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**Structuring International Operations And Deals:
Tax Effective Structuring Of Investments In India:
Mauritius, Singapore, Cyprus, Dubai, Brazil, The USA And Malta**

**Doing Business in India:
Critical Legal Issues for U.S. Companies
Sponsored by the Practicing Law Institute**

New York, NY, February 14, 2007
PLI New York Center

San Francisco CA, March 7, 2007
PLI California Center



Mauritius – Investing in India Background

- Historically, Mauritius has been the preferred route for foreign investment into India. This is largely attributable to the favourable terms of the Mauritius – India Double Tax Treaty, which was signed in 1982 and entered into force in 1983.
- Mauritius is currently the largest foreign direct investor in India.
- The Treaty has had a turbulent history and various aspects have been challenged in the Indian courts since its introduction - these culminated in a ruling by the Indian Supreme Court in October 2003 upholding the validity of the treaty generally, and in particular, that a tax residency certificate issued by the Mauritian Tax Authorities, is sufficient proof of residence for an entity to qualify for benefits under the Treaty.



Mauritius – India Double Taxation Treaty General Features

- Dividend withholding tax – no longer chargeable (on payments from India)
- Interest withholding tax – 0%
- Royalty withholding tax – 15%
- Tax sparing provisions allow for tax paid in India to be set off against tax in Mauritius (if any).
- Capital Gains – gains arising on the disposal of moveable property in India are subject to tax in Mauritius. However, Mauritius does not charge capital gains tax so that gains can effectively be realised free of tax. Part of the attraction of the Treaty has been this treatment of capital gains. However recent changes in India eliminating the tax on long term capital gains (capital assets held for more than three years and one year for listed securities or mutual fund units) and reducing the tax on short term gains from 30% to 10%, has reduced the advantages of the treaty.



Mauritius - Taxation of Foreign Income

There are two categories of Mauritius companies used for foreign investment:

- *Category 1 Global Business Company ("GBC1")*
- *Category 2 Global Business Company ("GBC2")*

GBC1 companies may qualify for benefits under Double Tax Agreements where the company has been issued with a tax residency certificate. (ie the company has at least 2 local resident directors; holds meetings of the board of directors in Mauritius; maintains a registered business address and premises in Mauritius; hold shareholders meetings in Mauritius; has a bank account in Mauritius; and has a local company secretary and auditor.)



Mauritius - Taxation of Foreign Income (contd.)

- GBC1 resident companies are subject to tax in Mauritius at the rate of 15%. However there is a unilateral tax relief of 80% of the foreign income received, thereby reducing the effective tax rate to 3%.
- A generous system of deductions is available so that the effective tax rate may be further reduced to 0%.
- Old "Offshore Companies" registered before 30th June 1998 may elect to pay tax at a rate of between 0% and 35%.
- There is no capital gains tax in Mauritius.
- There are no withholding taxes on payments made from Mauritius.
- There are no exchange controls or other restrictions on foreign payments from Mauritius.

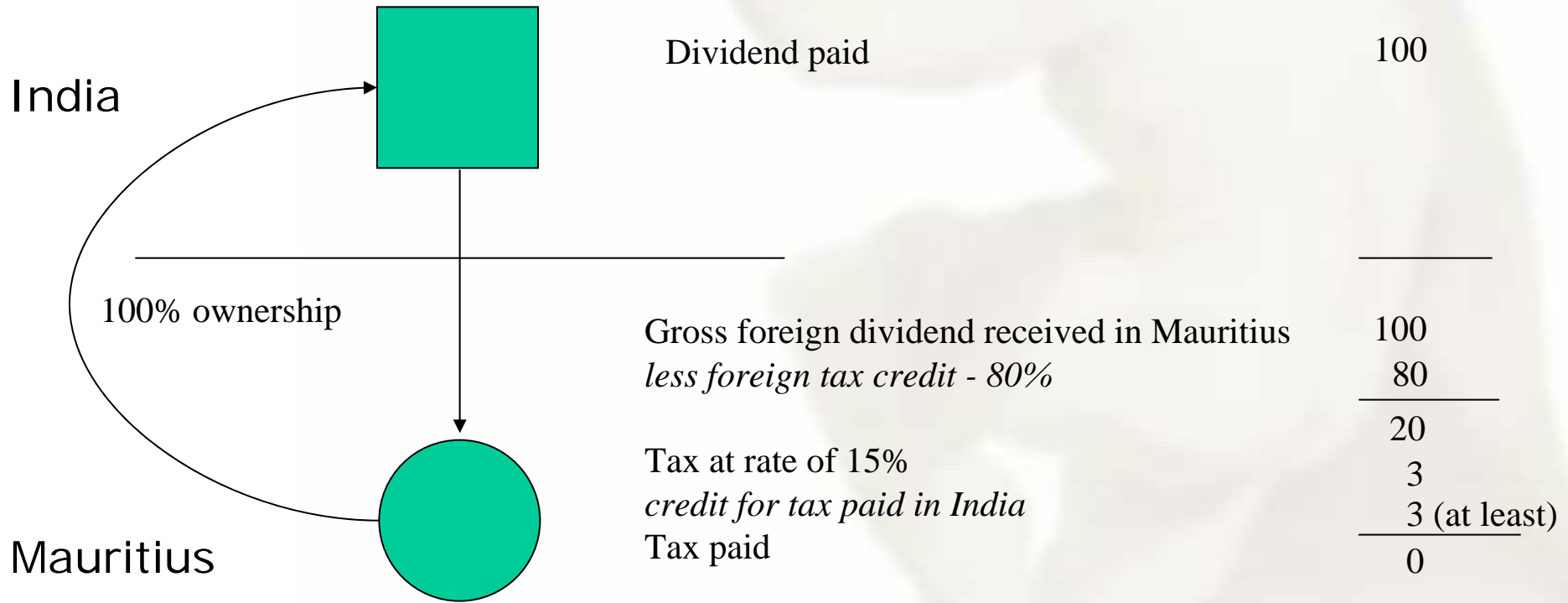


Mauritius - Taxation of Foreign Income (contd.)

- An outcome arising from the problems related to the Treaty, has been the increased use of “substance” structures in Mauritius. This in turn, gave rise to an anomaly that where substance services are provided in Mauritius, it may cause the foreign income to have a Mauritius source and therefore not qualify for the 80% deemed foreign tax credit deduction.
- The practice of the Mauritius tax authorities has been to allow the deemed tax credit on the whole of the income, even though the source may have been from Mauritius.
- This matter is currently under review and legislation and other practice notes will be implemented to give effect to the practice adopted by the tax authorities.



Simple Investment Structure - Mauritius





Singapore – Investing in India Background

- Singapore is one of the largest sources of Foreign Direct Investment in India and is the largest investor from the ASEAN region.
- The Singapore – India Double Tax Treaty was signed and entered into force in 1994 but has recently been amended as part of the negotiations of a comprehensive Economic Co-operation Agreement which began in 2003, where the Indian authorities indicated they see Singapore as a key to strengthening trading ties with its ASEAN trading partners.
- The amendments to the treaty are effective from 1st August 2004 and include reduced withholding rates on royalties and technical service fees as well as an exemption for capital gains.



Singapore – India Double Taxation Treaty

General Features

- Dividend withholding tax – no longer chargeable (on payments from India)
- Interest withholding tax – 15% unless the interest is paid on a loan granted by a bank or other similar bona fide financial institution.
- Royalty withholding tax – 10% on copyright and most other classes of royalties.
- Capital gains – gains on the disposal of moveable property in India are subject to tax in Singapore. However, Singapore does not generally charge capital gains tax so that those gains can effectively be realised free of tax. However, the amendments to the treaty do introduce “substance” requirements so that in order to qualify for the capital gains benefits under the treaty, the Singapore tax resident must either be listed in Singapore or have an annual operating expense in Singapore, in excess of S\$200,000.
- Tax sparing provisions allow for tax paid in India to be set off against tax in Singapore (if any).

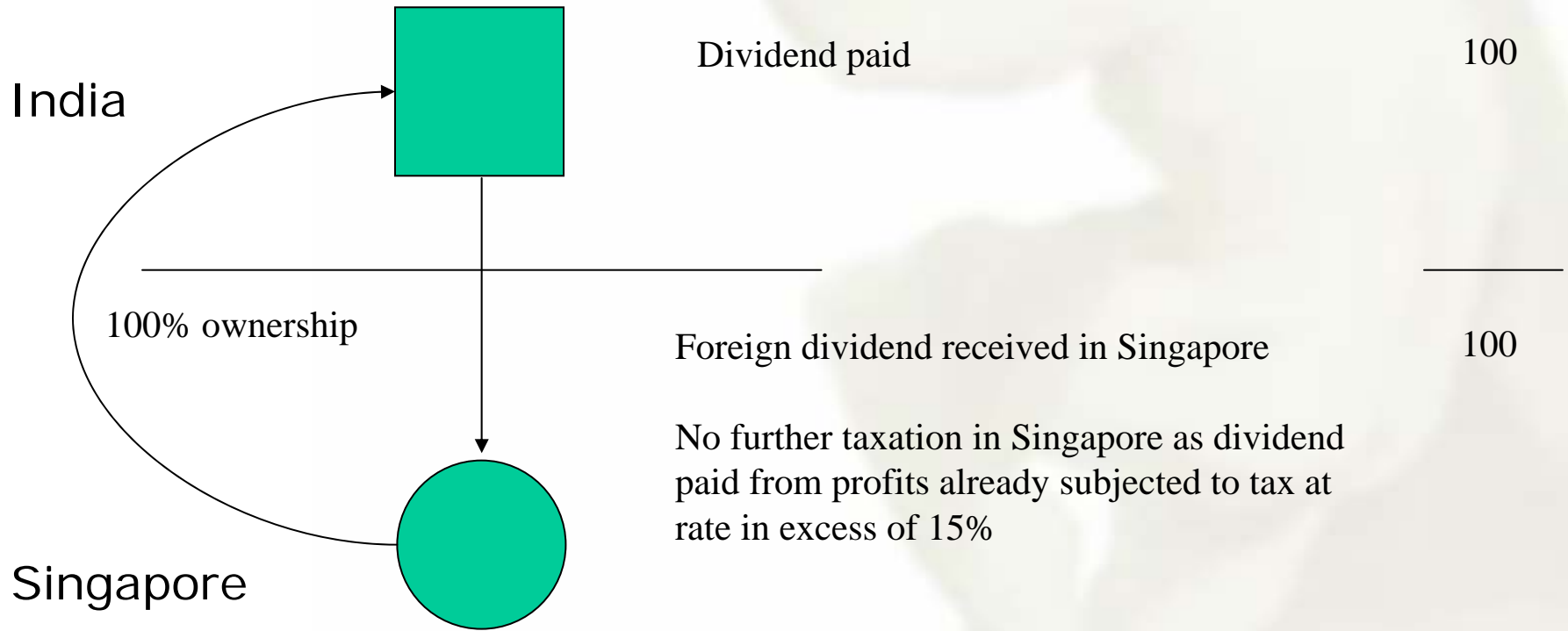


Singapore - Taxation of Foreign Income

- All Singapore companies are subject to tax on a territorial basis, so that generally, only income sourced or earned or remitted to Singapore is subject to tax.
- Income tax is levied at the rate of 20%.
- Foreign sourced dividends, branch profits and service income are exempt from tax in Singapore, provided they have been subject to foreign tax at a headline rate of at least 15%.
- There is no dividend withholding tax.
- Withholding tax payable on interest and royalties may be reduced under double tax treaty arrangements – Singapore has approximately 45 treaties.
- After tax profits can be retained outside Singapore without incurring any additional exposure to Singapore tax.



Simple Investment Structure - Singapore





Cyprus – Investing in India Background

- The tax treaty between Cyprus and India entered into force on December 12, 1994
- Today, Cyprus is becoming more popular as a jurisdiction for holding and finance structures for inbound investments into India
- Inter-governmental relationships are becoming stronger, with direct talks between government leaders focusing on improvement of trade relations. Recent discussions confirmed Cyprus as an important financial and trading jurisdiction with a commitment by the Cyprus officials that the incorporation of a Cyprus company for Indian investments, will take no longer than 5 working days (usually 10-15 working days)



Cyprus – India Double Taxation Treaty

General Features

- Dividends - no longer chargeable (on payments from India)
- Interest - 10% withholding tax
- Royalties – 15% withholding tax
- Tax sparing provisions allow for a credit so that tax paid in India may be set off against tax in Cyprus (if any).



Main features of the Cyprus tax regime

- Flat corporate income tax rate of 10 %
- Dividend income exemption (minimum conditions)
- No capital gains taxation
- No WHT on outbound dividends, interest and royalties
- No thin capitalization rules and minimum holding period
- EU and OECD approved
- Extensive tax treaty network, amongst others with India



Cyprus – India Structuring possibilities

- **Group finance structure**

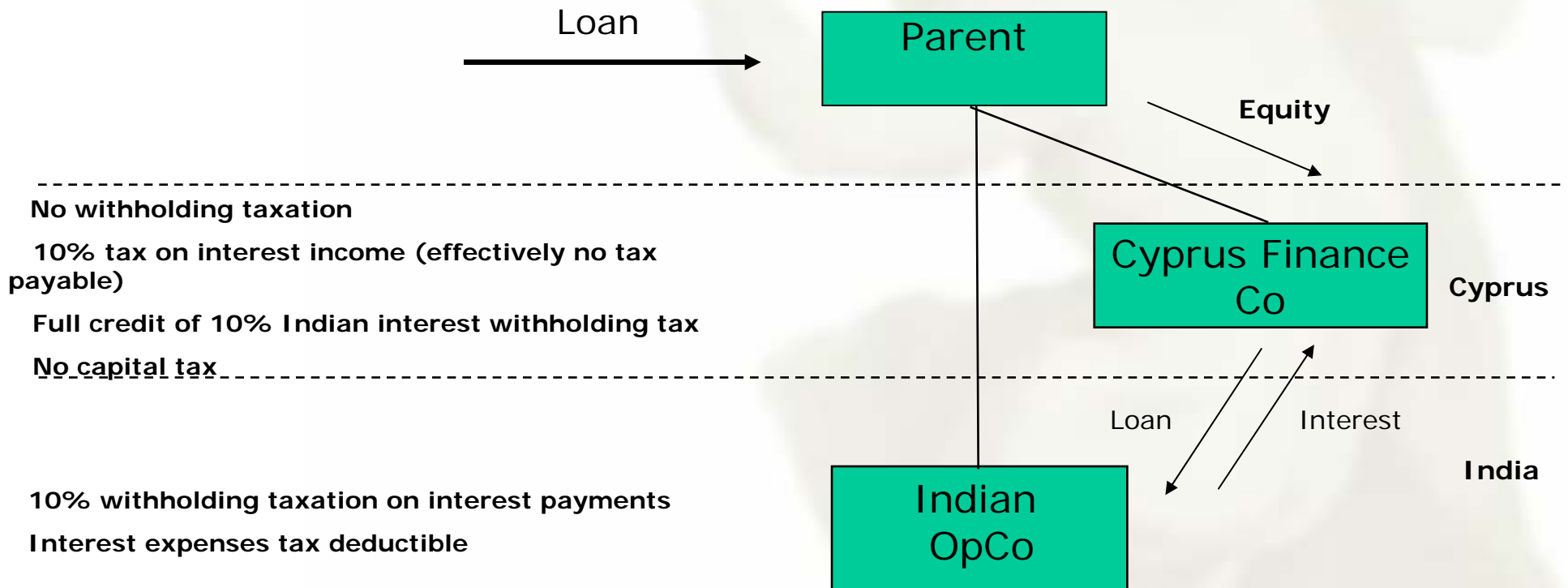
Cypriot company that is financed with equity, provides an Indian group company with a loan.

Characteristics:

- Interest deductible in India
- 10% Indian withholding on interest paid to Cyprus
- 10% Cyprus tax on interest income
- **But:** full tax credit on withholding tax paid
- Result: no tax due on Cyprus
- Cyprus company can distribute its profit without paying withholding tax to any country



Finance structure





Cyprus – India Structuring possibilities (contd.)

2. Permanent Establishment

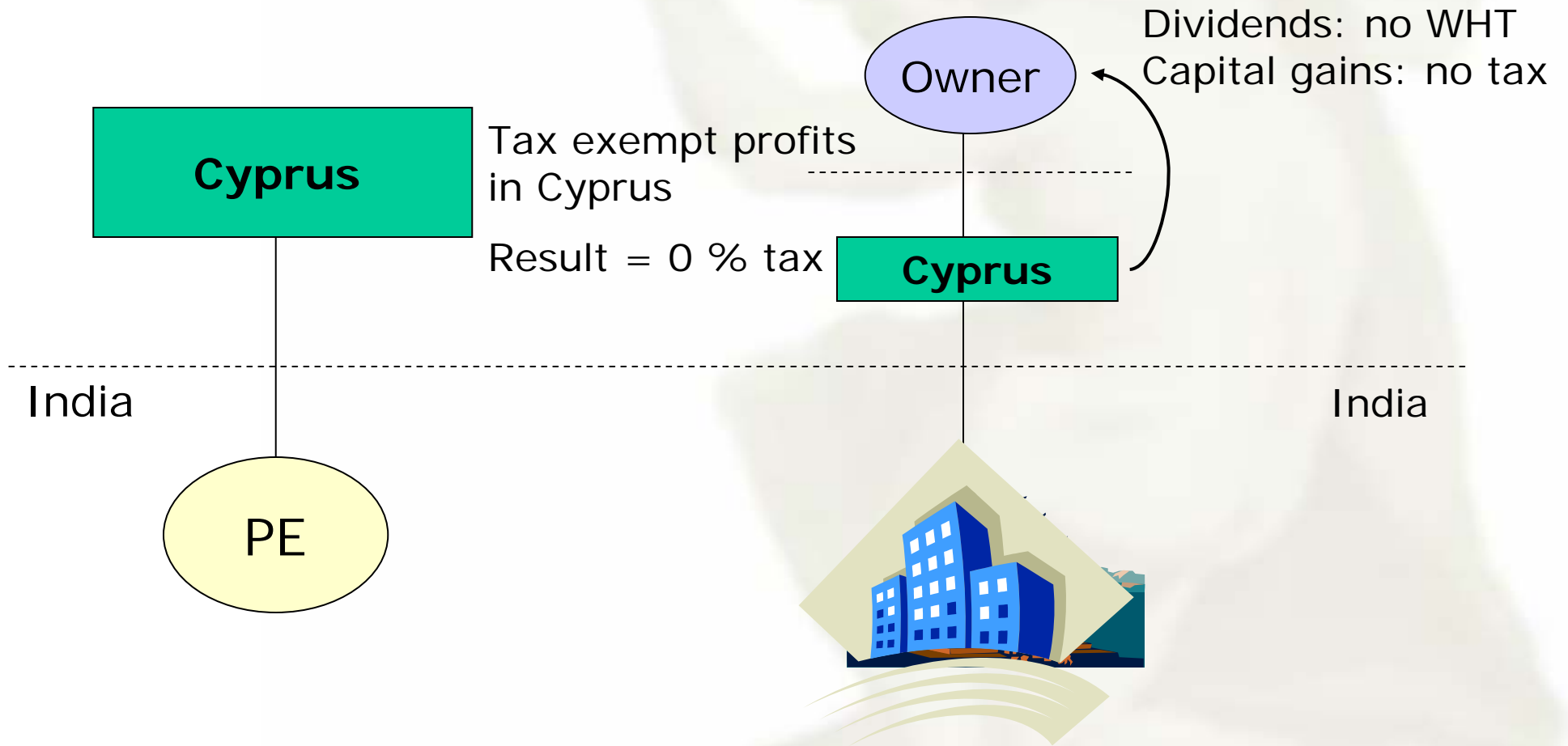
A Cypriot company has a branch in India.

Characteristics:

- PE profit taxed in India
- PE profit tax exempt in Cyprus
- Result: profit is repatriated to Cyprus without levy withholding tax
- Cypriot company can distribute its profit without paying withholding tax to any country in the world



Cyprus Permanent Establishment in India





Dubai – Investing in India Background

- Importance of the United Arab Emirates (“Dubai”) as a source of foreign direct investment in India is growing – particularly for Non-resident Indians located in the Middle East and Africa regions – also of interest for those involved in the oil and gas industries.
- The Dubai – India Double Tax Treaty was signed in 1992 and entered into force in 1993.
- Certain aspects of the Treaty have been subject to challenge by the Indian Tax Authorities, particularly in relation to the treatment of capital gains. However, a ruling by the Indian Authority for Advance Rulings in December last year has now clarified the position and upheld the terms of the Treaty.



Dubai – India Double Taxation Treaty

General Features

- Dividend withholding tax – no longer chargeable (on payments from India)
- Interest withholding tax – 12.5% unless the interest is paid on a loan granted by a bank or other similar bona fide financial institution (in which case the rate is 5%).
- Royalty withholding tax – 10%.
- Capital gains arising on the disposal of moveable property not connected with a permanent establishment in India are only taxable in Dubai (which does not tax capital gains).

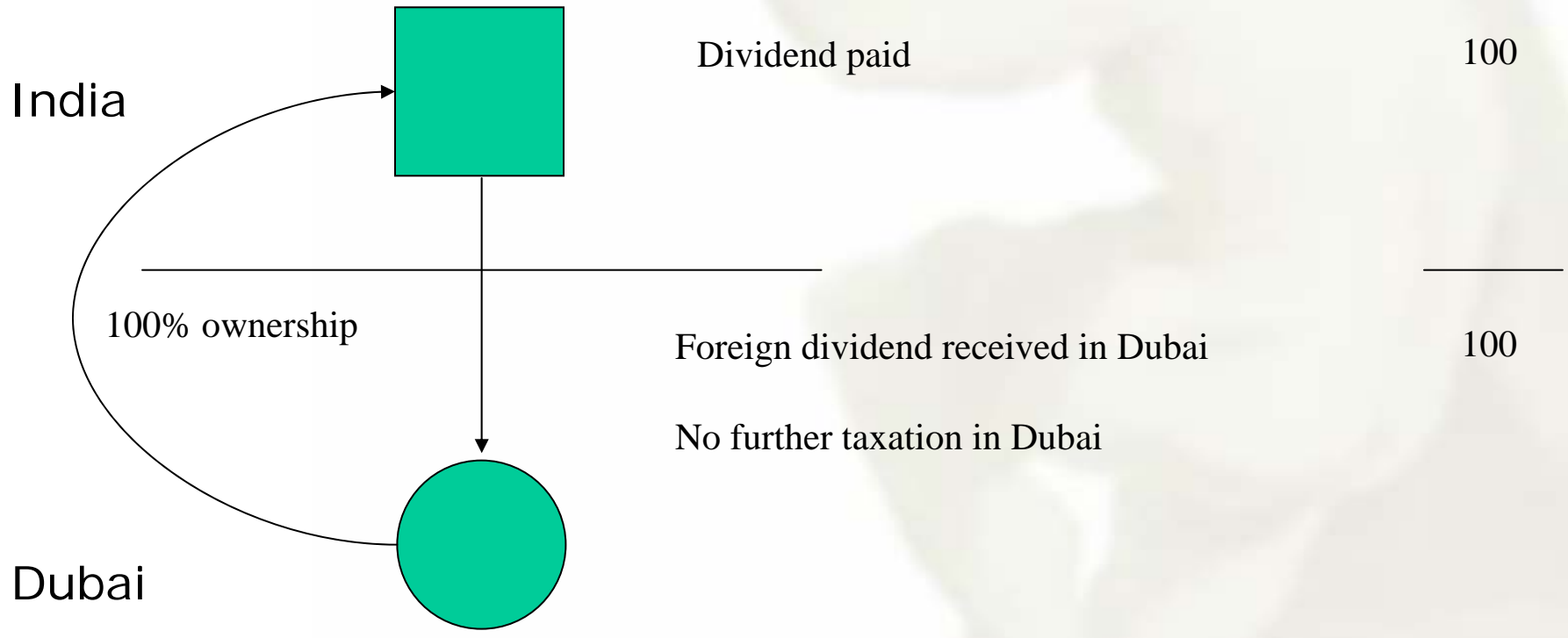


Dubai Taxation of Foreign Income

- There is no taxation in Dubai.
- There are no withholding taxes on payments from Dubai.
- There are no exchange controls or other restrictions on payments from Dubai.
- As a no-tax jurisdiction, after-tax profits can be held by the Dubai company without incurring any additional exposure to taxation.



Simple Investment Structure - Dubai





USA – Investing in India Background

- The USA is the largest source of foreign *indirect* investment in India.
- The USA – India Treaty was signed in 1989 and entered into force at the end of 1990.
- There are currently some unresolved issues regarding collection procedures under the treaty, but these do not effect its applicability.



USA – India Double Taxation Treaty

General Features

- Dividend withholding tax – no longer chargeable (on payments from India)
- Interest withholding tax – 15% unless the interest is paid on a loan granted by a bank or other similar bona fide financial institution (in which case the rate is 10%).
- Royalty withholding tax – 20%, except for royalties on films - 15%
- No allowance for capital gains exemptions.
- Tax sparing provisions allow for tax paid in India to be set off against tax in the USA (if any).



USA Taxation of Foreign Income

- All US companies are subject to tax on a worldwide basis.
- Gross income is taxable. Foreign taxes borne on foreign income may be credited against the corporation tax liability by way of foreign tax credits (see tax sparing provisions under the India Treaty). Typically, where a foreign dividend is received the foreign tax credit is the total of withholding taxes on the dividend, plus taxes paid by the foreign corporation relative to its profits from which the dividend has been paid.



Brazil – Investing in India Background

- The Brazil – India Double Tax Treaty was signed 1988 and entered into force in 1992.
- In 2004, India, Brazil and South Africa established the Trilateral Business Council so as to promote economic and trade relations between the three countries and their neighbours. Given the age of the existing treaty, it is intended that this will be updated as soon as practicable as part of the development of trade relations.



Brazil – India Double Taxation Treaty

General Features

- Dividend withholding tax – no longer chargeable (on payments from India)
- Interest withholding tax – 15% unless the interest is paid on a loan granted by a bank or other similar bona fide financial institution.
- Royalty withholding tax – 15%
- No allowance for capital gains exemptions
- Tax sparing provisions allow for tax paid in India to be set off against tax in Brazil (if any). However, for interest and royalties, and for deduction purposes, the 15 percent withholding tax paid is considered as having been paid at the rate of 25 percent.

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Brazil - Taxation of Foreign Income

- All Brazilian companies are subject to tax on a worldwide basis.
- Credit for similar taxes paid abroad is available, but only to the extent of the additional Brazilian tax payable on the foreign income. Foreign tax credits are available under the tax sparing provisions of the India Treaty.



Malta – Investing in India Background

- On March 9th 2005 the Governments of India and Malta signed a new double income tax treaty, replacing the earlier treaty entered into in 1994.
- The new treaty is effective from February 8th, 1995
- Bilateral trade between the two countries has been steadily increasing over the past few years, totaling US \$98 million from 2003 to 2004



Malta – India Double Taxation Treaty

General Features

- Dividend withholding tax – No longer chargeable on payments from India;
- Interest withholding tax - 10% withholding tax;
- Royalty withholding tax – 15% withholding tax
- No allowance for capital gains tax exemption;
- No tax sparing provisions.



Malta – Taxation of Foreign Income

- Taxation of worldwide income for resident and domiciled companies
- Corporate income tax 35%
- BUT: Full or almost full refund tax paid to shareholder upon dividend distribution
- No WHT on outbound dividends, interest and royalties
- EU Directives applicable
- Malta has a sophisticated international holding company and international trading company regimes
- Advance rulings are available and are applicable for 5 years

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Malta – International Holding Company

Qualifying participation

> 10% shareholding in the foreign company **OR**

Option to acquire the entire balance of shares not yet held by Maltese company **OR**

Representation on Board of Directors **OR**

Investment > Lm 500,000 (ca. EUR 1.200.000) **OR**

Extension of own (Maltese) business activities

Others

No minimum holding period

No activity test on subsidiary

No subject to tax requirement



Double taxation relief

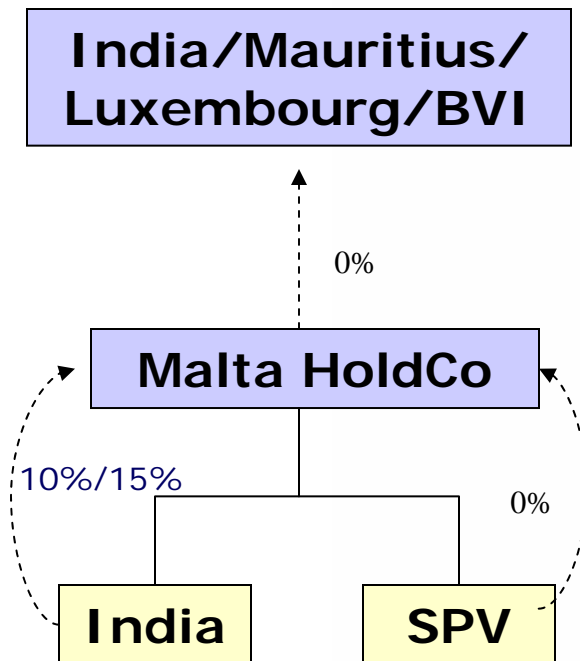
Company

Dividends	100
WHT	10
Net dividends to Malta	90

Tax (35%)	(31.5)
Distributable profits	58.5

**Non-resident shareholder
(EU/non-EU/treaty/non-treaty)**

Refund of company tax
to non-resident shareholder
31.5



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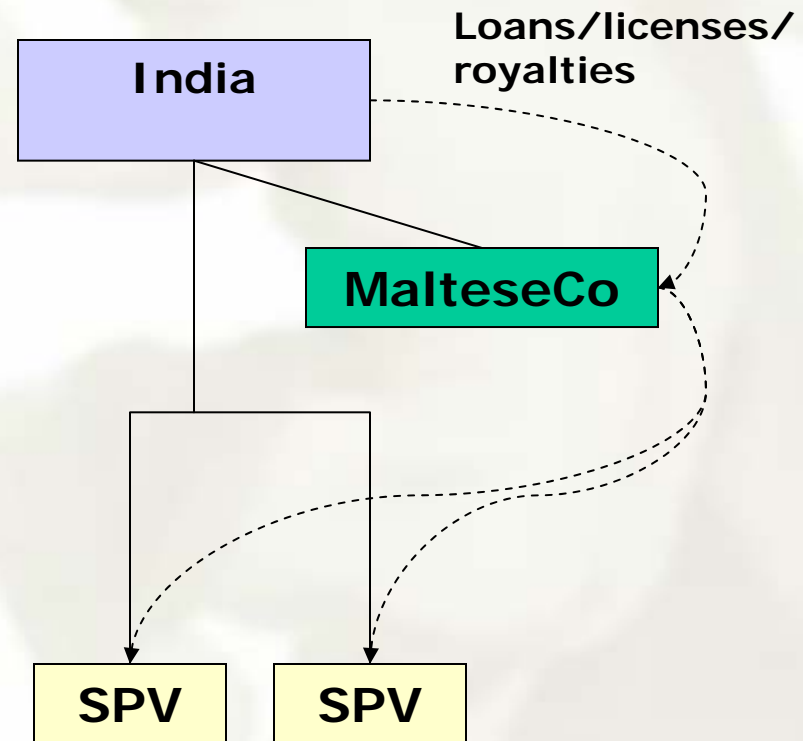
International Trading Company

- Trading outside Malta with Maltese non-residents
- Trading activities includes: finance, license, portfolio investments and commission income
- Subject to standard 35% CIT but non-resident shareholders entitled to 2/3 refund of tax paid on the profits out of which the dividends were paid out
- Non-resident shareholder subject to 27.5% tax on gross dividends but credit on dividend income
- Effective tax rate **4.17%**
- Tax refund received within 14 days
- Advance ruling valid for 5 years
- Exempt from stamp duty on issue or transfer of shares



Opportunities

- Financing companies (ITC)
- Royalty companies (ITC)
- Licensing companies (ITC)





Asset Protection Planning

- It is an important part of all cross-border structuring to ensure that not only the structure is tax efficient, but that it properly protects the investors from any adverse claims that may arise as a consequence of the investment – both from private parties and governments (such as from environmental hazards, on-site deaths or accidents, sexual harassment charges, aggressive government tax charges etc.).
- One of the most common methods of asset protection is to ensure the investments are structured through a limited liability entity, such as a limited liability company or (to a lesser extent) a limited liability partnership.
- Limited liability companies and partnerships are available and may be used in all of the jurisdictions discussed in this paper.



General Comments

- In the past, most structures for foreign investment in India have focused on reducing exposure to withholding tax (on the payment of dividends, interest and royalties from India) as well as mitigating exposure to capital gains tax. However, with dividend withholding tax being abolished in 1997, and the changes made last year to the capital gains tax rules, which eliminate the tax on long term capital gains (capital assets held for more than three years and one year for listed securities or mutual fund units) and reducing the tax on short term gains from 30% to 10%, most of the advantages which the traditional routes held, have been eroded.

Notwithstanding, each of the jurisdictions discussed offer different advantages and as with all cross-border structuring, it is important to choose the right jurisdiction to suit the structure. In this regard:



General Comments (contd.)

- Mauritius has the longest history of investment in India – the problems with the treaty in the past have now been resolved, so it is unlikely it will be challenged any further. Capital gains tax still applies in respect of short-term gains, so there may still be advantages in using Mauritius to mitigate exposure.
- Singapore is interesting – although the treaty is not likely to offer any advantages over other treaties, Singapore does have a “perception “ advantage as it is not generally considered to be a tax haven and has a reputation for sound regulation. Recent discussions between Singapore and India have focused on the removal of the qualifications for capital gains tax exemption in India.



General Comments (contd.)

- Cyprus has recently implemented a number of important changes to the development of its financial services sector, including new anti-money laundering and related regulations. Recent accession to the EU, has seen Cyprus become an important jurisdiction through which to structure foreign investment. Some of the features of the Cyprus imputation system were of concern to the EU, but in March and May of this year, agreement was reached on amending the current regime and for a new participation regime to be introduced at the beginning of 2007
- Dubai is of increasing importance, particularly for the regional Non-Resident Indian market and those involved in the oil and gas industry. Although the development of its financial sector infrastructure is comparatively new, Dubai is quickly becoming recognised as a significant regional financial centre. As with Mauritius, the opportunity to mitigate capital gains tax on short term investments, may still be of interest to some investors.



General Comments (contd.)

- Direct investment through the US and Brazil do not offer much in the way of tax savings as the treaties do not offer significant savings and the imposition of CFC rules do not allow for untaxed profits to be held offshore for any length of time.
- Malta, like Cyprus, is a recent entrant to the EU and as a consequence it's reputation as a financial centre has benefited significantly. Malta intends to introduce a participation exemption as per January 1, 2007.