

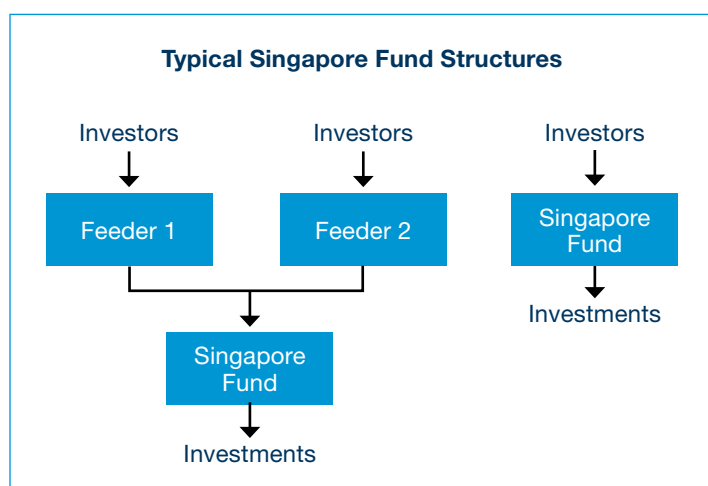
Investment Management

Harvest

Investment Management Industry Updates
Issue 4 • November 2009

Singapore as a Fund Location

Singapore is attracting attention as an alternative fund domicile location. A question that may come to the minds of fund managers is why they should consider Singapore as a location for setting up a fund, when there are other more commonly used locations such as the Cayman Islands and Mauritius to choose from. Many would have defaulted to the use of jurisdictions that they are familiar with. However, with the increasing concern over the use of jurisdictions which lack substance and are being attacked by tax authorities as being used only to secure tax treaty benefits, many are looking at alternative fund structures that can offer tax efficiency and at the same time withstand the substance test. Singapore has emerged as an attractive option. This can be attributed to the Singapore government's efforts in developing the investment management industry by introducing a series of tax benefits, and providing an infrastructure and environment that are conducive to business operations.



A. Reasons for choosing a Singapore fund

There are a number of reasons for considering Singapore as a location for setting up funds:

(i) *Different legal forms for funds*

A fund can be set up either as a company or a unit trust in Singapore. With the Singapore Limited Partnership Act coming into force on 4 May 2009, the Singapore limited partnership (LP) is also an available option.

(ii) *Network of Double Taxation Avoidance Agreements*

Singapore has a wide network of Double Taxation Avoidance Agreements (DTAs). To-date, Singapore has concluded more than 60 DTAs with countries including China, India and Japan.

Notably, the tax treaties which Singapore has concluded with certain Asian countries generally offer lower withholding tax rates on dividends and interest payments compared to the domestic withholding tax rates in those countries. In some cases, the tax treaties also provide for capital gains tax exemption.

However, to enjoy these benefits, the fund or its investing vehicle has to be set up as a Singapore-resident company.

(iii) *Certainty of tax treatment of Singapore funds*

Trading gains and income derived by a fund constituted in Singapore are generally taxable here to the extent that they are sourced in Singapore or received in Singapore from sources outside Singapore. Several tax incentive schemes which provide for the certainty of tax exemption on such income are available. These are discussed in detail below.

(iv) *Fund manager can be in the same location as the fund*

Singapore is strategically located and offers financial institutions a pro-business environment, excellent infrastructure, cost-competitiveness and a highly-skilled labour force, making it easy for a fund manager to set up its operations here. With the fund and its fund manager both being located in Singapore, the running of the fund becomes less administratively cumbersome. Furthermore, with the Singapore fund being managed in Singapore, it should become less of an issue demonstrating that the fund is in substance being operated in Singapore.

The icing on the cake is that the fund management company that manages the fund in Singapore may also apply for the income arising from its fund management activities here to be subject to a concessionary tax rate of 10%.

While income tax exemption may be available for a fund set up in Singapore under the various tax incentive schemes, other types of taxes may still be applicable. Examples of such taxes include goods and services tax (GST) on expenses incurred by the fund and withholding tax on interest payments by the fund to non-residents (say to the prime broker). Whilst the GST leakage has been substantially plugged as a result of a recent remission scheme announced by the MAS, the withholding tax on interest continues to remain a potential cost. These potential leakages essentially require a careful review of options and a thorough cost benefit analysis in order to minimise.

B. Tax exemption schemes for Singapore funds

As mentioned earlier, several tax exemption schemes are available for funds set up in Singapore, which cater for different circumstances. In the following sections, we will discuss two such schemes.

(i) Singapore-resident Fund Company Scheme

The tax exemption scheme for Singapore-resident fund companies (the “SRF Scheme”) was introduced in November 2006 to further develop the Singapore asset management industry. The SRF Scheme grants tax exemption for ‘specified income’ in respect of any ‘designated investment’ derived by any approved Singapore-resident fund set up as a company that satisfies the ‘qualifying fund’ test.

To enjoy tax exemption under the SRF Scheme, an application has to be submitted to the MAS. To be approved, a fund must undertake to meet the prescribed conditions, including the conditions that it:

- is a tax resident of Singapore where the control and management is exercised in Singapore (i.e. the fund company’s board meetings must be held in Singapore);
- is a company the value of issued securities of which is not 100% beneficially owned, directly or indirectly, by investors in Singapore (including investors who are resident individuals, resident non-individuals and permanent establishments in Singapore); and
- uses a Singapore-based fund administrator.

The investors will be split into two categories – qualifying investors and non-qualifying investors. A non-qualifying investor will have to pay a financial penalty to the IRAS. The financial penalty is calculated by attributing a percentage of the net profits in the fund’s audited accounts to that non-qualifying investor based on his interest in the fund on the last day of the financial year of the fund. The main type of investor who will be considered a non-qualifying investor appears to be a non-individual person based in Singapore (other than certain Singapore government entities) who take large (more than 30%) stakes in the fund.

An approved fund is required to comply with certain reporting/tax return filing obligations.

(ii) Enhanced-Tier Fund Tax Incentive Scheme

To provide Singapore-based fund managers with greater flexibility in sourcing for mandates, the MAS issued a circular on 30 April 2009 providing details of the Enhanced-Tier Fund Tax Incentive Scheme (“ET Scheme”) for fund vehicles. The key benefit of the ET Scheme is that the concept of qualifying and non-qualifying investors is not relevant under this scheme, and thus no investor is liable to a financial penalty. Also, under this scheme, fund vehicles can be set up as limited partnerships.

Funds approved under the ET Scheme (“ET Funds”) will be granted tax exemption for ‘specified income’ in respect of any ‘designated investment’. To be approved for the ET Scheme, the fund must undertake to meet the prescribed conditions, including the conditions that it:

- is a company, trust (other than a trust that is an approved pension or approved provident fund under section 5 of the Singapore Income Tax (Chapter 134), an approved CPF unit trust or designated unit trust, or a real estate investment trust) or limited partnership;
- has a minimum fund size of S\$50 million at the point of application; and
- uses a Singapore-based fund administrator if the fund is a company incorporated in Singapore, with its tax residency in Singapore.

All ET Funds are required to comply with certain reporting/tax return filing obligations.

Conclusion

In contrast to other fund locations, Singapore should stand out as a viable option, as it is possible to demonstrate substance out of Singapore where actual business activities can be conducted, thereby providing stronger grounds for claiming DTA benefits. The fund structure may also be simplified, reducing overall compliance costs. These benefits would need to be weighed against potential tax leakages on account of GST and withholding tax, and the issue of investor familiarity with Singapore. However, it is fair to say that serious consideration should be given to using Singapore as a fund location before the set-up of any fund structure, with a view to improving overall economic returns for the two key stakeholders – the investors and the fund manager.

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MICA (P) 131/02/2009 Co. Reg. No.: 199902830D