidance of Resolution Professional, they continued production of steel and also worked up a profit of almost Rs. 3,500 crores.

Maximization of assets means maximization of the assets of the particular project. Company X has 3 projects. Everywhere the financial as well as operational creditors are different but the corporate is common. So, if there's a corporate insolvency resolution process, will it hamper the other projects? No. [e.g. Essar Steel case]. Cumulative assets will keep on growing during the insolvency process and information memorandum stands redundant.

Similarly, infrastructure companies also continue delivering upon the projects, and the same shall be preserved and allowed to function in order to achieve “going concern” & “asset maximization”. Who actually are secured creditors? For instance; Banks give loans to corporations for land. This makes them a secured creditor to the land, and not the buildings. Whereas, other financial creditors are giving out loans for a particular flat, yet they are unsecured creditors.

Circumstances where there will be no initiation of corporate insolvency resolution process [Navin Raheja v. Shilpa Jain and Ors.] Despite not being an act of god, the circumstances are beyond control, for eg., stagnant production, lack of raw material, matter pending before govt. for granting license and other purposes. Navin Raheja v. Shilpa Jain and Ors. held that no insolvency process shall be initiated in such cases.

In a landmark case handled by Hammurabi & Solomon Partners, the National Company Law Appellate Tribunal in the case of Flat Buyers Association Winter Hills Vs. Umang Developers introduced the principle of reverse insolvency with focus on dealing with the interests of all stakeholders as well as meeting the needs for survival and sustainability of real estate businesses. With the introduction of Reverse Insolvency process, the CIRP for the specific project wherein completion is pending is worked out by carving a plan wherein the developers cooperate with the Resolution Professional with prescribed timelines for completion.

Pradhan Mantri Awas Yojna

Started in June 2015 under the Ministry of Housing and Urban Affairs, Government of India, Pradhan Mantri Awas Yojna is designed to take care of the housing needs of the entire country. The initial target is to provide 5 crore houses in India and is based on the spirit of cooperative federalism. While all the structural and logistical needs were taken care of by the State Government, the Central Government only supervised whether the scheme was implemented efficiently. Incidental housing program has transformed into a comprehensive housing program for both urban and rural areas. The scheme also provides financial aid to any buyer who is eligible under the Credit Linked Subsidy Scheme; whereas the houses are primarily made by the private sector.

Impact of COVID19 on Migrants

Reverse migration of labour is a serious challenge. Had they had a housing facility, they wouldn't have to travel back in despondency. Such an event not only affects the people but the economy as well. As large number of units are opening up but owing to the migration, had no labour force to work.

A sub scheme for affordable rental housing complex scheme was formulated to arrange rental housing for migrants. Migrants are not only workers but students, nurses, helpers, etc. If they belong to the EWS and have income of 3 lakhs or more, they can claim housing. It was implemented immediately and will go on till March 2022. The scheme will apply to all the statutory towns, all the notified planning areas, and all the developmental authorities.

Models of The Affordable Rental Housing Complex

Model 1: Identify the unoccupied houses from earlier schemes of both centre and states; or houses that have become run down. It was decided to let there be a private entity that will bid it out and the state govt. will fix a nominal rent. Any bidder who will take grant will be paying back money as soon as possible with the lowest possible rent. As and when they are able to recoup the investment made, they will then share the profit with an urban local body which can be fixed mutually.

Model 2: This model is much more comprehensive. Anybody who has a piece of land can go to the State Government and can say that they want to make an affordable rental housing complex. Income tax and GST is waived off. State Government also provides Trunk Infrastructure, they also provide municipal services only at residential costs and not at commercial rates. Additionally, lower rate of interest incentives in terms of technology innovation grant and also incentives in terms of GST, income tax, FSI, land use permission, etc. This model encourages and creates an ecosystem wherein the private investors can avail this scheme if they have a piece of land. The investing plate becomes much larger as government solely is not responsible for the investing as private corporate entities are also taking part in the model.

The objective of the specific EWS scheme must be met

It is pertinent that the timeline of completion, for state entities and the private bodies are matched. Often, the townships are ready, but the trunk infrastructure is not. The objective of the specific EWS scheme needs to be met, and it should be ensured that the targeted section is benefitted. The gaps should be filled efficiently and black marketing should be safeguarded against.

The Government of India is investing in the ecosystem of this scheme, i.e incentives based on cost and technology. There is some amount of trust that has to be built between, the people, the developers and the Government.

It has been very peculiar to India where the private development takes place at a much faster pace than the Trunk Infrastructure which impacts the saleability of real estate projects and in this case the rental scheme itself.

Therefore, there are some safeguards as to what rentals and projections have been calculated to the possibility of coming through. Also, one of the provisions says that if the project is not completed within the timeline, the investments and the grants which have been made will be called off with interest, but like in any contract, it would still need to provide force majeure options..

These exceptions need to be carved out for fair play. In model no. 2, where the land also needs to be bought or contributed as a part of the entire capital cost, whether land could be subsidized or taken through land acquisition process, so that the capital investment is slightly reduced thereby making it a larger implementable scheme.

Two additional things that have been made available. First, Trunk Infrastructure is being developed at a cost of State Government or the planning authority. Second thing is that, the developer is able to monetize it.

It will become necessary for the Central Government to impress upon the State Governments to modify or amend their developmental control regulation to bring this as a chapter legislated to make things clear. Legislation helps in a way that if there exist any misdemeanors on the part of developers or the tenant, there is always a remedy available with the developer as well as with the government to make the best out of it. The company must go on, that is really relevant as it not only meets the expectations of home buyers, but also a way to generate employment and funds.

In terms of Trunk Infrastructure, it should not happen that the building is ready and the infrastructure is not, which is why the State Governments. are taking time, as once an MOA is signed, they get tied legally, and if rents are not enough, there is also a sale component of 10% for the commercial area. When you decide the rent, it is also in consonance with the urban local bodies but then you can also raise the initial rent by 8% every 2 years.

Also, you would be able to monetize eg., a large piece of land, you can make something apart from that which may not be funded by tech. innovation grant but you can of course cross monetize it. In case of force majeure, the 18 months' time limit does not apply to every project, it only applies for TIG. In terms of central schemes being better, you can of course merge it with the state schemes and work simultaneously whereby trunk infrastructure will be provided.

With regard to the Trunk Infrastructure, a provision can be made where the State Government is able to deal with it on project to project basis. The only issue with regard to this is that Trunk Infrastructure can only be provided on governments own land. In some states which have a township policy where the affordable rental housing complex land up within the township, already given out to a developer, therefore in those cases, it stands as an exception to state policy.

Initial affordable rent for the ARHC?

Initial affordable rent for the ARHC will be fixed by the entity as per local survey. So, it always depends on the entity. It will be fixed by the entity i.e. the private or the public entity making it on the basis of a local survey and it can be revised from time to time.

Hence, a rent does not mean it will be always fixed by an urban local body, it will be on a local survey but the entity would be fixed.

TAKEAWAYS

Conclusion

Governments need to provide necessary legislative support alongwith NCLTs working on sustainability driven approaches to make Real Estate a viable sector and to ensure the the poor get the benefits of the affordable rental housing complexes and Pradhan mantri Awas Yojna ..

The milestones of the affordable rental housing complex scheme can only be met with a surviving and thriving real estate sector which can partner the implementation of the scheme upto the last mile. This cannot happen without the support of the NCLTs and state governments to keep survival and sustainability of the real estate sector at the center of their focus.

Click below to watch the KWS session

<https://www.youtube.com/watch?v=edjWx7l4yM8>



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Real Estate Sector, IBC & the Affordable Rental Housing Complexes Scheme

The potential avalanche of project delays post Covid19, navigating IBC & Affordable Housing targets for the Real Estate Sector

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Click below to listen to KWS session Podcast

<https://anchor.fm/hammurabi-solomon>



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PODCAST

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We have always aimed at being the change-maker for a newer India and the world around us. With our portfolio of services - law, public policy, regulation and justice converge to enable solutions to our client needs within the legal framework to operate in India with ease and predictability.

Our main aim is to provide world-class legal services with a unique client-centric approach. We aim at providing the utmost quality and result-oriented solutions with our out of the box thinking and teamwork. We focus on being very approachable and highly reliable legal advice with a practical and relevant approach, we tailor solutions with each client's needs.

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HEAD OFFICE

405A & 405B, Rectangle One - 4th Floor
Saket District Centre, Saket
New Delhi - 110017

Visit us at
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