Cayman Islands top choice for FPIs to invest in India

Synopsis

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Mumbai: A sleepy Caribbean island country is emerging as a preferred gateway for various foreign investors to route their investments into India.

With the Securities and Exchange Board of India tweaking rules for overseas funds with opaque structures in 2019 and foreigners finding little incentive to invest in the country’s stocks through tax-friendly jurisdictions, Cayman Islands are gaining popularity among them for their relatively lower operational costs. Cayman does not have a tax treaty with India.

Currently, there are 329 foreign portfolio investors (FPIs) investing in India through the Cayman Islands. Consultants advising foreign investors said the number was below 100 until a few years ago. There has been a surge in foreign direct investments (FDIs) from there. Between 2000 and 2019, cumulative FDI investments received stood at $3.8 billion, DIPP data showed. In FY20, FDI flows from Cayman Islands stood at $3.7 billion.

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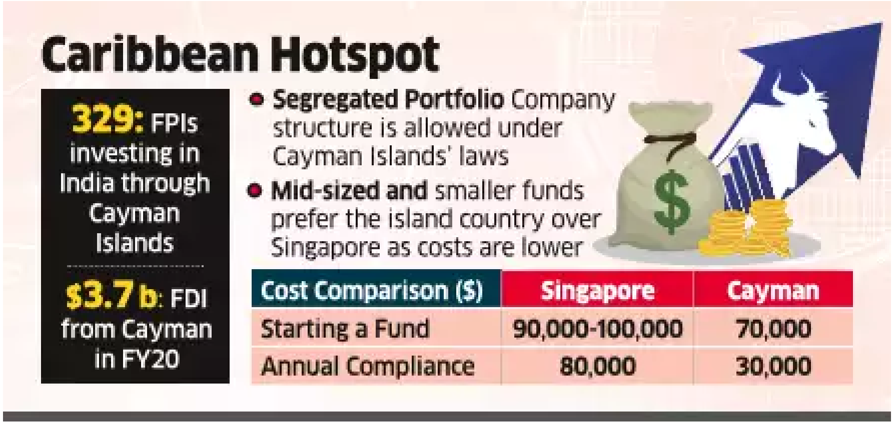
“Cayman is becoming a hot destination for foreign funds because it is cost-effective and allows the SPC structure, which was not permitted under the erstwhile Sebi FPI Regulations, except where such opaque structure had met the prescribed conditions,” said Dhaval Jariwala, partner of Mumbai-based PNDJ & Associates LLP, a firm that advises foreign investors on India.

Till 2019, segregated portfolios were not allowed. Such structures were considered ‘opaque’ by Sebi under the old norms as there were concerns that such vehicles were being used for money laundering. “Flexible segregated fund structures accorded by Cayman are cost-effective as well as legally ring-fenced and have increasingly been used for routing investments in India,” said Tejesh Chitlangi, partner, IC Universal Legal.

A chunk of foreign investors from Cayman are from the US and Canada. Some Hong Kong-based funds, too, are routing money into India through the island country following the India-China border conflict. The head of a large institutional brokerage requesting anonymity said some of the funds which traditionally came through Mauritius because of the tax treaty with India are now opting for Cayman.

The government has phased out tax advantages for investing in Indian stocks through jurisdictions like Mauritius and Singapore. But these benefits remain for derivatives and debt. With Mauritius coming under the so-called grey list of Financial Action Task Force (FATF) — an inter-governmental policy-making body setting anti-money laundering standards — the African nation has lost its popularity.



Cayman is preferred by many mid- and small-sized funds, which prefer the country over Singapore because of the lower expenses.

Though gains made by a Cayman structure need to pay normal taxes in India, these funds are finding that route cheaper and less cumbersome.

“We are increasingly seeing clients choosing to register FPIs based on their home jurisdiction, rather than an intermediate jurisdiction for the investment vehicles,” said Sriram Krishnan, managing director, Deutsche Securities Services. “In a way, this suggests that clients don’t mind the cost of doing business, which includes taxes, and it is important to have stability rather than be threatened with changes in rules from time to time, or be exposed to potential downgrading when it comes to any intermediate jurisdiction.”