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2021: A New Era for Rental Real Estate in India

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INTRODUCTION

In the context of housing policies in India, the need for a uniform rental housing law in the country was felt despite some states already having different versions of the Rent Control Act. On the one hand, there was no unified policy framework for rental housing; on the other, 11.09¹ million houses in urban India remained vacant despite a massive housing shortage. Over the years, there has also been a decline in the supply of formal rental housing and an increase in informal housing arrangements. While the central Rent Control Act was first passed in 1948 and adopted by different states thereafter, it was later amended or repealed in some states. However, there are many states where the Rent Control Act continues to be in force with some amendments. The Rent Control Act has disincentivized rental housing to a great extent. With maturity of the real estate sector over decades, the provisions became obsolete as home occupancy needs evolved as a result of urbanisation.

The Union Cabinet's move in June 2021 to approve the Model Tenancy Act, 2021², signals the creation of an organised rental housing marketplace and will act as a catalyst to augur the rental housing supply in India benefiting the urban middle class, working professionals, students and the floating population. The Model Tenancy Act, 2021 will be adapted by all States and Union Territories (UT) by either amending existing rental laws or enacting a new legislation. Once implemented, this policy adaptation will provide for market conditions to support private players and investor participation in rental housing as a business model - a step which will bring market forces into play where supply and demand will be the determinant of 'rent' as a term of tenancy.

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¹Census of India, 2011

²Model Tenancy Act, 2021 or "The Act" or "this Act" on all subsequent pages mean the same for the purpose of analysis in this report.

NEED FOR RENTAL HOUSING REGULATIONS IN INDIA

01

A HUGE MARKET OPPORTUNITY -

Urban India has 21.72 million rented households. Comprising the highest percentage share of rented households are eight states and Union Territories with 16.63 million³ or 76.5% of the total urban rented households.

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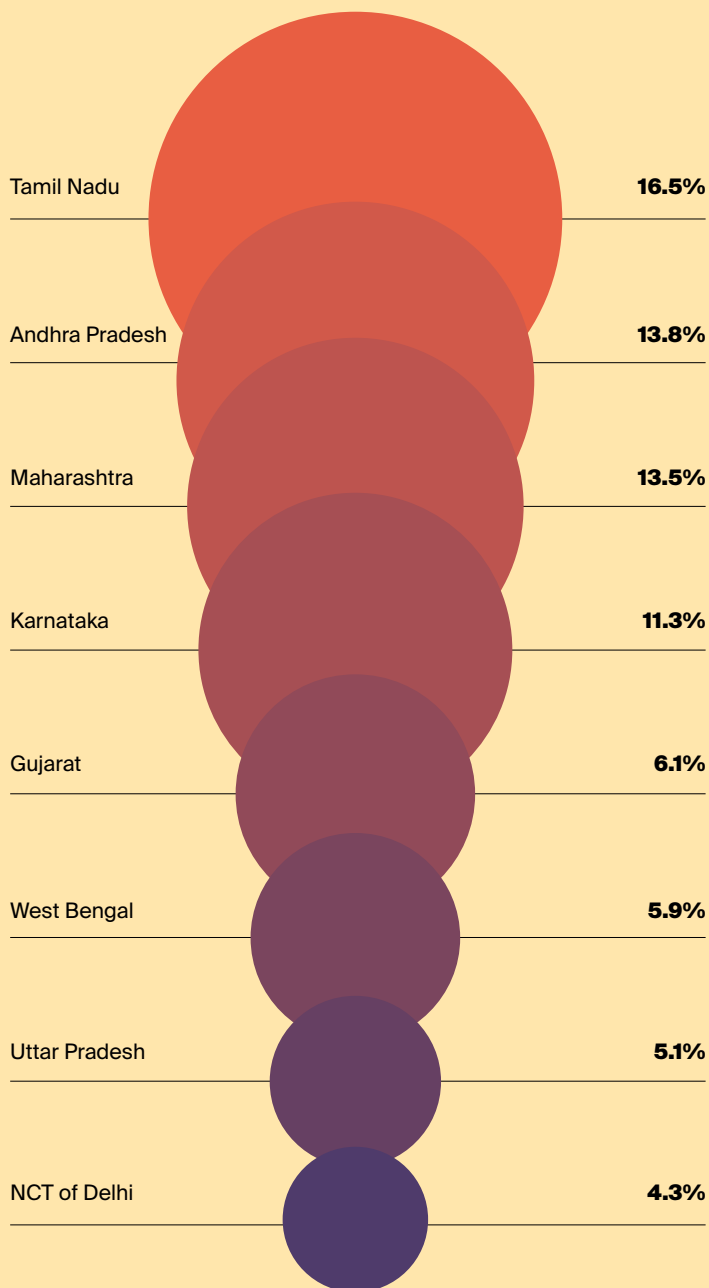
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TABLE 1:

STATES WITH THE HIGHEST PERCENTAGE SHARE OF RENTED HOUSEHOLDS IN INDIA*



Source: Knight Frank Research, Census 2011

³ Census of India, 2011

*percentage share of region in the total rented households in India

The statistics for rented households in major Indian cities may be much more now compared to the Census 2011 data. However, the fact that the states of Tamil Nadu, Andhra Pradesh, Maharashtra, Karnataka, Gujarat, West Bengal, Uttar Pradesh and the National Capital Territory (NCT) of Delhi command a hefty percentage share of the total rented households in urban India is largely attributed to key urban employment hubs in the cities of Chennai, Hyderabad, Mumbai, Pune, Bengaluru, Ahmedabad, Kolkata and the National Capital Region (NCR). The fact that most of the population lives in informal rented housing accommodation in these cities provides a huge opportunity for private housing operators and institutional participation in the organized rental housing market. It was due to the lack of policy push that housing projects solely for rental purposes were not a focus area for market participants. Once the Act is implemented across the length and breadth of the country, India may well be ready for the introduction of rental housing models such as Build-To-Rent and Rent-to-Own which are widely prevalent in residential markets globally.

02

VACANT HOUSING STOCK

Vacant houses as a percentage of total residential census houses in key Indian cities remains very high. While Gurugram has 25.8% of such inventory, Pune comes a close second at 21.7%, followed by Greater Mumbai at 15.3%⁴. In Delhi, Bengaluru, Ahmedabad and Ghaziabad, this percentage is between 11-15%. Once the rental housing regulations are implemented in letter and spirit by the states, this vacant inventory can be brought within the fold of formal rental housing as it would make it easier for all stakeholders – tenants and landlords to bridge the trust deficit and unlock the true potential of this housing stock.

03

HOME OWNERSHIP FOCUS OF GOVERNMENT POLICIES

Despite a huge population of 1.39 billion Indians, sky rocketing prices of residential realty in prime Indian cities and ever-expanding urban agglomerations, rental housing never took centerstage in the housing policy framework. Our current policy framework, with the focus of ‘Housing for All by 2022’, and the most recent addition of The Real Estate (Regulation and Development) Act, 2016 are skewed in favor of providing, promoting and regulating homebuying. There have been several impediments due to which rental housing regulations did not take shape in India in the past. Consequently, demand for need-based rental housing and market driven rental housing remained unmet as the policy enabler was lacking until now.

04

DISPUTE RESOLUTION MECHANISM FOR LANDLORDS AND TENANTS

The landlord-tenant relationship in India has been tainted due to trust issues. Despite tenancy and rent-related laws in Indian states, conflicts have been unavoidable. Each state has identified certain grounds for legal eviction of tenants by landlords, but in cities where it is difficult to find a rental home, violation of tenancy laws is commonplace. The tenancy laws in India are popularly perceived as ‘pro-tenant’ which is a big concern. In the absence of a regulatory framework to demarcate the rights and obligations of both parties, there have been long-drawn legal battles. Absence of regulation has been one of the biggest deterrents for landlords to give their properties on rent in the first place. With the Model Tenancy Act, 2021 coming into effect, the rental marketplace may not remain unattractive for property owners.

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⁴Knight Frank Research, Census 2011

SORE SPOTS FOR LANDLORDS

Fear of continuing possession illegally by tenants

Frequent demands of tenants with respect to structural maintenance

Upkeep of the premises along with common areas of access

Risk of long-drawn legal battle

SORE SPOTS FOR TENANTS

Fear of untimely eviction

Absence of a dedicated unified authority for grievance redressal

No control over security deposit demands

Disputes with respect to property maintenance

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KEY FEATURES OF THE MODEL TENANCY ACT, 2021

The Model Tenancy Act, 2021 aims to balance the scales for both landlords and tenants, so that perceptions about rent control laws favoring tenants can go away and a transparent and speedy regulatory environment can be created for resolution of disputes between both parties. Most of the sore spots that tenants and landlords experience in the process and tenure of tenancy, and the redressal mechanism in case of disputes have been outlined in the Model Tenancy Act, 2021. Some of the salient features of the Act are:

01

CREATION OF A THREE-TIER REDRESSAL STRUCTURE

This is envisaged as comprising Rent Authorities, Rent Courts and Rent Tribunals, the powers vested in them and selection criteria for personnel to be employed. This is a much-needed regulatory structure which will reduce the case burden on civil courts by diverting all tenancy related matters to these said authorities. The Rent Courts or the Rent Tribunals (as the case may be), will endeavor to dispose of cases expeditiously, and within 60 days from the date of receipt of the application or appeal. This will help in speedy dispute resolution.

03

RIGHTS AND OBLIGATIONS OF LANDLORDS AND TENANTS

The Act defines the do's and don'ts for each party and covers aspects such as retention of original tenancy agreements, rents and other charges payable, repair and maintenance of the property, entry into premises, besides information and duties of a property manager and consequences of violation of necessary duties, so that the routine aspects of managing tenancies can be clearly outlined and the need for litigation is reduced.

02

SECURITY DEPOSIT DEMANDS CAPPED

The Act puts a lid on the security deposit to be paid by a tenant in advance to - a) not exceed two months' rent in case of residential premises, and b) not exceed six months' rent in case of non-residential premises. While this will help improve dispute resolution, capping it by number of months' rent equivalent takes away the freedom of contracting. It would have been better if the Act left it to the discretion of parties involved to decide by way of mutual understanding. The upward or downward revision in security deposit needs to be looked into. The aspect of top-up or replenishment of the security deposit in case of adjustment by landlord for non-payment of rent by the tenant needs to be clarified by the law.

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EVICTION OF TENANT AND RECOVERY OF POSSESSION OF PREMISES BY THE LANDLORD

In the past, Rent Control Acts in different states such as the Delhi Rent Control Act, the Karnataka Rent Control Act and the Maharashtra Rent Control Act provided similar grounds for evicting a tenant and terminating tenancies which was highly disputed in the court of law. This often led to protracted litigation. By limiting the grounds for eviction and termination of tenancies, this Act seeks to bring a consistent approach towards addressing these issues at the ground level.

05

ROLE OF PROPERTY MANAGERS

The Act provides for the definition of property managers, their duties and consequences of violation. At the same time, it fixes accountability for property managers and they will be required to furnish details such as name, address, PAN number, Aadhar number and contact information for submission to Rent Authorities. Any individual or a legal entity including rental agent who acts on behalf of the landlord to manage the premises and who represents him in dealings with the tenant will be included here. This Act will provide more opportunities for property managers going forward, especially in the residential sector.

However, there are a few areas of concern which can create challenges in the implementation of the Model Tenancy Act, 2021:

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01

DEFINITIONS OF “LANDLORD” AND “TENANT”

The definitions of “landlord” and “tenant” in the Act are ambiguous and it is not clear if the Act is applicable to cover leases v/s licenses v/s tenancy. It falls under a grey area and more clarity on these definitions is required.

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MEANING OF “PREMISES”

As per the Act, “premises” means any building or part of a building, which is or is intended to be, let on rent for the purpose of residential or commercial use - except for hotel, lodging house, dharamshala and for industrial use with a few exceptions. States where the Rent Control Act is in place and where urban dwellings like slums/chawls were previously covered, may have to define it clearly under their state level laws to provide protection to both tenants and landlords.

02

FORCE MAJEURE

This Act defines “force majeure” as a situation of war, flood, drought, fire, cyclone, earthquake or any other calamity caused by nature affecting the habitation of the tenant in the premises let out on rent. Its focus is more on habitability. Since the Act deals with both commercial and residential, it would be better to address both types of transactions under the force majeure clause. Merely stating what would constitute Force Majeure and linking the same with habitability only may not help the stakeholders. For residential, perhaps the intent should be more focused on a tenant not being left stranded in case the tenancy comes to an end during a pandemic like situation. For commercial transactions, the events that constitute “force majeure” and the party on whom the burden and extent of risk would vest in case of the “force majeure” event, it would be best left to market dynamics.

04

NON-APPLICABILITY FOR CERTAIN TYPE OF PREMISES

Many properties - such as premises owned by the central government, state government, Union Territory administration; local authority or government enterprises, statutory body or cantonment board; premises owned by a company or premises owned by certain religious or charitable institutions - will not come within the purview of this Act. This will keep a large inventory of leasable premises out of the regulatory framework and tenants renting these will still have to rely on other legal recourse available for dispute resolution.

06

OTHERS

Identification and appointment of personnel for Rent Authority, Rent Courts and Rent Tribunals is a time intensive process and it will take additional and varied time period for the on-ground implementation of The Model Tenancy Act, 2021 by all states and UTs across the country. Since it is a state subject, for states where old Rent laws are to be repealed or amended, it may take even longer. There may be a few states which may not implement the Act at all.

05

DIGITAL PLATFORM CREATION BY THE RENT AUTHORITY

In a digital age, availability of information on real time basis is a well-established tenet of informed decision making. A robust digital infrastructure will need to be put in place so that document submission, creation of unique identification numbers and uploading details of tenancy agreements becomes hassle free for users. Delay in setting up of Rent Authorities or inadequate availability of resources at the ground level can pose challenges on this front. A national level uniform database which can be managed locally by states and UTs can be a simpler and holistic way to go about sourcing and storage of tenancy related information. This database can also be enhanced to include information about how many times a property has been let out by a landlord, how many tenancies have been taken up by a tenant in the past, and history of disputes raised with Rent Authorities, Rent Courts and Rent Tribunals and put in public domain. This can be utilized as a quality indicator tool by interested parties before entering into tenancy agreements in future. A rating mechanism reviewing both the parties can be developed on the basis of history of discharge/non discharge of duties and matters related to eviction and recovery of possession.

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With the objective of creating a regulatory eco system to govern landlord-tenant relationships, this Act has finally put down ground rules of tenancy in black and white. The Model Tenancy Act, 2021 approved by the Union Cabinet is similar to the earlier draft⁵ notified in 2019. However, it is the efficacy with which it is implemented across states and Union Territories that will go a long way in determining the way this Act is practiced and evolves over a period of time.

From a residential real estate standpoint, the enactment of the Model Tenancy Act, 2021 also raises a question about protected tenancies in India. Since there are a few states, such as Maharashtra and West Bengal, where a huge population lives in rented accommodation under the protection of the state level Rent Control laws, it remains to be seen if the Model Tenancy Act, 2021 is even implemented in the first place. Also, if it is implemented, whether it will be with retrospective effect.

In the case of commercial real estate transactions, depending on the transaction suitability, either of leasing or licensing framework is being adopted by market participants at present. However, given the dedicated adjudication machinery and likelihood of speedy grievance redressal, we expect a shift of new transactions from the licensing framework to this newly introduced law, provided freedom to contract is not curtailed by having provisions like force majeure and security deposit as it presently stands.

From learnings of the past, RERA implementation has been impactful to bring order to the outright sale market and most states and UTs have already adopted it in letter and spirit. New learnings from the developer-homebuyer disputes in RERA Courts across the country is paving the way for effective resolution of real estate sector disputes.

The Model Tenancy Act, 2021 will also go a long way in the history of Indian real estate – both commercial and residential - to create an effective rental marketplace in the foreseeable future. Additionally, as the rental housing market gets formalized, more players will enter this previously uncharted territory to provide the monetary wherewithal and execution expertise in real estate to create contemporary rental housing stock and herald a new era in this untouched part of the sector.



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