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Why Singapore? Why Business Trust?

Burdened by substantial debt reliance communications has for some time now wanted to unlock value in its undersea cable business flag telecom. For a variety of reasons, Flag could not make a vanilla global equity listing. Now it's decided to go public in Singapore via a trust structure. Why Singapore? Why Trust? Payaswini Upadhyay goes in search of some answers.

In 2007, Ascendas India Trust went public as Singapore's first listed business trust holding Indian IT park assets

In 2008, Indiabulls Properties Investment Trust listed on the Singapore stock exchange with commercial property in Mumbai as the underlying asset

Just 2 months ago, Fortis group owned Religare Healthcare Trust received an 'eligibility to list' approval from the Singapore stock exchange

And this month, Reliance Communications owned Global Telecommunications Infrastructure Trust filed an initial prospectus with the Monetary Authority of Singapore to list its undersea cable business.

- all sign of the growing popularity of this route. Before we get to the why, here's the how. In a typical business trust structure, the Indian company creates or uses an overseas subsidiary as a sponsor. The sponsor incorporates a Singapore based company as trustee manager. The trustee manager owns and manages the assets, the economic interest of which is sold via units of the trust, also established in Singapore. The units are listed on the Singapore stock exchange.

Evelyn Wee
Partner, Rajah & Tann
"It is essentially a hybrid structure that has the elements both of a trust and a company. Like a company, a business trust is established to run a business. However, it is not a separate legal entity. It is actually constituted by a trust deed. Under the trust deed, the trustee manager, which is the single responsible entity for the business trust, has the legal ownership of the assets of the trust and also manages the assets of the trust for beneficiaries of the trust."

Yash Asher
Partner, Amarchand Mangaldas
"If a company has a plan of total of 8 assets- say 8 ships- 2 ships, it already has and those are generating revenues; 6 ships have been ordered but not yet been delivered. It would be tax inefficient to move two ships to another company in India and try to list a company with just two ships. But there are investors who are willing to invest and hold these two ships which are generating regular income. And remember there is no assurance that a company which has two ships will give you return- it finally depends on the dividend policies and the growth policies of the company. But the business trust, by definition, tries to return money to the investors. In this environment, investors want to ensure that their capital grows; they don't want to depend upon the fluctuations of the market. The business trust gives them that sort of comfort. So Business trust is able to buy out these assets as compared to a company whose shares will have to be listed and there is no guarantee of return."

That by far is the biggest attraction a trust holds- that it can offer fixed returns.

Rahul Guptan
Partner, Clifford Chance, Asia
"For a company to declare a dividend, the typical test is where you have an accounting profit. So you could have a very lucrative cash-generating asset like a ship but you can't declare dividends to your equity shareholders because of the accounting rules and the Companies Act requirements that limit your ability to declare dividend because you don't have an accounting profit for different reason. Whereas, in the context of a business trust, to the extent you meet the Singapore's Business Trust Act's solvency test, you're able to declare dividend out of the cash flows that your assets are generating even though you may have an accounting loss at the end of the day."

For instance, Reliance communications owned GTI trust is offering unit holders a yield of between 9.5 to 11.5% in FY13 and 10.1 to 12.2% in FY 14. Besides fixed returns, investors are drawn by a higher degree of governance requirements in trusts.

Evelyn Wee
Partner, Rajah & Tann
"These are actually more stringent and set a higher standard of independence compared to companies that are listed on the exchange. These will include requirements that the majority of Directors must be independent from business and management relations of the trustee manager; that's one. Secondly, a majority of directors have to be independent from a substantial shareholder and finally that one-third of the Board needs to be independent from management and business relation of the trustee manger as well as every substantial shareholder of the trustee manager."

And the third thing going for the Singapore trust route is tax incentives.

Evelyn Wee
Partner, Rajah & Tann
"In terms of tax, Business trust is subject to income tax just like a company. So where there are

activities or businesses that are able to obtain tax incentives, these are useful businesses to put into a business trust because the tax savings can be significant. These tax incentives would include infrastructure as well as shipping enterprises tax incentives."

Rahul Guptan
Partner, Clifford Chance, Asia
"Investors who have a specific sector focus like infrastructure or real estate, investors who are long-term players in the market, private wealth investors who want to maximize the returns will look at this as fairly robust kind of instrument for long-term investment on capital."

On the India end, any overseas trust structure must first pass muster with RBI's overseas direct investment regulations. In fact that's why the need for an offshore company as sponsor because an Indian company cannot directly establish an offshore trust.

Pratibha Jain
Partner, Nishith Desai Associates
"There is a limitation of 400% of your net worth that you can invest in such an offshore subsidiary. And thirdly, because you're setting up an offshore subsidiary which then invests into the units of trust that would probably classify the sponsor as engaging in financial services. For a company engaging in financial services, there are further requirements that are laid down i.e. it needs to be an entity that is registered with a regulator in India, it needs to have taken prior approval for engaging in such activities, it is required to meet certain prudential norms with respect to capital adequacy etc."

Yash Asher
Partner, Amarchand Mangaldas
"In creating this entire structure, I think companies and Indian promoters need to be careful about ODI and round tripping issues. This may also depend upon where, finally, they want the structure to be. The additional issue is from the tax perspective. All these structures will need a detailed analysis of tax laws and how finally GAAR shapes up will also affect the future BT structures."

Its early days- both for Indian companies and the Singapore Business Trust market as currently only 9 such instruments are listed on the Singapore Stock Exchange. In 2007, Ascendas India raised $325 million from its business trust IPO. For Indiabulls, it was $193 million. Fortis and Reliance Communications are set to test the market soon- hoping to raise over $300 million and up to $1 billion respectively questions is, will investors be enthused?

Its early days yet for Singapore Trusts and may be not the right environment to experiment in because, ironically, right after we finished the story and just before we went on air, Reliance Communications announced that its putting its Singapore PO on hold awaiting more appropriate market conditions.