Indo-Singapore treaty to affect manufacturing cos

SUGATA GHOSH & K YATISH RAJAWAT

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MUMBAI: The imminent Indo-Singapore treaty has turned on the heat on tax haven Mauritius, and to some extent Cyprus. FIIs may now route their funds via Singapore, which has emerged as an Asian business hub.

"If the treaty goes through, Mauritius would definitely take a back seat, because Singapore is already a hub for several MNCs," said Punit Shah, partner, RSM & Co, which is a firm providing taxation, business advisory and other services. A possible shif would be bad news for Mauritius, where a sizeable part of the economy has grown around offshore banks handling foreign money.

Already, the FII fund managers and research desk for Asia Pacific markets work out of Singapore, with Mauritius being largely a post-box operation for funds. One of the fringe benefits of shifting to Singapore is that foreign funds can also raise capital as a local entity.

"Entities that were investing in Indian debt out of Cyprus may also shift to Singapore. Just as Mauritius attracts foreign funds investing in equity, Cyprus has been attractive for debt market investment. Cyprus has particularly low taxation on interest payments received, making it attractive under the double taxation avoidance treaty," said a lawyer with Nishith Desai Associates.

Singapore offers tax incentives to foreign firms and even their fund managers for investments outside Singapore, provided the foreign equity in such firms is at least 80%. FII routing funds through Singapore will have to thrash out the contentious issue of "business income" vis-à-vis "capital gains", since business income of an FII could be subjected to tax in Singapore. Similarly, business income would not also be taxed in India, unless the Singapore resident entity substantiates that it does not have a permanent establishment in India.

Legal circles think the treaty would have strict clauses to avoid "treaty shopping" by MNC firms, thanks to pressure from the US. The "limitation of benefit" rules in Singapore relates to less benefit to firms that do not remit the money made in other markets to Singapore. While the final picture is yet to emerge, this could primarily affect manufacturing companies, which run bank accounts in other countries to park money for funding operations.