Tax Hotline

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ITAT CLARIFIES APPLICABILITY OF MAURITIUS PROTOCOL (MAURITIUS PROTOCOL NOT NOTIFIED; TREATY BENEFITED GRANTED BASED ON TRC)

- ITAT reiterates that India Mauritius Protocol cannot be invoked till both countries don't notify the Protocol coming into effect.
- Sanctity of TRC, and commercial rationale to incorporate in Mauritius upheld – Treaty relief granted.

Yesterday, the Delhi bench, of the Income Tax Appellate Tribunal (ITAT) ruled in favor of the assessee (an investment fund based out of Mauritius), by:

- Allowing eligibility to claim benefits under Article 13 the India-Mauritius tax treaty (DTAA); and
- Noting that the recent protocol to the DTAA (introducing the principal purpose test (PPT)), has not yet been notified (and to this extent, ***does not apply***).

The assessee was incorporated in Mauritius, and held a valid TRC and GB license (issued by the Mauritian authorities); and was also registered as a foreign portfolio investor (FPI) with the Securities & Exchange Board of India (SEBI). In the disputed year, the assessee had received income from the transfer of investments in Indian shares, trading in futures and options in India, and dividends from Indian companies. On these streams of income, the assessee claimed:

- Benefit under Article 13(4) on grandfathered shares, and income from futures and options;
- Beneficial rate under Article 13(3B) for shares sold before March 31, 2018; and
- Dividend income and long-term capital gains on which securities transaction tax was paid, were claimed as exempt under provisions of the Income Tax Act (ITA).

Revenue made 2 key arguments:

(a) *No commercial substance in Mauritius*: Control & management of the assessee was outside Mauritius, and in UAE, based on the beneficial owner (of the assessee and the entire corporate structure) being an individual who was a resident of UAE. Accordingly, decision making was outside Mauritius. This finding of the Revenue was based on information requisitioned from SEBI.

(b) *Protocol*: Modified preamble reflects the common intention of the states to eliminate double taxation without creating opportunities for non-taxation, reduced taxation through tax evasion, or tax avoidance (including through treaty shopping). To this extent, while acknowledging that the Protocol would be effected only after both states notify them, the Revenue nonetheless argued that as per Article 3(2) of the Protocol, the provisions would apply from the date of entry into force regardless of when the taxes were levied, and regardless of the dispute tax year.

Ruling of the ITAT:

- Beneficial Ownership: The ITAT observed that decisions were taken independently by the board of directors of the assessee (who were all Mauritian residents) – and the board resolutions depicted this. Further, the ITAT noted that the documents requisitioned from SEBI pertained to a different year and could not be relied upon to ascertain the lack of control and management in Mauritius. Further, the fact that the assessee continued its investment activities in India post March 31, 2017 – reflected the genuineness of commercial rationale to incorporate the assessee in Mauritius.
- Economic Substance: Assessee held a valid TRC, GB License, and registration as FPI form SEBI. Assessee has also held 100% by another Mauritius company. To this extent, the ITAT noted that the assessee was a genuine tax resident of Mauritius, and that the Revenue had failed to meet its evidentiary burden to disprove the same.
- Protocol: Reiterating the language of Article 3(1) of the Protocol, the ITAT noted that the same will only come into force once both states notify the same. In its absence, the Protocol cannot be invoked by the revenue authorities.

While revenue authorities may indeed have referred to the revised preamble within the Protocol, this ruling serves as a prudent judicial precedent – which clarifies the non-applicability of the Protocol, prior to both countries notifying the same.

Further, despite the two-layer structure in Mauritius (i.e., assessee and its holding company, both being residents of Mauritius), the ITAT has accepted the commercial substance and rationale for setting up the assessee in Mauritius,

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based on facts and circumstances of this case. The ruling re-enforces the adequacy of the TRC as sufficient evidence to claim benefits under the treaty (in line with judicial precedents and Circular 789 of the CBDT).

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