

INVESTMENT IN PROPERTY – REAL ESTATE OR COLLECTIVE INVESTMENT SCHEME UNDER SEBI?

An individual's achievement is often linked to owning a Home or a piece of land or building and the Society is accustomed to judging a person's success in terms of investment in Real Estate. Real Estate is the common form of security that people look for since it's the only mode of investment easily accessible to all income groups. The term "Real Estate" itself indicates physical/ actual properties which includes both developed or undeveloped lands, houses, condominiums, commercial spaces, farm plots, etc. The most essential feature of a real estate transaction is that which is clearly distinguishable immovable property say, a flat or plot which is identifiable by its description, etc.¹ Every individual's prospect today is to derive profit proportionately which leads to investment in Collective Investment Schemes (CIS) but what is projected as Real Estate by certain Companies. The prime question is whether such schemes are regulated and require registration under the law?

Securities & Exchange Board of India (SEBI) is the regulator for the securities market in India. SEBI was established on April 12, 1992 in accordance with the provisions of the Securities and Exchange Board of India Act, 1992 (SEBI Act). The Preamble of SEBI describes its basic functions as "...to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected therewith or incidental thereto". CIS is defined under Section 11AA of SEBI Act which was inserted by the SEBI (amendment) Act, 1999 w.e.f 22nd February 2000 and the Section has been amended periodically.



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¹ Order dated 31st Mar 2015 passed by SEBI in the matter of Richa Infra Developers India Ltd.

“Collective investment scheme.

11AA.(1) Any scheme or arrangement which satisfies the conditions referred to in sub-section (2) or sub-section (2A) shall be a collective investment scheme:

Provided that any pooling of funds under any scheme or arrangement, which is not registered with the Board or is not covered under sub-section (3), involving a corpus amount of one hundred crore rupees or more shall be deemed to be a collective investment scheme.

(2) Any scheme or arrangement made or offered by any person under which,—

(i) the contributions, or payments made by the investors, by whatever name called, are pooled and utilized for the purposes of the scheme or arrangement;

(ii) the contributions or payments are made to such scheme or arrangement by the investors with a view to receive profits, income, produce or property, whether movable or immovable, from such scheme or arrangement;

(iii) the property, contribution or investment forming part of scheme or arrangement, whether identifiable or not, is managed on behalf of the investors;

(iv) the investors do not have day-to-day control over the management and operation of the scheme or arrangement.

(2A) Any scheme or arrangement made or offered by any person satisfying the conditions as may be specified in accordance with the regulations made under this Act.

(3) Notwithstanding anything contained in sub-section (2) or sub-section (2A) any scheme or arrangement—

(i) made or offered by a co-operative society registered under the Co-operative Societies Act, 1912 (2 of 1912) or a society being a society registered or deemed to be registered under any law relating to co-operative societies for the time being in force in any State;

(ii) under which deposits are accepted by non-banking financial companies as defined in clause (f) of section 45-I of the Reserve Bank of India Act, 1934 (2 of 1934);

(iii) being a contract of insurance to which the Insurance Act, 1938 (4 of 1938), applies;

(iv) providing for any Scheme, Pension Scheme or the Insurance Scheme framed under the Employees Provident Fund and Miscellaneous Provisions Act, 1952 (19 of 1952);”

In short, CIS is any scheme or arrangement, which satisfies the conditions, referred to in sub-section (2) of section 11AA of the SEBI Act. Any scheme or arrangement made or offered by any person or entities under which the contributions, or payments made by the investors, are pooled and utilised with a view to receive profits, income, produce or property, and is managed on behalf of the investors where investors do not have day to day control over the management and operation of such scheme or arrangement is a CIS. A typical commercial Real Estate Scheme does not fall under CIS if there is no pooling of funds

involved offering any assured returns². The words used in sub-section (1) of section 11AA are that the scheme or arrangement should satisfy the conditions referred, means all the 4 conditions should be satisfied, then only scheme of the company can be said to be covered within the definition of CIS.³ The proviso of sub-section 1 to Section 11AA was amended by the SEBI (Amendment) Act 1999, w.r.e.f. 18-07-2013 which provides that pooling of funds under any scheme involving a corpus amount of One Hundred Crores or more shall deemed to be a CIS even though it does not satisfy all the four conditions under sub-section (1) of section 11AA. In the past decade, companies engaged in Real Estate business or other fund raising activities under the pretext of infrastructure projects have been the nucleus of SEBI in view of the new strategies adopted by them to attract investors to meet the everlasting financial crunches. Offering returns either in cash or kind is the most convenient way of attracting gullible investors coupled with interest in Real estate often comes under axe of SEBI which is vested with several powers including closure of such schemes, imposing penalty, reference to the Government for initiation of civil/criminal proceedings against the Directors of the Company, reference to the Ministry of Corporate Affairs, to initiate the process of winding up of the company, attachment and recovery proceedings under the SEBI Act and rules and regulations framed thereunder, etc. A typical example of CIS under the pretext of Real Estate is the infamous case of P.G.F Limited⁴ wherein, the Apex Court held that sale and development of lands in certain units along with the offer to develop the same by planting trees, plants, etc., and thereby assuring the customers of a high amount of appreciation in land value, which is nothing but a return to be acquired by the customers after making the purchase of land based on the development assured by P.G.F Ltd. falls within the definition of CIS.

Section 12(1B) of the SEBI Act, states that "*no person shall sponsor or cause to be sponsored or carry on or caused to be carried on a 'collective investment scheme' unless he obtains a certificate of registration from the Board in accordance with the regulations*". Regulation 3 of the SEBI (CIS) Regulations, 1999 ("CIS Regulations") also prohibits carrying on CIS activities without obtaining registration from SEBI. Therefore, the launching/ floating/ sponsoring/causing to sponsor any 'CIS' by any 'person' without obtaining the certificate of registration in terms of the provisions of the CIS Regulations is in contravention of Section 12(1B) of the SEBI Act and regulation 3 of the CIS Regulations.

² Order dated 03rd June 2014 passed by SEBI in the matter of Puravankara Projects.

³ PACL India Ltd. Vs. Union of India [2004]49 SCL 250 (Raj); MANU/RH/0281/2003

⁴ P.G.F Ltd. & Ors. Vs. Union of India & Ors. AIR 2013 SC 3702; MANU/SC/0247/2013

Our recently got a favourable order for our client before SEBI Mumbai, in a matter pertaining to CIS. SEBI had restrained our client from carrying out its business activities alleging that it is into fund mobilising activity which is in the nature of CIS as defined in Sec.11AA of SEBI Act. Upholding our contention that our client was into the business of real estate i.e., purely into selling of plots & in order to come under CIS, all the conditions stipulated under Sec.11AA(2) has to be met SEBI has declared that our client does not come under CIS and is purely into real estate. Hence, while floating new Projects and developing new business idea, the entities into Real Estate Sector have to examine the law and at the same time, even the public has to be cautious before getting carried away by easy instalment schemes to buy plots of land coupled with assurance of high returns through developing the plots by the companies/ developers.

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