

## The Finance (Miscellaneous Provisions) Act No 11 of 2018

- . Substantial changes to the Financial Services Act and the Income Tax Act, but also changes to note in the Companies Act and Foundations Act
- . Taxation of Trusts and Foundations unaffected, other than requirement for Foundations to register and trustees to keep a Register of Trusts. Also GBC's to keep customer KYC records
- . **Grandfathering Provisions** for GBL's-
  - . GBL1's & GBL2's incorporated on or before 16 October 2017 may continue until 30 June 2021 retaining tax benefits, and thereafter GBL1 is deemed a GBC, and GBL2 is deemed an Authorised Company ("AC"), but -
    - . GBC2 tax exemption shall not apply to-
      - . IP assets acquired from related parties after 16 October 2017

- . IP assets acquired from non-related parties or new IP acquired after 30 June 2018
- . income from assets or projects acquired or started after 31 December 2018
- . “foreign sourced income” for a GBL1 until 30 June 2021 is deemed to include income derived from transactions with non-residents or other Global Business entities

## Authorised Company (“AC”)

- . From 1 January 2019 if a Mauritian incorporated company with majority of shares or voting rights or beneficial interest (such as through a trust) are held or controlled by non-citizens of Mauritius, and the company obtains its business principally (majority) outside Mauritius, and its POEM is outside of Mauritius, it must apply for an AC license
- . Note that GBC2s must have no Mauritian resident ownership and do no business in Mauritius. ACs are very different. Also GBL2s could be tax resident in Mauritius having its incorporation, CMC and/or POEM in Mauritius. It relied on a tax exemption. It was only deemed non-resident for DTA participation purposes. AC,s are not tax resident in Mauritius despite local incorporation (new s73A) and likely not allowed CMC in Mauritius
- . As with GBL2s, AC’s are excluded form doing business as set out in 4<sup>th</sup> Schedule to the Financial Services Act (financial, management, nominee, administration, director, trustee, CIS manager)
- . ACs need a registered agent which must be a Mauritian management company, must furnish annual financial summaries and file annual tax returns to MRA. Annual license fee of USD 350. Will not be a cheap company to maintain

## Global Business Company (“GBC”)

- . From 1 January 2019 if a Mauritian incorporated company with majority of shares or voting rights or beneficial interest (such as through a trust) are held or controlled by non-citizens of Mauritius, and the company obtains its business principally (majority) outside Mauritius, it must apply for a GBC license. This means-
  - . Mauritian residents (but not citizens) can no longer own or use a domestic Mauritian company where the majority of the origin (not source) of the revenue is from outside of Mauritius. (Note: Does this apply to a domestic company that holds the shares in a GBC? Is this an oversight or a deliberate opportunity to use domestic companies?)
  - . GBC must conduct its core income generating activities-
    - (i) From or in Mauritius,
    - (ii) Employing directly/indirectly a suitable number of employees (directly or indirectly) suitably qualified to carry out the core activities,
    - (iii) Have a minimum level of expenditure appropriate to its activities,

(iv) Be managed and controlled from Mauritius, and

(v) Be administered by a management company

. "managed and controlled" in Mauritius. Highly indicative factors include –

. at least 2 Mauritian resident directors of sufficient calibre

. at all times maintain its principal bank account in Mauritius

. Keep and maintain accounting records in Mauritius at its registered office

. prepare and audit financial statements in Mauritius

. Mauritian board meetings to include at least 2 Mauritian resident directors

(Note: This is not aligned to the international meaning of Central Management & Control "CMC")

. GBC is subject to a 15% company tax rate, with exception that "export of goods" activities is subject

to a 3% tax rate. So any sale of tangibles as principal solely outside of Mauritius qualifies for 3% rate, but not any services or value added activities in relation thereto (e.g. agency, procurement, marketing, distribution, sales agency, transport, logistics, management services, or any other activity where GBC does not buy and sell tangibles as principal)

- . subject to compliance with a “substance” requirement, a GBC may claim an 80% partial tax exemption on the following exclusive types of foreign originated income –
  - . foreign interest (excluding banks)
  - . foreign dividends
  - . profits of a foreign permanent establishment
  - . foreign fees and profits of a FSC licensed CIS scheme, closed end fund, CIS Manager, CIS administrator, investment advisor or asset manager
  - . shipping and aircraft leasing
- . 100% exemption available for –

- . 5 year exemption for Mauritian resident FSC approved individual asset manager or fund manager, managing assets of USD100 million
- . Interest paid by GBC to foreign resident out of foreign sourced income (no 15% TDS)
- . Royalties paid by a Mauritian company out of foreign sourced income (no 15% TDS)
- . Profits from sale of gold, silver and platinum held for continuous period of 6 months by any person
- . Income derived from registered owner of a local vessel, including chartering
- . Income received by registered owner of local vessel registered in Mauritius arising from deep sea international trade
- . 5 year exemption on provision of health services, where registered with BOI under Investment Promotion Act until 2025
- . An exemption on income of person (or a company) licensed under the Captive Insurance Act 2015, subject to substance requirements
- . 8 year exemption for company issued with a Global Headquarters Administration License by FSC

- . 5 year exemption to a company issued by the FSC with any of the following –
  - . Global Treasury Activities License
  - . Global Legal Advisory Services License
  - . Overseas Family Office (single) license
  - . Overseas Family Office (Multiple) License
- . Individual non-citizen of Mauritius or a company wholly owned by non-citizen of Mauritius investing USD25 million in Mauritius as approved by BOI
- . 8 year exemption for company involved in innovation-driven activities for intellectual property assets developed in Mauritius
- . 8 year exemption for company deriving income from manufacture of pharmaceutical products, medical devices and high tech products
- . 8 year exemption for company registered with Economic Development Board (“EDB”) to operate a food processing plant in Mauritius
- . 5 year exemption for property developer or project financing institution in collaboration with Mauritius Africa Fund developing special economic zones

- . 8 year exemption for company registered with EDB engage in manufacturing of automotive parts in Mauritius
- . 8 year tax exemption on income derived by a person from any activity in Mauritius under the Sheltered Farming Scheme set up by Food & Agricultural Research & Extension Institute
- . 80% partial exemption requires demonstrating "substance" –
  - . certain minimum full-time dedicated employees and minimum annual expenditure in Mauritius, which as per FSC Circular 12 October 2018 as a guideline –
    - . for passive investment holding GBC (excluding IP rights) – no employees and USD 12000 annual expenses
    - . for active/trading GBC –
      - . 1 employee for turnover up to USD 100m
      - . 2 employees for turnover of more than USD 100m
      - . USD 15000 annual expenses

- . CIS Manager/Asset Merger
  - . 1 employee for up to USD 100m turnover
  - . 2 employees for USD 100 – USD 500m
  - . 3 employees or more where more than USD 500m
  
- . Investment Advisor
  - . 1 employee and USD 30 000 annual expenses
  
- . Other
  - . 1 employee and USD 25 000 annual expenses
  
- . General expense allocation difficulties

Where a GBC has 3% taxable income, 80% partial exemption income and 15% taxable income, what are rules for apportioning deductible expenses of a general operating nature?

## What to do with existing GBL2's after 30 June 2021 or before?

- . Convert to a GBC. An appropriate option for passive investment holding company with active subsidiaries, which can include other GBCs, and can leverage off existing substance of an operating GBC or GBL1
- . Redomicile GBL2's to another jurisdiction (such as Seychelles, Hong Kong, BVI, Cayman Islands, England, Ireland, Dubai), but may then keep compliance, accounting, administration, all back-office functions and bank account administration in Mauritius, but insure that CMC stays outside of Mauritius.
- . For GBL2's redomiciled or its assets distributed to a new company elsewhere, consider feasibility of having POEM in Mauritius but not CMC. There must be careful Delegation of Authority Protocols to distinguish between CMC functions (in redomiciled country) and POEM functions in Mauritius.
- . Given cost, time zone, logistics and infrastructure, Mauritius can still promote itself to SA Beneficial Owners as an attractive location, but not for ACs and for GBCs only if tax incentives apply. **In Mauritius "one size does not fit all" anymore**
- . Changing to an AC is usually not a good option

## Understand the differences between CMC and POEM

### **POEM**

Operational control by executive employees who “call the shots” on high level on-going activity

See SARS Interpretation Note 6 (Issue 2) dated 5 November 2015  
[www.sars.gov.za/legalcounsel/legaladvisory/interpretation notes/numbers1-20/IN6](http://www.sars.gov.za/legalcounsel/legaladvisory/interpretation%20notes/numbers1-20/IN6) (Issue2)

### **CMC**

The highest level of decisions conducted usually by the board of directors, dealing with determinations on issues of company vision, strategy, corporate actions, policy and shareholder requirements.

MRA and FSC seem to rely on majority Mauritian resident directors/ Mauritian bank account/ Mauritian based accounting records as the “tick the box” test, but **this is not aligned to international case law** (UK and Australia in particular), and it is regrettable that MRA has no official guideline or interpretation note.

SARS IN6 (Issue 2) is aligned with the official OECD guideline on the meaning of POEM

## **Relevant Tax Law Amendments in South Africa during 2018**

### Change to donor "tax-back" rules on revenue

#### Currently

If in consequence of a gratuity made by a SA resident ("the donor") to non-SA resident (e.g. GBC or Trust) income is earned by such non-resident or a consequential party ("the donee"), such income is deemed to be income of the donor. (s7(8))

But if the income would have been exempt in SA had the donee been a SA taxpayer, then it is also exempt in hands of the donor. (s7(8))

#### Note

Foreign dividends are exempt from SA tax if recipient holds 10% or more of shares and voting rights of the foreign company paying the dividend (s10B(2))

#### Effective 1 March 2019

Must disregard that the donee's income would have been exempt under s10B(2) where the donee held more than 50% (alone or together with other "connected persons" to the donee) of the foreign company paying the dividend, and the donor or a "connected person" to the donor

is a connected person to the donee. Result is the beneficiary is taxed (up to 45%) on distributions

### Change to taxation of revenue distributions by foreign trusts to SA resident beneficiaries

#### Currently

s25B(2A) implies that where a foreign trust distributes capital to a SA beneficiary and that capital arose from exempt income in a previous year had the trust been a SA tax resident, then that distribution will also be exempt in the hands of the SA beneficiary

#### Note

Under S10B(2) if the trust received dividend income in a previous year where it had at least 10% shareholding in the foreign company paying the dividend, had it been a SA tax resident it would have been exempt from tax on the dividend, and accordingly the distribution is exempt for the beneficiary

#### Effective 1 March 2019

Must disregard that the trust's income would have been exempt under s10B(2) where trust held more than 50% (alone or together with connected persons to the Trust) of the foreign company paying the dividend. Result is a 20% tax on dividends for beneficiary

## Change to donor "tax back" capital gains

### Currently

To the extent that capital gains realized by a non-resident ("donee") arise from a gratuity from a SA resident ("donor"), the capital gain is deemed to accrue in the hands of the donor, and if it would have been exempt in hands of donee, then it is also exempt in hands of donor

### Note

Under para 64B(1) and (4) (8<sup>th</sup> Schedule) where a capital gain is realized on sale of shares in a foreign company where the interest held was at least 10% of the foreign company, held for at least 18 months, sold at fair market value to a foreign person who is not connected person, then the capital gain is exempt from capital gains tax ("CGT")

### Effective 1 March 2019

Must disregard that the donee would have been exempt from CGT under para 64B(1) or (4) where donee held more than 50% (alone or together with connected person to the donee) of the foreign company in which shares were sold, and the donor, or a connected person to the donor, is a connected person to the donee. Result is that CGT of up to 18% is payable by individual donor

## Change to taxation of capital distributions by foreign trusts to SA resident beneficiaries

### Currently

Para 80(3) implies that where a foreign trust distributes capital to a SA beneficiary and that capital arose from exempt capital gains in a previous year had the trust been a SA tax resident, then that distribution will also be exempt in the hands of the SA beneficiary

### Note

Para 64B(1) and (4) (8<sup>th</sup> Schedule) (Same as above)

### Effective 1 March 2019

Must disregard that the Trust's capital gain would have been exempt under para 64B(1) or (4), where the Trust held more than 50% (alone or together with connected persons to the Trust) of the foreign company paying the dividend. Result is that up to 18% CGT for individual beneficiary (36% for company or SA trust) on the capital distribution.

## Change to the "Controlled Foreign Company" ("CFC") definition

### Effective 1 January 2018

s9D(1) amended to include in CFC definition any foreign company whose financial results are reflected in the consolidated financial statements of SA resident holding company arising from IFRS 10 (arising from control)

## Effect of the Multilateral Instrument ("MLI") on Mauritian Double Taxation Agreements ("DTAs")

- . The MLI arises from the Base Erosion and Profit Shifting ("BEPS") Action Plan comprising 15 Actions developed by the OECD
- . Action 6: Preventing Granting of Treaty Benefits in Inappropriate Circumstances
- . Action 13: Guidance on transfer Pricing Documentation and Country-by-Country Reporting
- . Action 15: Development of an International Instrument to assist countries with implementing BEPS and amend bilateral tax treaties
- . MLI, whilst not being a comprehensive multilateral tax convention, serves as an instrument to quickly facilitate the automatic amendment of bilateral DTAs to align with the BEPS Actions, and gives signatories various elections to apply in relation to its DTAs with other countries
- . On 7 June 2017 67 countries signed the MLI. Mauritius signed on 5 July 2017
- . Signatories have 3 minimum compulsory changes to its DTAs with other MLI signatories-

- . DTA intention and purpose clause must state that the DTA shall not be used to create opportunities for non-taxation or reduced taxation through tax evasion and avoidance, including through treaty-shopping arrangements
- . incorporation of either a Principal Purpose Test ("PPT"), either with or without a simplified Limitation of Benefits ("LOB") clause. Or a detailed LOB clause
- . include a Mutual Agreement Procedure ("MAP")
  
- . Mauritius has elected the PPT for now. The meaning of PPT should be clearly understood
- . Use the OECD MLI Matching Database available at <http://www.oecd.org/ctp/treaties/mli-matching-database.htm>

## **Identifying some of the Activities that get no Mauritian Tax Incentive**

As from 1 January 2019 any GBC with proper substance in Mauritius and applying transfer pricing compliance is subject to 15% company tax on (without limitation) all of the following activities-

- . **E-commerce**: development, sale and licensing of any intangible asset, as well as all services such as digital marketing, design, point-of-sale, advertising, search engine optimization, consultancy, installation, maintenance
- . **Financial Services**: All non-CIS related activities involving fund management and any financial service not covered by the 80% partial exemption or without a banking license, including insurance, currency trading and management, commodity and financing structures, venture capital services, debt factoring, private equity, asset leasing
- . **All trading in tangibles-related value-added services**: Including selling (other than as principal), distribution, marketing, agency, advertising, management, consultancy, logistics, procurement and labour broking
- . **Intangibles**: Any activity involving development, sale, enhancement, licensing and general exploitation of intellectual property, including

trademarks, know-how, franchising, data serviced and telecommunications

- . Property Development: Including construction, property and construction management, procurement, labour broking and professional services (quantity surveyors, architects, engineers etc)
- . Group Services to Operating Subsidiaries: Including asset leasing, labour broking, financial management, administration, technical services, group trademark licensing, treasury, legal and tax, business advisory

## Benefits of GBC's

- . Linked to benefits of Mauritius as a jurisdiction-
  - . Geographical location close to Africa
  - . SADC and COMESA membership
  - . Economic and political stability, rule of law
  - . No Indigenous Empowerment laws
  - . No currency exchange controls
  - . Sound banking infrastructure
  - . Ease of obtaining personal residency for skilled employees (but not so good incentives for them to stay long term)
  - . DTA network with sub-Saharan Africa, India and China
  - . cost effective local support staff
  - . relatively simple tax laws permitting tax efficient structuring
  - . From a pure tax perspective where the effective tax rate is low (15% is too high for most small to medium enterprises given that the substance costs of being in Mauritius) and the need for a DTA benefits

## **Benefits of ACs**

- . None! ..... unless needed as a SPV flow-through vehicle within a shareholding, funding or commercial structure
- . Invariably far better tax risk and cost effective to have a foreign incorporated company (in a jurisdiction such as Seychelles, BVI, Cayman, Hong Kong) with administration in Mauritius (and possibly POEM), but ensuring that CMC not in Mauritius

## Mauritian Tax Risk Management Issues

### Source of Income (derived from Mauritius)

- . Full understanding of the meaning of “*derived from Mauritius*” s5(1)(a), which is the “source” concept applicable to non-residents being subject to Mauritian tax. New definition “foreign sourced income” is unhelpfully stated as income which is not derived from Mauritius
- . Problematic as MRA and legislation use vague terminology referring to the “source of funds” that may indicate from where the revenue is received, which is different from the tax concept of “source” (“derived from”)
- . MRA has no comprehensive Interpretation Note on meaning of source or “derived from”, so we look at International Tax Case Law. UK and SA case law is helpful and deals with “source” as follows-
  - . First identify the “originating cause” or “dominant originating case” of the income
  - . Then determine the location where this originating cause primarily took place.
- . s74 of the Mauritian ITA provides a non-exclusive list of when income is Mauritian sourced, and provides for application of apportionment of source

## Mauritian Tax Residency

- . Clearly understand tax residency definitions for companies, foundations, trusts and partnerships
- . New s73A(1) states that notwithstanding the residency definitions in s73, a Mauritian incorporated company will be treated as non-resident if its POEM is outside of Mauritius. This targets ACs, but can there be CMC of the AC is in Mauritius??? Probably not permissible by FSC
- . Be careful of s82(2) which deems a business to be conducted in Mauritius where a non-resident sells goods through a resident (such as a local agent) and brings the goods into Mauritius (even if the goods are re-exported and sold outside of Mauritius)

## Transfer Pricing

- . s75 is an arm's length test but as it only applies to where a non-resident carries on business activities in Mauritius it is not a genuine "transfer pricing" section
- . Other than the s90 (discussed below) Mauritius does not have any transfer pricing rules, BUT with BEPS pressure on Mauritius expect the MRA to adopt and enforce OECD Transfer Pricing Guidelines by end of 2019. This will compliment substance requirements with far more scientific and comprehensive tests and guidelines than the inadequate MRA Circular of 12/10/18

## General Tax Anti-Avoidance (“GAAR”) Rules

- . Clearly understand s90 that is the primary Mauritian GAAR, which outlines circumstances that permits MRA to conclude that the “sole or main purpose” of a transaction or arrangement was to obtain a tax benefit. These circumstances generally deal with lack of commercial substance, abnormality and/or not at arm’s-length. MRA can then recharacterize the financial arrangement so that it is arm’s length
- . Note a new definition “tax avoidance”

## Some Mauritian Tax Planning Ideas for SA BOs

- . All intangible and tangible asset dependent activities, capital intensive activities and certain technical service activities (including any application of Intellectual Property) is initially set up in a foreign incorporated NON-Mauritian tax resident entity ("NewCo") (depending on business model this may require a jurisdiction with a favourable DTA with Mauritius, factoring in MLI changes);
- . Initially the POEM of the NewCo is not important if it is not making material profits. When the business matures sufficiently, then form a GBC in Mauritius ("GBCco") with the role of providing POEM services and a group holding company role. A market related agreement between NewCo and GBCco provides for agency service and holding company role by GBCco that allows for use of the Mauritian DTA network (particularly with various African countries that have not signed the MLI), and permits a large share of profits to accrue to the NewCo and not the GBCco without exposure to Mauritian tax.
- . Explore the use of DTAs that other low tax countries have with Mauritius (such as Barbados, Cyprus, Malta, Guernsey, Luxembourg, Seychelles, UK, Malaysia) that reduce or eliminate Mauritian tax (including TDS) yet do not impose tax on foreign income (again subject to MLI revisions, if applicable)

- . Given SA tax risks (discussed below), consider using Foundations (rather than trusts), agency arrangements, companies limited by guarantee (this is like a quasi-trust) and partnerships

## South African Tax Risk Management Issues

- . SA Exchange Control Regulations
  - . Will apply to structures with SA residents as discretionary beneficiaries of trust shareholders to GBCs
  - . Cannot have a GBC deriving income (even if market related) from the Rand CMA or owning assets in the Rand CMA (illegal “loop” structure)
  - . SA Excon problems often solved with the formal emigration of the main SA BO
- . POEM (Tax Residency)
  - . Expect a big attack by SARS on the POEM of Mauritian trusts (big risk)
  - . POEM dispute for GBCs will be governed by the new 2013 DTA with SA which is based on MAP and the application of the MOU between SA and Mauritius dated 22 May 2015 (“the MOU”). Follow the guidelines in the MOU, which include-
    - . where board meetings are held
    - . where CEO and other executives carry out their functions

- . where day-to-day management activities take place
  - . where accounting records are kept
  - . BEPS Action 6 Commentary by OECD dealing with POEM
- 
- . Failing agreement by MAP, the DTA benefits will not apply and SARS application of POEM will prevail

### Permanent Establishment ("PE")

- . As per OECD definition of PE and exclusions in the DTA

### Controlled Foreign Company Rules

- . Outline in s9D of SA ITA
- . Either use offshore trusts to hold 50%+ shareholding, otherwise ensure that the GBC profits (that are active and not passive) are attributable to a "foreign business establishment" as defined

## Transfer Pricing Compliance

- . Applicable where there are transactions between SA tax residents and a GBC that is a "connected party"
- . Understand the complex and detailed "connected party" definition in the SA ITA
- . A detailed and professionally prepared Transfer Pricing Policy Document is necessary pursuant to a detailed functional analysis, and must comply with OECD International Transfer Pricing Guidelines and conform to SARS Practice Note 7

## SA GAAP Rules

- . Other than numerous targeted anti-avoidance provisions, the primary GAAP is set out in sections 80A to 80L of the SA ITA that refer to "impermissible tax avoidance arrangements" that involve-
  - . abnormality in the context of a *bona fide* business purpose
  - . lack of commercial substance
  - . round trip financing
  - . accommodating or tax-indifferent parties

- . presumption that the sole of main purpose was to obtain a tax benefit
- . Extremely important to have an official document on record that illustrates that the use of Mauritius and the formation of a GBC and related entities was primarily motivated by bona fide business objectives and benefits (such as no exchange controls, access to cost effective staff, no indigenous empowerment laws, international value added for exit purposes, etc)
- . Having illustrated a commercial motivation for using Mauritius, a SA BO is always permitted to structure the business initiative in the most tax efficient way possible

## Case Studies, Questions and Discussion

- . Time permitting

## Final Thoughts

- . Unless MRA and Government reconsiders the tax benefits and offers a partial exemption to ANY GBC activity where the revenue is paid by non-resident clients, the Mauritian Offshore Financial Sector will quickly and substantially reduce in scope and fiscal relevance to Mauritius. Mauritius will become a niche jurisdiction for offshore services, and Mauritian banks may suffer accordingly
- . Irrespective of the tax dispensation, Mauritian management companies will struggle to survive unless they are associated with or form part of a group of offshore companies offering services in multiple low tax jurisdictions
- . Clients and management companies must get detailed independent legal and tax advice before initiating any structure
- . Given the risk of SARS audit, investigation and aggressive assessment, clients should consider taking out tax risk insurance to cover the substantial accounting and legal fees incurred in SA defending a litigious claim by SARS (only Tax Risk Underwriters offers this unique service [www.taxrisk.co.za](http://www.taxrisk.co.za))

