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Foreign investors watch and wait as India goes to the polls

Foreign investment in India has reached a vital crossroads as India's 814 million voters go to the polls to elect the central government.

The general election, due to conclude on 12 May, is a hotly debated topic, provoking strong views and opinions across the country. Indians and foreign investors alike are waiting with bated breath to see who will lead the country for the next five years.

Indian stock markets are dominated by foreign investors. Buying or selling by foreign institutional investors (FIIs) strongly drives stock market indices in either direction. The volume of transactions by FIIs is always discussed with great interest and it has been observed that, often, when FIIs are buying, domestic financial institutions are selling and vice versa.

Clearing the hurdles

In the last two years, we have seen several changes announced to foreign investor regulations. In 2011, qualified foreign investors (QFIs) were recognised as a new category of investor. However, the QFI route never really took off due to lack of clarity on the tax front. A few months ago, a committee was set up by the Securities Exchange Board of India (SEBI) to suggest measures to harmonise various investment routes into India. The committee recommended combining QFIs, FIIs and FII sub-accounts into one route, called foreign portfolio investors (FPIs), with the aim of simplifying entry and compliance norms for foreign investors in India. SEBI accepted the committee's report and, subsequently, all regulatory hurdles were cleared. Various rules and regulations were notified by SEBI and corresponding notifications have also been issued by the Reserve Bank of India. Certain changes that were required under the Income Tax Act were also notified. As a result, the FPI regime is ready to be rolled out. Unfortunately, as procedural ground work has not been done yet, the FPI rollout has been postponed until 30 June 2014.

Rolling out regulation

The FPI regulation rollout is extremely important for India. In the last two years, FII registrations have been slow, with very few new registrations. International investors are wary of the Indian political scenario. The virtual policy paralysis that has gripped the Indian Government and the unearthing of several scams involving billions of rupees has rattled investors. Tax-related developments too have not helped the situation. Cases like Vodafone, where the tax authorities have demanded huge amounts of tax revenues from large multinational corporations operating in India (coupled with the retrospective amendment to the law to overturn the Supreme Court's decision in Vodafone's favour) have only added to the concerns of foreign investors.

Sitting tight

India now finds itself at a crossroads. While the Indian economy continues to be an attractive destination for investment, with a change in government likely following the election, many investors are waiting in the wings. If the right wing Bharatiya Janata Party (BJP) comes to power, riding on the back of a massive campaign by its prime ministerial candidate Narendra Modi, it is very likely that the stock markets will see a flurry of activity. Those who have held back their investment plans for now will surely start investing in Indian stocks. On the other hand, if there is a hung parliament, the future for India as a destination for foreign investment seems bleak. With a number of countries competing for foreign investment – and Africa becoming increasingly popular with investors – there is bound to be a flight of capital, which does not bode well for the Indian economy. Businesses and investors both in India and around the world await the election results due to be announced on 16 May with great interest.

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'Wait-and-see' approach to Shanghai Free Trade Zone

The latest developments from China's trade policy reform pilot zone.

At the end of September 2013, China's State Counsel formally opened a Free Trade Zone (FTZ) in Shanghai as a testing ground for a variety of policy reforms intended to further encourage both inbound and outbound foreign trade and investment.

Since then, government agencies involved in the project have released circulars describing the guiding policies and principles adopted within the FTZ. While, in many cases, formal implementation regulations have yet to be published, the documentation released to date offers insight into the potential benefits that will become increasingly available to domestic and foreign-invested enterprises that register within the FTZ.

One-stop-shop

The FTZ is managed by the Shanghai FTZ Administration Committee, which has been set up as a one-stop-shop for coordination of all FTZ activities. Working in concert with the related government agencies, the FTZ Administration Committee has been empowered to:

- relax the regulatory environment
- open up a wider range of service industries to foreign investment
- ease restrictions on outbound investment
- simplify customs procedures related to the import and export of goods
- reform foreign exchange regulations, including the free convertibility of RMB currency.

Restrictions

Similar in nature to 'China's Catalogue for Guidance of Foreign Investment Industries', the Shanghai FTZ Negative List restricts or excludes a variety of foreign-invested business types from enjoying the benefits of company registration reforms. However, many more industries are now open to foreign investment within the FTZ, especially those in the services sector.

Businesses that are not on this list are now allowed to register with the FTZ Administration Committee in a streamlined and simplified process never previously seen in China. First, qualified companies are no longer required to apply for approvals ahead of registration. Second, with some exceptions, minimum registered capital requirements have been eradicated, to the extent that company investors can not only decide on the amount of registered capital to be injected, but also the timeframe and other terms of capital payments. These changes have reduced the time required to open a company – by half, in many cases.

Most of the restrictions in the current FTZ Negative List are related to business activities that may compromise China's national security in relation to natural and energy resources, the financial services industry, cultural services and others. The next revision of the list is, however, expected to further reduce the number of restricted business types.

Loosening the reins on financial services

In a first step towards liberalising the financial services industry, the People's Bank of China and FTZ Administration Committee have authorised and implemented a programme by which third-party service providers in the FTZ may be engaged to carry out cross-border transactions in RMB currency. Five service providers have been approved, with more expected to follow.

In addition, the State Administration of Foreign Exchange (SAFE) recently announced rules for simplifying current account and capital account settlements, as well as helping multinational companies optimise their cash management and improve capital efficiency. Furthermore, SAFE approvals are no longer required for outbound payment of guarantee fees by companies and non-banking financial institutions within the FTZ. Much of the administration of the new policies will reside with the banks, with SAFE simply monitoring activities though reporting processes.

The Central Bank has also approved a plan to allow banks in the FTZ to set interest rates on company or individual account deposits of less than US$3m. Other financial policies expected this year should provide for greater flexibility over interest rates and further reduced control over foreign exchange.

Shanghai FTZ goes national

As of February this year, more than 6,000 new company registrations were conducted in the Shanghai FTZ. Only 400 were foreign-invested companies, and most of the businesses were related to trade. It would therefore appear that while domestic Chinese companies and individuals are rapidly embracing the concept of the FTZ, foreign investors are taking a more relaxed, wait-and-see approach.

As predicted when the FTZ was first announced last year, many of the reforms on trial are being rolled out to other areas in China. For example, company registration and registered capital regulations are being relaxed, foreign exchange rules are changing, and other cities and districts are applying for full FTZ status throughout the country.

It is expected that a year from now the regulatory environment in China will look quite different from how it does today. This should allow global businesses to conduct their activities with increasing ease. However, China is well known for taking small incremental steps when opening up to foreign influences within its borders. So, at this stage, taking a wait-and-see approach to any sweeping reforms may well be the right thing to do.

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Malta's citizenship model for attracting individual investors

How Malta's Individual Investor Programme stacks up against similar European schemes.

Malta's Individual Investor Programme (IIP) has undergone a fine-tuning process since its initial launch. The Malta IIP is currently the only programme of its kind that has had its validity officially recognised by the European Commission. It is considered a model for other countries to follow.

The Maltese Government recently reported that a number of citizenship applications under the Malta IIP have been approved, mainly as the applicants have been resident in Malta for a period of time. Consequently, successful applicants may be in possession of their passports within a few months.

Malta's IIP

Malta's IIP grants citizenship by naturalisation to applicants who can prove that they have been resident in the country for at least 12 months. Once a certificate of naturalisation has been issued, an individual can apply for a Maltese passport. A combination of physical presence and other factors are taken into consideration to determine this residence requirement, rather than a specific number of days.

How does it work?

Successful applicants will benefit from the same rights enjoyed by EU citizens in all 28 EU countries and Switzerland, as well as passport and visa-free travel to over 163 countries, including the US. The full application process can take 6 to 24 months and is subject to a one-off contribution of €650,000 by the main applicant. Furthermore, applicants must prove that they are in possession of a residential fixed address in Malta with a minimal value of €350,000 or paying a minimal annual rent of €16,000. This needs to be retained for a period of at least five years. Moreover, an investment of €150,000 in stocks, bonds, debentures, special purpose vehicles or other investments is also required and must be retained for five years.

Alternative IPPs

Cyprus and Austria offer similar investor programmes which may result in immediate citizenship, although both countries argue that they should not be compared to Malta's IIP. The process in Cyprus, although one of the fastest, requires the applicant to invest €5m in the country for a three-year term, create jobs and employ Cypriot nationals. Moreover, an applicant is subject to Cypriot taxes, must purchase property and invest in government private bonds. The Cypriot Government is working on amending the existing programme in light of the European Commission's agreement with Malta. The Austrian system may reward foreigners with citizenship in cases of extraordinary merit. The process can take a number of years (requiring ten years' residency in Austria) and is also subject to substantial investment or job creation.

Other countries such as Belgium, Portugal, Spain and Greece also offer residency, which may lead to citizenship with Schengen privileges, i.e. enabling passport-free movement between a large number of European countries. In the case of Belgium, a five-year residence period is required, after which time an individual may apply for citizenship and, if accepted, receive a Belgian passport within five years. Applicants are also subject to minimum investment requirements and annual residency fees. In Portugal, citizenship programmes include an investment, business development and retirement route, all of which are subject to a substantial amount of property acquisition, income requirements and/or business investment.

EU non-Schengen countries like Ireland and the UK provide an entry clearance visa, leading to indefinite leave to remain and citizenship. The value of investment required in Ireland is €500,000 in an approved fund or €1m in a government bond for a five-year term, whereas in the UK it starts from a minimum of €1m over a five-year term. If the investment amount is higher, the term of retention of investment may be reduced accordingly.

Nexia BT is an 'accredited person' by the Government of Malta and may assist applicants in completion and submission of applications under the IIP.

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Renewable energy investment opportunities in Poland

The Polish parliament is widely anticipated to pass its Renewable Energy Sources (RES) Act this year – four years after the EU deadline.

Poland is the last, large European country to jump on the once overcrowded renewable energy bandwagon. The renewable energy sector continues to attract investor interest however, so the development is seen as better late than never.

Poland needs extra capacity urgently due to the impending decommissioning of many socialist-era power plants. The country's power grid requires major renovation and there is also the need for more interconnection points and high-voltage lines, to connect the north with the south.

As a latecomer to renewable energy, Poland will benefit from continuing capital expenditure decreases in leading technologies, such as wind and photovoltaic. This will make it significantly cheaper for the Government to develop the sector, further reassuring investors that there will not be a U-turn on renewable energy plans.

A number of companies will benefit from the boom in the Polish renewable energy sector. This includes companies traditionally associated with RES, such as funds, banks and developers, engineering, procurement and construction firms, as well as the general services sector. There will also be significant opportunities for the tax and legal professions, as many issues are yet to be covered by Polish law.

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NEXIA INTERNATIONAL

Global Insight

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Key tax issues for businesses going global

Businesses exploring global opportunities should be mindful of international tax issues.

The internet and other technological developments have made it easier than ever for companies of all sizes to sell their products and services overseas. But that doesn't mean international tax issues are any less complex.

Are you paying more tax than necessary?

In the US, manufacturers and others that export American-made goods overseas can enjoy substantial tax benefits by setting up an interest-charge domestic international sales corporation (IC-DISC). These benefits are also available for architecture and engineering services related to foreign construction projects and for certain software exports.

An IC-DISC is designed to receive commissions on export sales on a tax-advantaged basis. A corporation on paper only, does not need to have offices or employees and it's not required to provide any services, so it's relatively inexpensive to set up and operate. If an IC-DISC is structured properly and meets certain requirements, it can reduce taxes on export profits by 40% or more and defer tax payments on those profits.

Despite these benefits, this tax break is under-utilised. One reason for this is that many companies don't realise they are eligible. For example, companies that manufacture component parts that are ultimately incorporated into exported products may qualify, even though they don't export their products directly.

Is the price right?

Transfer pricing is one of the top issues for revenue-strapped tax authorities around the world. It concerns the prices for which related parties, such as a corporation and its foreign subsidiary, exchange goods, services or intangible assets in cross-border transactions.

Governments are concerned that companies manipulate these prices in order to shift profits to lower-tax jurisdictions. Contrary to popular belief, transfer-pricing restrictions aren't limited to international transactions. In the US for example, they also apply to domestic companies that do business with related parties across state lines.

To deter tax avoidance, transfer-pricing rules require related parties to set prices that are comparable to those charged in arm's length transactions, using one of several accepted methods. It's also a good idea to document intercompany pricing decisions contemporaneously (in some countries documentation is required) to ensure compliance with the rules. The consequences of non-compliance are severe. In the US, for example, penalties range from 20-40% of the underpaid tax.

Companies concerned about transfer-pricing liability should consider negotiating an advance pricing agreement with the tax authorities to avoid any tax surprises further down the road.

Are your foreign accounts in order?

Individuals and entities in the US with a financial interest in, or signature authority over, certain foreign accounts are required to report these accounts to the US authorities annually on the Financial Crimes Enforcement Network Form 114 – Report of Foreign Bank and Financial Accounts (FBAR). The form is required if the aggregate value of foreign accounts, such as bank accounts, brokerage accounts, mutual funds or trusts exceeds US$10,000 at any time during a calendar year.

Failure to file required FBARs could result in substantial monetary penalties and, in extreme cases, imprisonment. In some cases, these penalties will apply to a company's officers or employees with signature authority over foreign accounts.

Individuals or companies that have missed FBAR filings in previous years should consider participating in the IRS's Offshore Voluntary Disclosure Initiative. In most cases, coming forward voluntarily allows monetary penalties to be minimised and avoids criminal prosecution.

Are you ready for FATCA?

The Foreign Account Tax Compliance Act (FATCA) was enacted in 2010 in an effort to prevent US taxpayers from hiding assets overseas. The act requires foreign financial institutions and other foreign entities to file reports with the IRS identifying their US account holders or major investors.

The act encourages compliance by imposing a 30% withholding tax on certain US-source payments including interest, dividends, rents, royalties and compensation. From 1 July 2014, US entities and others in control of these payments must begin withholding 30% of payments to non-compliant foreign entities. Companies making payments to foreign entities should verify and document their FATCA status and determine their withholding obligations.

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Finding the right way to value a business

Valuing a business is made even more complicated by the variety of approaches to choose from.

A company's share value is always subject to much discussion among shareholders and investors. As the Dutch saying goes: "Value is what the next idiot will pay." In fact, this is what we call price and price is not a synonym for value.

Value is a complex concept. It exists in the mind of the individual and is completely subjective in relation to the expectations and wishes of that person. For example, a car enthusiast may value a vintage car very differently to a normal motorist. Trying to objectify that value isn't easy.

Walking in the buyer's shoes
In the case of a corporate transaction, one must try to empathise with the potential buyer and put oneself in their shoes to understand the assumptions and expectations they might have for the future cash flow of the business. This will give you an insight into the value of the object to the buyer and, in turn, the price they might be willing to pay for it. A buyer will never purchase an object for more than its perceived value, but they might use it as a guide to the maximum amount they would be willing to pay.

Take, for example, a transportation company that is interested in buying another transportation company. The target company may hold a strategic advantage for the buyer if, for instance, the buyer's routes are adjacent to the routes of the target company, offering potentially substantial cost reductions in future years. If the potential buyer is a financial investor, it will be more difficult to achieve the same cost reductions.

Return versus risk
Another important question is how to calculate the return the buyer will require on an investment with a business-specific risk? A popular method is to use the capital asset pricing

model. This portfolio theory was developed in the 1960s and takes the risk-free rate as a basis. In the Netherlands, one usually takes the interest rate at the time of valuation of ten-year Dutch treasury bonds, which are considered as risk free as you can possibly get. A market risk premium is added, which accounts for the additional return shares have yielded on top of the risk-free rate. According to research by McKinsey, this varies between 5% and 6%. As some market can be more volatile than others, a correction is made to take account of the market risk premium, which is known as Beta. The Beta is multiplied by the market risk premium giving you the cost of equity.

If the business being valued is small or has specific risks then these will also need to be taken into account. Many firms carrying out valuations will offer an additional, statistically generated, specific risk premium, based on the size of the business being valued or other characteristics. These will also be part of the cost of equity.

The build-up model

Another method often used in the valuation of small and medium-sized enterprises is the build-up model. This method embraces the subjectivity of valuation and instead of trying to objectify the cost of equity, analyses the company's ability to operate independently. It builds on the same risk-free rate and market risk premium, but rather than including Beta and specific risk premiums, breaks down the dependencies of the company and assigns a subjective value to the perceived risk. Those perceived dependencies are ideally incorporated into forecasted free cash flows, for example, in the form of scenarios. Of course, professional judgment is needed to ensure that this is within certain limits.

The cost of equity will always be open to discussion, but this is preferable to putting blind faith in an outcome by using formulas calculated into double-digit decimals.

Using multiples of EBIT or EBITDA are useful tools to put your valuation in perspective. If your outcome from commonly used valuation methods differs significantly from the multiple outcome, there could be an error in your valuation. On the other hand, sector multiples originate from prices and negotiations and do not incorporate the intentions of the proposed buyer – rather, they incorporate those of previous (and perhaps completely different) buyers.

Chartered valuers in the Netherlands are highly trained professionals who are qualified to perform business valuations.

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Singapore: an international market

An update on the recent performance of the Singapore Exchange.

Singapore's capital markets are among the most international in Asia. Foreign issuers constitute 291 (38%) of the companies listed on the Singapore Exchange (SGX). Of these foreign issuers, 133 (46%) are Chinese companies.

SGX performance

A total of 767 companies are listed on the SGX, of which 626 are on the Mainboard exchange and 141 are on the Catalist exchange, the SGX's secondary board. The Mainboard and Catalist have a total market capitalisation of S$949.5bn and S$9.6bn, respectively. The average market capitalisation on the SGX is slowly returning to pre-financial crisis levels and corporate fundraising activities are increasing.

IPO levels

In 2012, a total of 26 issuers raised about S$4.5bn through initial public offerings (IPOs), where 14 issuers were listed on the Mainboard and 8 on the Catalist. The most prominent IPO that year was IHH Healthcare Berhad, Asia's biggest hospital operator, which had a dual listing on the Malaysia and Singapore stock exchanges. The IPO raised a total of S$2.5bn and was the third largest in the world for 2012.

Despite 2013 being a slow year for the Singapore stock market, with the Straits Times Index closing a mere 0.01% higher than the year before, the IPO market was alive with activity. Total equity fundraising grew by 40% to S$6.3bn in 2013 and a total of 27 IPOs debuted on the SGX.

In the first half of 2013, seven IPOs floated on the Mainboard and three on the Catalist. IPO market momentum in the second half of the year, boosted by the IPO of Singapore Press Holdings' (SPH) real estate investment trust (REIT) in July 2013. The IPO of SPH REIT featured 308.9m shares at S$0.9 each, raising a total of S$504m, and was 25 times over-subscribed.

Singapore's IPO market subsequently became the second largest in the world in the third quarter of 2013, according to independent research. Overall in 2013, there were a total of 15 listings on the Mainboard, raising S$6,031.5m, and 12 listings on the Catalist, raising S$253.3m.

Strong draw for trusts

SGX has been a strong magnet for REITs and business trust listings in the region. In 2013, REITs and business trust listings constituted seven out of the 15 IPOs floated on the Mainboard. Some of the more prominent ones included SPH REIT, Croesus Retail Trust and

OUE Hospitality Trust. However, the performance of these issuers fell below their respective IPO offer prices, with the exception of SPH REIT, which managed to achieve a gain of 0.09%.

In fact, at the time of writing, only four out of the 15 Mainboard issuers were trading above their offer prices. The top performers included Overseas Education, Pacific Radiance, SPH REIT and Linc Energy.

Tightening up Mainboard listings

SGX introduced stricter admission criteria for companies listing on the Mainboard in August 2012. Based on the new requirements, an issuer must have:

- a minimum consolidated pre-tax profit of at least S$30m for the latest financial year, with an operating track record of at least three years

- a market capitalisation at IPO of no less than S$150m if it has been profitable in the latest financial year, with an operating track record of at least three years

- a market capitalisation at IPO of no less than S$300m, with a generated operating revenue in the latest completed financial year.

Moreover, the minimum issue price of the IPO shares has been raised to S$0.50 per share, compared with the previous price of S$0.20.

SGX also introduced new Mainboard admission rules and continuing listing obligations for mineral, oil and gas companies in September 2013. The new rules seek to better safeguard investors' interests given the technical and specialised nature of the industry.

According to Magnus Böcker, CEO of SGX, the enhanced admission standards will increase Singapore's attractiveness for companies and investors, further strengthening its position as an international financial centre.

Smaller companies are increasingly likely to turn to the Catalist, the specialist growth company market. These small-cap companies outperformed the Mainboard in 2013, with seven out of 12 Catalist IPOs making gains on their respective IPO prices.

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The benefits and risks of cloud computing

The benefits and risks of cloud computing

Educating yourself and your people on the benefits and risks associated with cloud computing is of the utmost importance.

Cloud computing is here and virtually every organisation is using it in some way, shape, or form. We look below at the opportunities presented by cloud computing, the risks associated with housing your sensitive data in the cloud, using virtual computing environments and vendor management considerations for those exploring their cloud options.

What is 'the cloud'?

'The cloud' is an all-encompassing term for a virtualised information technology (IT) computing environment in which individuals and businesses work with applications and data stored and maintained on shared computing platforms. These may be hosted 'on the Internet' or run from in-house systems (i.e. a private cloud). Google's popular email system, Gmail, is an example of a cloud-based application, but this is just one model. Apple's iCloud is another example. There are three main cloud service models — software as a service, platform as a service, and infrastructure as a service — deployed in four types of settings — private, community, public and hybrid clouds.

Service models

- Software as a service (SaaS) provides integrated access to a provider's software applications. The provider usually has responsibility for nearly all the controls.

- Platform as a service (PaaS) provides access to basic operating software and services to develop and use customer-created software applications. Control responsibility can vary and is shared between provider and customer.

- Infrastructure as a service (IaaS) provides access to server hardware, storage, network capacity, and other fundamental computing resources. Most of the controls are the customer's responsibility.

Deployment models

- Private cloud is accessible from the intranet or internally hosted, and used by a single organisation.
- Community cloud has infrastructure accessible to a specific community, group, or association.
- Public cloud is accessible from the internet, externally hosted, and used by the general public.
- Hybrid cloud is a combination of two or more clouds.

Cloud benefits

Cloud computing provides a scalable online environment that makes it possible to handle an increased volume of work without impacting system performance. Cloud computing also offers significant computing capability and an economy of scale that might not otherwise be affordable, particularly for small and medium-sized organisations, without the IT infrastructure investment. Cloud computing advantages include:

- Lower capital costs — Organisations can provide unique services using large-scale computing resources from cloud service providers, and then nimbly add or remove IT capacity to meet peak and fluctuating service demands while only paying for actual capacity used.
- Lower IT operating costs — Organisations can rent added server space for a few hours at a time rather than maintain proprietary servers, without worrying about upgrading their resources whenever a new application version is available. They also have the flexibility to host their virtual IT infrastructure in locations offering the lowest cost.
- Improved operations — Organisations can reduce the need to handle hardware or software installation or maintenance.
- Improved BCP/DR infrastructure — Organisations may leverage the process to create more robust disaster recovery and business continuity features and services, if properly managed.
- Higher efficiency — Organisations may be able to optimize their IT infrastructure and gain quick access to the computing services required.

The risks

- Environmental security — The concentration of computing resources and users in a cloud computing environment represents a concentration of security threats. Because of their size and significance, cloud environments are often targeted by virtual machines and bot malware, brute force and other attacks. Ask your cloud provider about access controls, vulnerability assessment practices, and patch and configuration management controls to see that they are adequately protecting the systems and your data.

- Data privacy and security — Hosting confidential data with cloud service providers involves the transfer of a considerable amount of an organization's control over data security to the provider. Make sure your vendor understands your organisation's data privacy and security needs. Also, make sure your cloud provider is aware of relevant data security and privacy rules and regulations that apply in your particular jurisdiction.

- Data availability and business continuity — A major risk to business continuity in the cloud computing environment is loss of internet connectivity. Ask your cloud provider what controls are in place to ensure internet connectivity. Ensure that you have a backup plan for when the service is not available (not if it is not available). If a vulnerability is identified, you may have to terminate all access to the cloud provider until the vulnerability is rectified. Finally, the seizure of a data-hosting server by law enforcement agencies may result in the interruption of unrelated services stored on the same machine.

- Record retention requirements — If your business is subject to record retention requirements, make sure your cloud provider understands what they are so it can meet them. This should include litigation preparedness and litigation hold requests.

- Data management — Many organisations do not know where the data is and where it flows so it becomes difficult to manage. Organisations are often unaware of any subcontractor arrangements, which increases the complexity and the need to manage and control the processes.

- Disaster recovery — Hosting your computing resources and data at a cloud provider makes the cloud provider's disaster recovery capabilities vitally important to your company's disaster recovery plans. Know your cloud provider's disaster recovery capabilities and ask your provider if they have been tested.

- Transitioning — Organisations seem to be less well prepared in the event that they want to cease or change the contractual relationship. Ensure you know how you will get your information back and what the associated costs might be.

Evaluating your options

Many cloud provider options are available, each with unique risks. As you evaluate your choices and the associated risks, consider the following:

- Be diligent about understanding which controls the cloud provider is responsible for, and which controls they expect you to be responsible for. The further down the "cloud stack" you go (SaaS → PaaS → IaaS) the more responsibility for controls you assume.

- Cloud providers are sometimes reluctant to produce third-party audit reports unless an audit clause is included in the contract. Work to include audit clauses and other relevant, measureable Service Level Agreements (SLAs) in your contract. Some service providers may require clients to pay for reports.

- Some internal audit departments are performing control reviews of cloud providers, in addition to receiving and analysing third party audit reports. This is driven by certain controls not being tested, exclusion of pertinent systems, or other factor that require on-site testing.

- Evaluate the capabilities for problem resolution. How will the provider work with you to resolve issues? Do you have a nominated individual who will help or are you at the mercy of a help line and a timeline that does not meet your needs? Standard cloud provider audit reports typically do not include vulnerability/penetration testing results. Providers are hesitant to allow scanning, as they believe this may compromise their infrastructure.

Cloud computing is a widely used format and we don't see this changing anytime soon. Knowing that you are managing the risks associated with housing your sensitive data offsite will give you confidence with the platform, so you can take advantage of the opportunities presented by the cloud. You will be well served to manage this relationship just like any other well-managed and monitored, well-contracted arrangement with a significant vendor.

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Global Insight

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US economic outlook

Economic activity improves in the US in 2014, but challenges remain.

Economic activity in the US is expected to accelerate in 2014. The escalation will be solid but constrained by a vacillating private sector, slower monetary stimulus and increasing regulations.

Growth in real gross domestic product (GDP), i.e., total output of goods and services adjusted for inflation, should approach 2010's – the best year since the recession – which ended 2.8% higher than the prior year.

Consumer spending, more than two-thirds of GDP, will lead the acceleration as jobs growth picks up.

Positive factors

After a severe winter across much of the US, the labour market gathered momentum in the first quarter. Consequently, the jobs recovery – the slowest since the 1930s – will be complete by mid-year, when employment will finally exceed the January 2008 peak. The rate of hiring is expected to increase gradually in the second half of the year.

Although sub-par, the gains in jobs and earnings have produced paychecks larger than before the recession. With those gains augmented substantially by other sources, e.g. income transfers, after-tax incomes are 18.5% (8.2% net inflation) higher than at the end of 2007. That increased households' spendable income by some US$2trn. And debt service reductions (via diminished mortgages and consumer credit) freed almost US$400bn of that for households to spend or save.

With profits contributing a record share of GDP, and business and household balance sheets restored (household net worth is a record US$80.7trn), private investment should ramp up over the course of 2014. Business spending on plant, equipment and structures (one-eighth of GDP) is gaining traction. And spending on residential structures (still well below its long-term share of GDP) is rising.

Constraints on growth

The recovery's cumulative progress has lifted consumer and business sentiment; but its stutter-step sluggishness has left them cautious, willing to spend but not freely. This will constrain 2014's acceleration.

As outsized Federal deficits have been scaled back, the government sector has been a drag on the economy While that constraint is lessening, continued fiscal consolidation will suppress public-sector spending in 2014.

Two other factors will further inhibit the expansion's pick-up. The first is the Federal Reserve's continuing curtailment of monetary stimulus. That will cause interest rates to rise, albeit gradually.

The other constraint involves the implementation of various policy changes, e.g. financial re-regulation and healthcare reform, which are increasing the costs and uncertainty of doing business. Irrespective of their long-term benefits, they will dampen growth in the near term.

On net, however, the economic expansion should gather momentum during 2014.

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Global Insight

April 2014

A critical year for Europe

Europe is finally expected to return to positive economic growth in 2014.

The members of the eurozone face a number of critical decisions in 2014 if they are to put in place an effective system to prevent a rerun of the banking crisis and regain public support. Meanwhile the European Central Bank (ECB) is under pressure to provide more stimulus as a new economic threat, outright deflation, starts to rear its head.

Is Europe finally on the road to economic recovery?

The consensus view is that Europe will return to economic growth this year, but that the growth rate is unlikely to exceed 1% in 2014 – a long way from the higher growth rates that were common before the global financial crisis.

Surveys of business expectations, including the widely followed purchasing managers' indices, are picking up in many European countries. Consumer and business confidence ratings are also improving. However, none of these indicators yet point to anything more than meagre economic growth this year.

Main areas of vulnerability

Unemployment in the eurozone has continued to rise. It now stands at more than 12%, nearly twice the US and UK average. That will not start to fall until growth resumes in earnest. Bank lending remains weak by historical standards and borrowing costs for the troubled periphery nations remain too high for comfort.

In its latest quarterly economic assessment the European Commission admitted that Europe's productivity record since the mid-1990s has been poor and made worse by widespread misallocation of resources during the credit boom. On the positive side inflation has been falling, but even that poses new risks of its own.

Deflation a concern

With the average rate of inflation in the eurozone now down to 0.8% per annum, deflation is hazardously close to taking a grip.

Due to their negative rates of growth many countries in Europe have been unable to make any inroads into their high debt levels since the crisis. The vast majority of eurozone members have debt to GDP ratios above 80% (source: Bloomberg) well above the maximum limit mandated by the treaties which created the euro in the 1990s.

The ECB doesn't see deflation as an imminent threat. The main problem it faces is not having the same freedom to deploy stimulus measures as other central banks, including quantitative easing. Such programmes appear to be ruled out by European treaties, but governments could agree to override the restrictions if a new deflation crisis seems likely.

Preventing another banking crisis

In November 2014 the ECB will formally take on a new role as the lead supervisor for the largest banks across the eurozone, taking a lead role in winding up or rescuing any that get into financial distress. All the banks will be subject to both an asset quality review and a 'stress test', to estimate the resilience of balance sheets to economic and financial downturns. This new bank resolution regime is only one of a broader range of measures that are needed to create a genuine banking union across Europe. European governments currently lack public support to go any further towards this ultimate objective.

Looking forward not back

Despite these potential difficulties, investors have become much more positive about Europe since the middle of 2013. Borrowing costs of the most troubled 'periphery' countries have continued to fall quite sharply, reflecting the market view that the risk of the eurozone breaking up has largely disappeared. The euro has been surprisingly strong and European shares have outperformed those of the UK and US.

It is the job of financial markets to look forward, not back, and investors' current verdict is that growth will return. 2014 is the year when we will find out if this renewal of confidence in Europe's future is justified or not.

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Global Insight

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Asian M&A increasingly upbeat

First-quarter deal volumes show a continued upward trend in M&A activity in Asia.

M&A activities in Asia appear to be increasingly promising as the global economy recovers and asset price volatility eases, according to many bankers and private equity (PE) practitioners.

Total M&A deal value generated in the Asia-Pacific region (excluding Japan) reached US$403.4bn in 2013, up 15% on 2012.

Singapore, Malaysia and Indonesia recorded aggregate deal activity valued at US$59.4bn spread across 670 deals in 2013. Of these, Singapore – a useful barometer for the region as a whole – registered a total of 286 deals valued at US$28.1bn.

Cross-border deals accounted for US$24.5 billion in 2013, spread across 204 deals, with inbound deals contributing 61% of the total. There were 82 domestic deals, valued at US$3.69 billion.
For the first quarter of 2014, deal value for Asia-Pacific totalled US$101.6bn, with inbound M&A deals worth US$23.5bn and outbound M&A worth US$14.1bn. According to industry observers, a significant portion of Singapore deals are expected to materialise in 2014.

Control buys to drive acquisitions
Some PE practitioners are expecting acquisitions to focus more on control buys, as opposed to minority investments. Former frontier markets in South-East Asia, with their growing economies, will continue to rank as a top priority on investors' agendas. However, dealmakers' preference for deals in the mid-market is likely to continue. Deals involving small to medium-sized enterprises are typically more sought after due to their growth potential and likelihood to produce higher returns.

A study by Accenture suggests that companies tend to create more shareholder value when they buy businesses during early bull markets or markets in the initial phases of an economic recovery.

Corporate buyers
Corporate acquirers who have been inactive in the past couple of years, building up cash reserves, may well revive their M&A appetite. This is likely to be further encouraged by the improved financing environment and strategic objectives to beef up operations. With IPO possibilities remaining challenging, PE investors looking to exit may find opportunities through trade sales to corporate buyers.

Many industry observers expect Asian buyers to be increasingly active over the next 18 months, both in intra-Asia and outbound M&A. There is also the possibility of a pick-up in Japanese M&A activity, although due to its limited growth, Japanese corporates are largely looking outside the country.

Emerging sectors

There is a steady trend towards the consumer space, encouraged by regional demographics and demand for consumer goods among the younger generation across the Asian region. Consumer sector M&A ranked third, with US$16.3bn worth of transactions, in the first quarter of 2014 after real estate (US$19.7bn) and energy, mining and utilities (US$17.9bn). The energy space will remain popular and is likely to see continued strong investment in the year ahead, despite the political risks and regulatory hurdles involved, especially in the developing markets. The telecommunications, media and technology sector is touted as the up-and-coming favourite among PE and corporate acquirers.

The China factor

China's government considers M&A an effective means to strengthen company resource integration, competitiveness, excess capacity allocation and structural improvements. It has recently embarked on rules changes at the State Council level to support M&A activity. These changes focus on improvement of government systems and regulations so as to streamline and simplify the processes and procedures involved for most types of M&A. For example, when listed companies (other than 'back-door' listed companies) are involved, pre-approvals will no longer be required and the registration process will be simplified. Qualified companies will be allowed to finance M&A activities through equity and debt issues. M&A financing through PE, venture, and other funding classes are also being encouraged. With the exception of certain industries, private capital investment through M&A will be encouraged and state-owned parent companies will also be allowed to receive private capital and inject funds into private companies.

With these new developments, we expect to see greater M&A activity involving Chinese companies and are beginning to see more state-owned enterprises making acquisitions in overseas capital markets.

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Global Insight

April 2014

News briefs

A round up of tax, regulatory and business issues from around the world.

New tax treaty between Ukraine and Cyprus

A new double taxation treaty between Ukraine and Cyprus came into force on 1 January 2014. The new agreement replaces the former Cyprus-USSR treaty and provides for higher rates of withholding tax in relation to dividends, interest and royalties.

For dividends, the withholding tax rate will be limited to 5% if the beneficial owner holds at least 20% of the capital of the paying company or has invested at least €100,000 in the company. If these conditions are not met the withholding tax is limited to 15%.

The maximum rate of withholding tax on interest under the new agreement is 2%.

Royalties paid in respect of copyright of scientific research, patents, trademarks, secret formulas, processes, industrial or commercial know-how are taxed at 5%. Other types of royalties including for literary and musical compositions, films and software are taxed at 10%.

The new treaty retains the beneficial arrangements regarding capital gains. Capital gains realised by a Cyprus-resident company derived from the disposal of shares in a Ukrainian company will continue to be exempt from tax in Ukraine. In Cyprus, there is no tax on the disposal of shares unless the gain is derived from real estate in Cyprus. Therefore, the use of Cypriot companies will continue to be an ideal way of holding real estate in Ukraine, as it will effectively allow property there to be disposed of tax-free.

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Turkey introduces compulsory independent auditing
Independent audits are mandatory for certain categories of companies in Turkey, as of 1 January 2014. These include those regulated by the Capital Markets Board of Turkey, companies operating under banking and supervision agency regulations, insurance companies, members of the Istanbul Gold Exchange and owners of television channels.

Other companies, which in 2012 and 2013 met a minimum of two of the following three criteria, will also be subject to an independent audit.
1. Total assets of at least 75m Turkish lira
2. Annual net sales equal to at least 150m Turkish lira
3. 250 employees or more
Such companies were required to appoint an independent auditor at the General Assembly held at the end of March 2014.

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Members of Sephardic community to be granted Spanish citizenship
The Spanish Ministry of Justice has prepared a draft bill proposing to allow eligible Sephardic individuals to apply for Spanish citizenship – regardless of their existing nationality or place of residence.

Successful applicants will benefit from Spain's membership of the EU, including the free movement of persons, goods, services and capital within the union.

Applications should be ideally submitted within two years of when the law comes into effect. Sephardic individuals already in the process of applying for Spanish citizenship may use this new procedure, although they will need to expressly request it and provide the necessary documentation.

The Sephardic community has long held a close connection with Spain, being descendents of Jews from Sefarad (Spain in Hebrew).

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World Trade Centre to open in Gibraltar

The £45m Gibraltar World Trade Centre is set to open at the end of 2015. It will be the largest single office building on the Rock, offering space to businesses of all sizes and putting Gibraltar even more firmly on the global business map.

The development will be the perfect entry point for new companies looking to benefit from a legal system based on UK common law, low business-friendly taxation, no capital gains tax or VAT, little red tape, EU membership and regulation, OECD White List status and a strategic geographic position.

Over the last five years, Gibraltar's economy has flourished despite global economic turmoil. Its GDP is estimated to have grown by 35% and it is ranked among the top 20 countries globally for growth.

Gibraltar's attractive fiscal and regulatory environment continues to attract international businesses and the new World Trade Centre will enhance its standing.

Benady Cohen & Co works with the government to promote the jurisdiction on the international stage and provides a range of value-added services – both established and new.

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