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TAX NEWSLETTER

The Finance (Miscellaneous Provisions) Act 2018 ("FA 2018") significantly amended the regulatory and tax framework applicable to companies (including global business companies) in Mauritius in order to bring them in line with the OECD's minimum standards on Base Erosion Profit Shifting ("BEPS").

The amended laws have been supplemented with tax regulations and guidance from the local regulator, the Financial Services Commission (the "FSC").

The main regulatory changes include:

(i) the abolition of global business category 2 companies ("GBC2 companies") from 1 January 2019;
(ii) the introduction of the "authorised company" from 1 October 2018;
(iii) the renaming of global business companies category 1 ("GBC1 companies") as global business companies from 1 January 2019 and the introduction of enhanced substance requirements for global business companies; and
(iv) the introduction of specific activity-related and industry-related substance requirements for companies licensed by the FSC.

This newsletter summarises the main tax changes and highlights the potential implications on doing business in Mauritius.

ABOLITION OF THE DEEMED FOREIGN TAX CREDIT REGIME

- The "deemed foreign tax credit" (or "DFTC") will be abolished with effect from 1 January 2019, save for GBC1 companies which were established on or before 16 October 2017 which can continue to benefit from the DFTC until 30 June 2021.

- By way of background, the DFTC previously enabled GBC1 companies to benefit from a "deemed foreign tax credit" equal to 80% of the Mauritius tax credit, without having to prove whether foreign tax was actually suffered. In practice, this meant that GBC1 companies were subject to a maximum effective tax rate of 3%.

- Companies can continue to claim credit for actual foreign tax suffered (unless they are claiming partial exemption – see further below).

ABOLITION OF GBC2 COMPANIES

- As mentioned above, GBC2 companies will be abolished from 1 January 2019. However, GBC2 companies established on or before 16 October 2017 will continue to be exempt from tax until 30 June 2021.

INTRODUCTION OF THE PARTIAL EXEMPTION REGIME

- The standard tax rate of 15% will be applicable to chargeable profits of all companies, whether they are domestic or global business companies. Banks will be subject to a special tax regime.

- With effect from 1 January 2019, an income tax exemption of 80% shall apply on the following streams of income:

(i) foreign source dividend, provided the dividend has not been allowed as a deduction in the source country and the company satisfies certain conditions relating to the substance of its activities;
(ii) interest, provided the company satisfies certain conditions relating to the substance of its activities;
(iii) profit attributable to a permanent establishment which a resident company has in a foreign country;
(iv) income derived by a collective investment scheme, closed end fund, CIS manager, CIS administrator, investment adviser or asset manager, licensed or approved by the FSC, provided that the company satisfies certain substance conditions as required by the FSC; and
(v) foreign income derived by a company engaged in ship, aircraft leasing provided the company satisfies certain conditions relating to the substance of its activities.

- Companies which earn foreign source income which have been subject to foreign tax in excess of 12% are expected to be able to opt to claim for credit for foreign tax instead of the partial exemption.

- The definition of foreign source income has been amended to refer to income which is not derived from Mauritius (while it previously also included income derived by GBC1 companies in relation to its transactions with non-residents or other global business companies).

- The substance conditions to be satisfied in order to claim the partial exemption are as follows:

  (i) <u>in relation to foreign source dividends</u>, the company complies with its filing obligations under the Companies Act or the Financial Services Act and has adequate resources for holding and managing share participations.

  Therefore, for pure equity holding companies, which only hold equity participations and earn only dividends and capital gains, the substance requirements are less stringent as there is less concern of such regimes being used for BEPS;

  (ii) <u>in relation to interest</u>, the company (a) carries out its core income generating activities (which includes agreeing funding terms, setting the terms and duration of any financing, monitoring and revising any agreements, and managing any risks) in Mauritius; (b) employs directly or indirectly an adequate number of suitably qualified persons to conduct its core income generating activities and (c) incurs a minimum expenditure proportionate to its level of activities.

  The substance threshold is higher in relation to debt structures (as opposed to pure equity regime). It is hoped that decisions taken by the board of directors in Mauritius will be sufficient to show that the core income generating activities are carried out in Mauritius;

  (iii) <u>in relation to ships and aircraft leasing activities</u>, the company (a) carries out its core income generating activities (which includes agreeing funding terms, identifying and acquiring assets to be leased, setting the terms and duration of any leasing, monitoring and revising any agreements, and managing any risks) in Mauritius; (b) employs directly or indirectly an adequate number of suitably qualified persons to conduct its core income generating activities and (c) incurs a minimum expenditure proportionate to its level of activities;

  (iv) in relation to fund-related activities, the substance requirements as set out by the FSC.

- The substance conditions are in line with the OECD's guidelines on substance and in particular the OECD's 2017 progress report on harmful tax practices. It is noteworthy that (except in relation to fund-related activities) the substance conditions operate independently to the FSC substance requirements, although in practice there will be some overlap. All companies (regardless of whether they are global business companies or not) are required to satisfy them.

- The Income Tax Act has also been amended to clarify that profits relating to the export of goods (which are taxable at the rate of 3%) include export of goods by companies established in Mauritius whereby the shipment of such goods is made directly by the shipper in the original exporting country to the final importer in the importing country, without the goods being physically landed in Mauritius.

- Streams of income which do not qualify for the partial exemption will henceforth be taxable at the standard rate of 15% (subject to credit for actual foreign tax suffered). Concerns have been expressed by the industry that the list of income streams that qualify for the partial exemption is too restrictive and ought to be extended to other types of foreign earned income.

- Any gains or profits (including gains which are not capital in nature) made by the disposal of securities or debt obligations by any person are exempt. Previously this exemption only applied to disposals made by global business companies. The definition of "securities" is broad and includes certain types of derivatives.

AMENDMENT OF TAX RESIDENCE TEST: PLACE OF EFFECTIVE MANAGEMENT/POEM

- A company is typically considered to be tax resident in Mauritius if it is incorporated in Mauritius or is managed and controlled in Mauritius. From 1 October 2018, a company whose place of effective management is located outside Mauritius is treated as being non-resident for tax purposes.

- There is no statutory definition of the term "place of effective management" nor (as at the date of this newsletter) any guidance by the Mauritius Revenue Authority ("MRA") as to what would constitute "place of effective management". There is no universal definition of this concept and various countries have adopted their own interpretation. According to the Commentary on the OECD Model Convention, "place of effective management" is the place where key management and commercial decisions that are necessary for the conduct of the entity's business as a whole are in substance made.

- A global business company category 1 will need to be "managed and controlled" in Mauritius for regulatory purposes. However, it may be argued that the OECD definition of "place of effective management" provides a higher threshold than "management and control". Until clear guidance is issued by the MRA on the definition of "place of effective management", there is a technical risk that a global business company, whilst being managed and controlled in Mauritius, may be treated as nonetheless having its place of effective management outside Mauritius. It is hoped that MRA's interpretation of "place of effective management" would be in line with the regulatory requirements of the FSC.

- An authorised company should be non-resident for tax purposes since it is a company whose place of effective management is required to be outside Mauritius for regulatory purposes.

BANKING ACTIVITIES

- As from year of assessment 2020/2021, Segment A and Segment B regime of taxation of banking activities will no longer exist.

- Chargeable income of banks will be taxed at 5% for chargeable income up to Rs 1.5bn and at the rate of 15% of any chargeable income in excess of Rs 1.5bn.

- In case: (i) the chargeable income exceeds Rs 1.5 billion in an income year, and the chargeable income of the base year (year of assessment 2017/2018 for a bank in operation as at 30 June 2018 or the first year of assessment for a bank whose activities started after 1 July 2018) exceeds Rs 1.5billion; (ii) the chargeable income of the current year exceeds that of the base year; and (iii) the prescribed conditions are satisfied, the bank will be taxed at 5% for chargeable income up to Rs 1.5bn, at 15% for any chargeable income above Rs 1.5 billion up to the amount of chargeable income of the base year, and at 5% for the balance.

- In case (i) the bank has a chargeable income of more than Rs 1.5 billion in an income year; (ii) the chargeable income of the base year does not exceed Rs 1.5 billion; (iii) the chargeable income exceeds that of the base year; (iv) and the prescribed conditions are satisfied, the bank will be taxed at 5%.

- As at the date of this newsletter, the relevant conditions have not yet been prescribed.

ENHANCED REGULATORY SUBSTANCE REQUIREMENTS

- FA 2018 amended the Financial Services Act to require a global business company to satisfy new substance requirements, namely that it shall, at all times carry out its core income generating activities in, or from, Mauritius by (A) employing, either directly or indirectly, a reasonable number of suitably qualified persons to carry out the core activities; and (B) having a minimum level of expenditure, which is proportionate to its level of activities.

- The FSC issued circulars on 12 and 15 October 2018 to provide guidance on the above substance requirements, with effect from 1 January 2019. Grand-fathered GBC1 companies will have until 30 June 2021 to satisfy those enhanced requirements, but from a practical point of view, early compliance is expected to be encouraged. The circulars can be accessed here:

  https://www.fscmauritius.org/media/67458/cl-on-substance-gb.pdf
  https://www.fscmauritius.org/media/67462/cl-on-core-income-generating-activities-v5.pdf

- The circulars suggest that an investment holding global business company that does not hold any other licences will be required to have a minimum local expenditure of at least USD 12,000 but no requirement to have employees.

- Global business companies which are non-investment holding companies or which have other licences (such as an asset manager licences) are required to have both minimum local expenditure and indirect or indirect employment (with varying thresholds depending on the nature of their activity).

- Interestingly, the legislation and circulars refer to direct or indirect employment. Therefore employment through a management company should be sufficient to satisfy the minimum employment requirement, although it is yet unclear for how many GBC companies an “indirect” employee may work for. The consideration of “jurisdictional” employment as opposed to entity by entity employment has been greeted favourably by management companies who employ thousands of people through management companies and who often provide a full-suite of back office services to global business companies (such as accounting, company secretarial and tax services).

- In addition, certain categories of licensees, namely Global Headquarters Administration, Global Treasury Activities, Overseas Family Office (Single), Overseas Family Office (Multiple), Investment Banking, and Global Legal Advisory Services have higher thresholds for substance requirements (including having a physical office in Mauritius, a minimum number of employees resident in Mauritius and incurring a minimum amount of annual operating expenditure in Mauritius) in order to qualify for the statutory tax holiday applicable to them.

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