Mauritius Economy: BEPS, IPPAs, DTAs & More!

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Taxlinked (TL): Besides geographic proximity, how has Mauritius established itself as an International Financial Centre (IFC) of choice for India and Africa-bound and outbound investments and businesses?

Kamal Hawabhay (KH): The Mauritius IFC was established in 1991 and is now a mature and well-established IFC known globally for several years now as the most favoured hub for inbound investments in India. Additionally, Africa-bound investment funds and SPVs today routinely access Africa through the efficient & cost-effective Mauritius IFC to minimize risks inherent in many African states and maximize returns to investors.

Mauritius has been the ideal gateway to India since over two decades now because of the certainty of its fiscal and regulatory laws coupled with the absence of foreign exchange control and the rule of law that all businessmen and investors primarily look for. The principal reasons behind the success of Mauritius include: 1) the favourable treaty that it has with India; 2) the considerable expertise and knowledge of Indian foreign institutional investment and portfolio laws, among others, that Mauritius professionals have acquired over time; 3) the commonality of language & culture; 4) lesser costs & greater ease of doing business, and: 5) very importantly, an impartial judiciary system of high standard, relative quick delivery of justice & favourable time zone at GMT +4.

The strategic location of Mauritius allows it to rightly position itself as the gateway for investment in India and Africa. Africa has great unexploited potential and has steadily been attracting billions of FDI. Mauritius has several well-established tax treaties with 15 African countries that include Uganda, Kenya, Tunisia, South Africa, Botswana and Swaziland and awaits ratification with several others. Mauritius is also a member of the Common Market for Eastern and Southern Africa (COMESA) and the South African Development Community (SADC). Mauritius thus provides India an efficient platform to do business in or invest in the African market.

Mauritius was identified as a favourable and tax efficient platform for African investments in the World Investment Report 2010 and has always been on the white list of the OECD, confirming its standing as an IFC of substance. It is worth emphasizing that Mauritius is first and foremost an African country but, being an island, it is insulated from the inherent risks of continental Africa.

Other than geographic proximity, the rationale for accessing Indian and Africa via Mauritius is as follows:

1. **Politically Stable** - Democratic independent state in line with UK Westminster model.
2. **International Recognition** - 1st in the Mo Ibrahim Index of African Governance 2015, ranked 1st in Africa by the World Bank Doing Business 2016 & the Global Competitiveness Index 2015-

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2016. The A.T. Kearney Global Services Location Index 2016 ranks Mauritius 3rd in Africa.

3. Updated Regulatory and Legal Framework – Old laws have been replaced by a new framework that ranges between 1 to 10 years old and is constantly updated. Hybrid legal system being a mix of Anglo-Saxon common law and the Code Napoleon. We understand both English & French-speaking Africa!

4. Stable, Impartial and Tested Legal Platform -Ultimate court of appeal in Mauritius is the UK Privy Council affording more comfort and appeal to sophisticated international investors.

5. Appropriate Supervision of Market Participants – By Bank of Mauritius for naming matters & the Financial Services Commission, the regulator for all non-banking matters.

6. Ease of Doing Business - 100% foreign ownership is allowed & no exchange controls.

7. Types of Entities Available – Private and public company with limited liability & limited by shares, limited partnership, general partnership, limited life company, trust, foundation, foreign company registered in Mauritius.

8. Anti-money Laundering Framework - Strict AML/CFT laws since 2002 including the Financial Intelligence Unit, which is the central Mauritian agency for the request, receipt, analysis and dissemination of financial information regarding suspected proceeds of crime and alleged money laundering offences, as well as the financing of any activities or transactions related to terrorism to relevant authorities.

9. Confidentiality - Statutory protection of legitimate confidentiality. Note that no secrecy laws are in force in Mauritius.

10. Funds Friendly Legislation – The law is geared to promote the set up of funds. The Securities Act 2005 provides for the set-up of flexible schemes such as Professional, Specialised or Expert Funds. Sophisticated investors benefit from extensive exemptions from compliance requirements.

11. An IFC of Substance – Benefits under the extensive tax treaty (DTA) network is contingent on the funds having a local tax residence, subject to meeting certain conditions under the law. The conditions are designed to ensure that the place of effective management and control is the IFC.

12. Stock Exchange of Mauritius ("SEM") - The SEM is a multi-asset class stock exchange (market cap of about $7bn) and allows foreign listing of equities and bonds in foreign currency. SEM is a member of the World Federation of Exchanges, a Cayman Islands Monetary Authority Approved Stock Exchange, and is designated by United Kingdom's HMRC as a "recognised Stock Exchange" for Inheritance Tax purposes. UK pension schemes are thus permitted to hold securities listed on the Official Market of the SEM, giving companies and funds listed on SEM access to a larger market of sophisticated, well-capitalised investors.

13. Bourse Africa - An international multi-asset class exchange from Mauritius that currently offers trading on three market segments viz., commodities, currencies and equities providing African and international market participants with an efficient market for risk management, trading, investing and capital raising needs. The exchange offers a state-of-the-art electronic trading platform with efficient clearing and settlement systems.

14. DTA Network - Mauritius currently has 43 double taxation treaties that have been signed and ratified, out of which 15 are with African countries.

15. Maximisation of Returns - The DTA network may be utilized to maximise return on investments achieved through 100% exemption of capital gains, stamp duty & reduced withholding taxes.

16. Mitigation of Investment Risks – Investment and business risks in African countries may be mitigated through bilateral agreements the IFC has with 20 African member states. Benefits include free repatriation of investment capital and returns; most favoured nation rule with respect to the treatment of investment, and; compensation for losses in case of war or armed conflict or riot, etc. This makes Africa-bound investment funds more attractive to institutional investors.

17. Mauritius International Arbitration Centre - The LCIA -MIAC Arbitration Centre is a joint venture between the well-known and respected UK-based LCIA. International arbitration services are thus available in Mauritius. International dispute resolution can now be expeditious & cost-effective under internationally agreed rules.

18. Structuring of Funds - Both open and closed-end (PE) funds may be set up as a company or LP. Reduced compliance applies to a closed-end fund, which offers private placements to sophisticated or expert investors. Easier to set up, cost-effective, entry and exit strategy of investors are eased and investment managers may draw carry interest tax free if structured correctly.

19. Adequate Pool of Qualified Professional Service Providers and Trained Staff - The Big 4,

medium-sized and smaller accounting firms, international law firms and international banks and duly licenced and regulated independent fund administration firms are part of the ecosystem. Trained staff whether CA(SA)s, ACCAs, ACAs, ICSAs, TEPs, etc., are available at cost-effective rates.

20. **The Continental Connection** – The IFC is a natural platform for private equity investments into Africa as Mauritius is a member of the major African regional trade organizations. Mauritius is the only IFC that offers a combination of treaty network benefits and the usual tax and non-tax benefits of a mature IFC, along with access to several preferential trade agreements.

Today, Mauritius is home to some of the leading actors in the African private equity space including Actis, Helios and the African Development Bank, to mention but a few. The African Development Bank currently houses more than 50% of its African private equity structures in Mauritius. Currently, more than 900 Global Funds operate from Mauritius with an estimated NAV $70+ billion. Investing directly into the relevant investment recipient country in Africa may offer rewards but these are more likely than not mitigated by the challenges inherent in Africa leading to unwanted consequences in the long term. The choice of jurisdiction for a private equity fund operating in Africa is influenced by many factors relating to the overall operating environment.

Mauritius is clearly the front-runner IFC for Africa because it has created a business-enabling environment that is internationally competitive combined with cost-effective competence and infrastructure.

TL: What sorts of Investment Promotion and Protection Agreements have been signed between African nations and Mauritius? In your opinion, how are these more important than tax treaties?

KH: Mauritius has signed Investment Promotion and Protection Agreements (IPPAs) with 20 African member states, notably those with Madagascar, Ghana, Burundi, Mozambique, Guinea Republic, Cameroon, South Africa, Mauritania, Comoros, Benin, Rwanda, Swaziland, Botswana, Senegal, Kenya, Zimbabwe, Chad, Republic of Congo, Tanzania and Nigeria.

IPPAs typically offer the following protection to investors from the contracting states:

1. Free repatriation of investment capital and returns;
2. Guarantee against expropriation without compensation for the Mauritian entity;
3. Most favoured nation rule with respect to the treatment of investment;
4. Compensation for losses in case of war or armed conflict or riot, etc., and;
5. Arrangement for settlement of disputes between investors and the contracting states.

Several African countries are still unfortunately prone to political risks or sudden changes in government policies. Investing via the Mauritius hub assists to ward off such risks. The IPPA therefore makes Africa-bound investment funds more attractive to institutional investors. Tax treaties allocate taxing rights to contracting states while IPPAs operate to protect the investment, which is arguably more important than any resulting potential tax charge.

TL: South Africa and Mauritius signed a new tax treaty in 2015. What have been some of its major features? For example, does it facilitate the structuring and administration of South Africa outbound business and investment into the rest of Africa via Mauritius?

KH: In May 2015, Mauritius signed and ratified the new tax treaty with South Africa but also a Memorandum of Understanding (MoU), which clarifies the Place of Effective Management (POEM) criterion used in the new treaty. The date of entry into force of the DTA and the MoU is 1 January 2016.

Despite certain material changes to the DTA, as discussed below, for many investors making use of Mauritian-based structures, it should be "business as usual," provided they abide by certain new requirements in the treaty.

The amendment that caused the most concern is the one to Article 4 of the old DTA, which introduces a tax residence tie-breaker test for a juristic person when there is a case of dual residence. POEM is now replaced with a mutual agreement procedure ("MAP") known as the "Competent Authority Procedure" (CA) between the competent authorities of the contracting states. The MoU attempts to address this concern by clarifying the factors that the CAs will consider when

endeavouring to settle the question of dual residence thereby restoring certainty to a large extent. There are justified criticisms against the MoU but, in my view, we are still better off with it than without.

The other principal changes are as follows:

1. The new DTA maintains the dividend withholding tax at 5% for shareholding of least 10% but favourably **reduces** the rate **from 15% to 10%** in all other cases.
2. The reduction to 0% in respect of interest paid to a Mauritius company **remains intact** in the new tax treaty for interest on debt instruments listed on a stock exchange like the JSE, while all other types of interest is now subject to a maximum source rate of tax of 10% (previously 0%).
3. South Africa has introduced an interest withholding tax of 15% in 2015 on all SA source interest payments to non-residents. The new DTA will **reduce** the interest rate from 15% to 10% in respect of Mauritius companies.
4. The DTA **reduces to 5%** (previously 0%) the flat South African withholding tax rate of 15% applicable to any royalty, from a South African source, paid by a South African company to a Mauritius company provided the royalty is beneficially owned by the Mauritius company.
5. The new DTA leaves unchanged the mode of taxation of capital gains on movable property but now allots the taxing right on capital gains that arise from the sale of shares in a South African company that is "property rich" to the source country.
6. Art 25 of the new DTA also allows for more comprehensive exchange of information but this is in line with world trends such as FATCA and CRS.

It is a fact that zero withholding tax rates in tax treaties are no longer sustainable in the current age. I have therefore refrained from drawing any comparison in this respect with the old treaty.

In the case of a Mauritius company held 100% by non-South African tax resident shareholders who invest or do business in South Africa, the withholding tax hurdles are now higher than previously in the case of interest at 10% and royalty at 5%. Furthermore, capital gains tax on property rich company is now taxable in South Africa while dividend withholding tax is maintained at 5% and there is no tax in South Africa on capital gains arising on disposition of movable property in South Africa in the absence of a permanent establishment in that country.

Having said that, it is also a fact that the withholding tax rates on dividends, interest and royalty provided for in the new DTA are still lower than the prevailing South African withholding tax rates. Foreign investors would thus still be better off investing into South Africa via Mauritius.

In the case of a Mauritius company held 100% by South African tax resident shareholders who invest or do business in the rest of Africa, no Mauritius withholding tax on dividend, interest or royalty will apply on any remittance of such income streams to South Africa or to any other country, on behalf of the beneficial owners. Mauritius does not tax capital gains currently. Of course, CFC Rules in South Africa on holdings by South African tax residents of 50% or more is an issue that needs to be mitigated.

Accordingly, in my view, the changes are more of a hindrance to inward businesses/investments into South Africa than to the outward ones. The amendments are thus paradoxically and definitely quite favourable for South African companies using Mauritius as a gateway for foreign investments/businesses.

It is however critical that POEM of Mauritius companies remains unambiguously in Mauritius.

TL: How has Mauritius tackled the BEPS package and its 15 Actions? More specifically, what role do you see for Mauritius when it comes to compliance with Action 5 ("Harmful Tax Practices")?

As in several other countries, BEPS is also hotly being debated and alternative solutions considered in Mauritius. We are still a distance away from conclusively "tackling" the BEPS package of 15 actions but then so are most, if not all, countries.

Given the nature and type of business that we generally have in the Mauritius IFC, Actions 2, 3, 4, 5, 6 and 15 are the most pertinent for us.

The challenges that we face in Mauritius include the following:

1. Need to redefine what constitutes acceptable tax planning;

2. The IFC has to accelerate its restructuring and to align business substance and value creation with the intended tax outcome;
3. Mauritius has to reinforce its image as a clean jurisdiction so as to attract investors, and;
4. Negotiation of treaties in the post-BEPS era must be considered.

Action 5 deals primarily with:

1. Preferential regimes used for artificial profit shifting; and
2. The lack of transparency in tax ruling relating to preferential regimes.

For Mauritius, the non-IP Regime is more relevant and covers seven so called preferential regimes, of which I will focus briefly on the following more relevant regimes:

1. Headquarters regimes
2. Fund management regimes
3. Holding company regimes

Headquarters Regimes:

The OECD report considers that the substance-enhancing and core income-generating activities in a headquarters company could include the taking of relevant management decisions, incurring expenditures on behalf of group entities and co-ordinating group activities.

Fund Management Regimes:

Core income-generating activities for a fund manager have been identified as including, amongst others, taking decisions on holding and selling of investments, calculating risks, taking decisions on currency or interest fluctuations and hedging positions, and preparing relevant regulatory or other reports for government authorities and investors.

Holding Company Regimes:

OECD recognizes that such holding companies may not in fact require much substance in order to exercise their main activity of holding and managing equity participations save that they comply with corporate law requirements and minimum substance activities to perform such activities. The report mentions people on the ground and premises.

In other types of holding companies, the BEPS report explains that the substantial activity requirement should require taxpayers to engage in the core activities of the company.

Concerns identified by the Action 5 report include inability to identify the beneficial owner of dividends and the granting of undue treaty benefits. The law in Mauritius has always required the identity of immediate and ultimate beneficial owners of corporations to be known and treaty benefits are granted only upon compliance with stipulated substance conditions.

In the area of transparency, compulsory spontaneous exchange of information on principally transfer pricing related rulings is identified. Mauritius has no detailed transfer pricing rulings and adopts an arm's length approach that gives authority to the Director General of the Mauritius Revenue Authority to make adjustments if he thinks fit to do so.

Mauritius has undergone in June 2010 a combined Phase 1 and 2 peer review by the Global Forum on Transparency and Exchange of Information for Tax purposes. All elements, save for one, were found to be in place, some needing improvements. A further review of the amendments made to the legal and regulatory framework for transparency and exchange of information pursuant to the combined Phase 1 and 2 review was undertaken by the Global Forum in August 2011. All elements were determined to be in place, some requiring improvements.

A second review was undertaken in February 2014 by the Global Forum of further amendments brought to address recommendations made earlier in the first supplementary review report of the Global Forum.

The report concluded that Mauritius has implemented all recommendations of the Global Forum and achieved an overall rating of "largely compliant." Exchange of information therefore is not an issue.

Given that substance is key with respect to Action 5, as pointed out above, let's consider what Mauritius has done and is doing in this respect.

Mauritius has from the beginning of its IFC in 1991 been a tax treaty centric jurisdiction which

required that at least a minimum set of substance conditions be present in the local operations of corporations to obtain Mauritius tax residency status for tax treaty benefits purposes. These substance conditions are that the corporation:

1. Has at least 2 directors, residents in Mauritius, who are appropriately qualified and are of sufficient calibre to exercise independence of mind and judgement;

2. Maintains, at all times, its principal bank account in Mauritius;

3. Keeps and maintains, at all times, its accounting records at its registered office in Mauritius;

4. Prepares its statutory financial statements and causes to have such financial statements to be audited in Mauritius, and;

5. Provides for meeting of directors to include at least 2 directors from Mauritius.

Additional substance requirements are in force in Mauritius since 1 January 2015 to mitigate BEPS.

A new compulsory requirement is that a corporation that is authorised/licensed as a collective investment scheme, closed end fund or external pension scheme, is administered from Mauritius and at least one of the following criteria must be adopted by Mauritius-based corporations:

1. The corporation has or shall have office premises in Mauritius; or

2. The corporation employs or shall employ on a full time basis, at administrative/technical level, at least one person who shall be resident in Mauritius; or

3. The corporation's constitution contains a clause whereby all disputes arising out of the constitution shall be resolved by way of arbitration in Mauritius; or

4. The corporation holds or is expected to hold, within the next 12 months, assets (excluding cash held in bank account or shares/interests in another corporation) that are worth at least USD 100,000 in Mauritius; or

5. The corporation's shares are listed on a securities exchange licensed by the Financial Services Corporation; or

6. The corporation has or is expected to have a yearly expenditure in Mauritius, which can be reasonably expected from any similar corporation, which is controlled and managed from Mauritius.

By contrast, it is only on 1 January 2014 that a new Decree entered into force in the Netherlands, which codifies the existing administrative guidance on substance requirements for companies engaged in inter-company financing and/or licencing activities and for Dutch companies that claim treaty benefits. Well, very similar substance requirements have been in effect in Mauritius since 1991 and were enhanced in 2015!

The view is taken in Mauritius that the existing substance conditions will go a long way to address Action 5 concerns and requirements. Nevertheless, the interaction of Action 5 with other Action plans such as exchange of information, treaty abuse, neutralize effect of hybrid mismatch, ring fencing and CFC rules are still being considered.

OECD itself recognizes that "Other [BEPS] measures require domestic legal or regulatory changes to take effect." In my view, most BEPS measures require such changes. The BEPS project to date has accomplished the relatively easy part of the mission, which is to get countries to agree to an objective on paper. In fact, the G20 Heads of States, meeting in October 2015 in Lima, Peru, endorsed the final BEPS reports only three days after their issue. It would have been humanly impossible for the Heads of States to appreciate the basic, technical and finer details of the voluminous 2000+ reports in just three days. Evidently, their quick endorsement was in the interest of sending a strong political signal that aggressive tax planning is out.

However, the proof of the pudding will be when these countries actually change their domestic laws and bilateral treaties in line with BEPS. This would mean general alignment of fiscal policies of a vast number of countries, which virtually means the removal of competing fiscal incentives to attract FDI, the demise of special economic zones that generally offer tax holidays, etc. It is interesting to note that BEPS allows bilateral agreements to be negotiated at the option of participating countries. It is likely that this method will be preferred as opposed to the multilateral instrument that makes sovereignty and government flexibility moot concepts.

Added to these uncertainties is the outcome of the US presidential election late this year. In February this year, Jack Lew, US Treasury secretary, accused the EU of unfairly targeting American companies in its investigation into possible corporate tax avoidance, warning it could jeopardise investment in the bloc. In the letter addressed to the President of the European Commission, Mr Lew warned that he had "serious concerns about fundamental fairness" of the EU's tax policy. Such statements say a lot about the mind set prevailing on the other side of the Atlantic and, since the overwhelming MNCs that are impacted by BEPS are American, it will be interesting to see how all

this plays out and perhaps at the end, BEPS may morph into something very different!

I think A LOT of water will need to flow under the bridge before BEPS becomes a big reality!

TL: Any other thoughts you would like to share with our community?

KH: I am concerned about negative criticisms being unfairly thrust upon the Mauritius IFC in the wake of the Panama Papers despite the fact that the International Consortium of Investigative Journalists has not revealed any Mauritius names yet and has not listed Mauritius among the IFCs found to be most used in the leaked documents.

There have been reports however about a company being re-domiciled from Bahamas to Mauritius with the foregone conclusion that this was done to avoid Ugandan taxes by making use of the Mauritius Uganda double tax avoidance treaty (DTA), which the company has denied. There is nothing illegal in this *per se* but this transaction has motivated arguments that Mauritius facilitates round tripping!

Oxfam also jumped on this bandwagon and issued a study that criticizes IFC (World Bank) for using Mauritius as a hub for 40% of its investments into sub-Saharan Africa and alleges maliciously that Mauritius is known to facilitate "round-tripping." This is utterly baseless. The regulatory framework in Mauritius has several provisions that prohibit round tripping.

Oxfam further says that sub-Saharan Africa is the poorest region in the world and it desperately needs corporate tax revenues to invest in public services and infrastructure.

The Oxfam author, on the one hand, acknowledges that these sub-Saharan countries are seriously lacking in several ways but fails to recognize that no one would pour millions of dollars in any venture or any African countries without hedging the considerable inherent and systemic risks, including currency risks present there. IFC also has to ensure an adequate IRR for its investments and has to report back! Putting so much money into a poorly developed country without investment security, without repatriation guarantee, without proper regulatory framework and where ease of doing business is a remote concept, is madness!

Another crucial fact seems to be lost on the author of the Oxfam article. This is that under any tax agreements between Mauritius and the investee countries that were used by IFC to invest in sub-Saharan Africa, the active income so generated would be taxed in the source African country and only passive income would be taxed in Mauritius! He does not seem to have considered that without appropriate risks hedge, the money would probably not have flowed to those countries and no income tax would have been raised in the first place!

The IFC rubbished the Oxfam report by saying simply that it is "flawed"!

Putting on my investigator's cap, as seems to be the fashion these days, I checked the publicly available (on Internet) credentials of the author of the blatantly malevolent Oxfam report and I discovered that he holds a Bachelor of Arts (B.A.) Journalism and Mass Communications and has been working as a Media Officer with Oxfam for only 8 months! Prior to that he worked in several other positions with an international cable network TV company, all unrelated to taxation matters!

The unbearable lightness of the Oxfam report is astounding. But then as they say, there are none so blind as those who will not see!

Views: 64