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Foreign entities acquiring real estate in India

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Every non-Indian entity (foreign entity) setting up operations inevitably becomes involved in the acquisition of real estate whether by lease, license, or sale. While Japanese entrepreneurs have long been doing business in India, their interest in real estate varies from commercial to industrial land and across varied sectors.

This article analyzes the basic guidelines for the acquisition of real estate by foreign entities, under the following broad headings: a) Foreign direct investment (FDI) policy read with the Foreign Exchange Management Act, 1999; b) central (federal) laws, and c) state and local laws.

A foreign entity usually establishes its presence as a liaison office, branch office, a subsidiary under the Companies Act, 2013 or as a limited liability partnership, and is allowed to acquire real estate, except agricultural land, for its business purposes. In Japan there are no restrictions on foreign entities acquiring land but in India a foreign entity is prohibited from engaging in real estate business. Real estate business means dealing in land and immoveable property with a view to earning profit but does not include development of townships, real estate investment trusts (REIT) registered and regulated under the Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2014, construction of residential and commercial premises, roads and bridges, educational institutions, recreational facilities, and city and regional level infrastructure. Earnings from rent or income from leases of property not amounting to transfer are not deemed to be real estate business.

The acquisition of real estate is similar to that in Japan, which includes:

Engaging a real estate broker. It is advisable to engage a real estate broker to help the company identify a property suitable for its requirements. A broker is paid on successful closure of the transaction.

Drafting and negotiating the initial letter of intent (LOI). This is the initial document establishing the basic framework and the commercial terms agreed between the parties. The LOI is a non-binding agreement and no consideration or advance is paid. However, in a number of cities in India market practice is for payment of a token amount on the execution of the LOI, thereby making it a binding agreement. It is advisable that the LOI should be executed by the Indian entity.

Conducting due diligence with respect to the property. Prior to acquiring a property on leasehold or by purchase, detailed due diligence must be conducted with respect to the property to investigate title, usage, structure, encumbrances and outstanding litigation. One difficulty is the absence of centralized records, necessitating physical inspection at various offices and local courts. Documentation is generally similar, but each property has its own peculiarities based on its location. It is advisable to consult an attorney with expertise in the area.

Negotiating and executing the lease or sale agreement. If there are preliminary conditions to be completed a company will usually enter into an agreement to lease or sell before executing the main agreement. However, such an agreement is not mandatory. A detailed agreement to lease or sell forms the basis of the final transaction documentation. Careful negotiations at this stage ensure the successful execution of such documentation. In some states an agreement to sell may attract substantial stamp duty, a form of tax paid to the government and which varies in different states. Some states require that the agreement to sell be registered with the relevant Registrar of Assurances under the Registration Act, 1908.

Execution of deed of lease or conveyance. After completion of the conditions precedent in the lease or sale agreement, the parties execute the final agreement as the deed of lease or conveyance. Where there is no lease or sale agreement the parties can directly execute the deed of lease or conveyance.

Stamping and registration. After execution the deed of lease or conveyance is submitted to the relevant Registrar of Assurances for registration. Stamp duty is a form of a tax levied by the Government, and varies from state to state. A compulsorily registrable document, if not registered, confers no rights and cannot be produced as evidence to prove the transfer of immovable property or any of its terms in the event of a dispute.

As in Japanese law, land and buildings are separate and distinct real property, and separate registration is permitted. While some states have online registration, the majority rely on records maintained in physical registration books. India is a diverse country with varied real estate laws that differ from state to state. Accordingly, it is always advisable to enlist the assistance of a real estate attorney with appropriate expertise.

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