laSentinelle Pour devancer demain

l'entretien

RÉALISÉ PAR
LINDSAY PROSPER

Rajesh Simhan, Partner, International Tax, Nishith Desai Associates

"Mauritius may emerge as a better debt jurisdiction than Netherlands"

Rajesh Simhan believes that debt based investments will still flow to India through Mauritius. He played an active part in a seminar which took place in Port-Louis on 7th April on the implications of the Base Erosion and Profit Shifting (BEPS). The one day seminar was organized jointly by Nishith Desai Associates and Juristconsult Chambers.

Mauritius and India have finally decided to sign a protocol with a view to revisit the actual version of the Double Taxation Avoidance Agreement. In some quarters, mainly those already engaged in the global business, it is said that the changes made to article 13 concerning capital gains will have adverse effects on the global business industry. What are your views about the real impact changes to article 13 will have on the industry as a whole?

The removal of the exemption from capital gains, which fuelled many investments into India for decades, will not affect investments in equity already made before 1st April 2017 in light of the grandfathering clause under which such investments remain protected. In fact, from a policy standpoint, they seem to be protected against uncertain application of domestic Indian General Anti-Avoidance Rule, the GAAR, provisions in the future.

However, if convertible instruments such as Compulsorily Convertible Preference Shares (CCPS) and Compulsorily Convertible Debentures (CCDs) acquired prior to 1st April 2017 are converted after the date, they will be considered to have been acquired after 1st April 2017; thus excluding them from the benefits available under the existing clause.

Therefore, after 1st April 2017, insofar as use of Mauritius is concerned, we expect to see companies having debt based investments or investments through hybrid securities that take advantage of the lower interest rate of 7.5% instead of the much higher rates (up to 40%) in force now and the focus to shift on a debt based strategy.

Further, during the transition period of two years from 1st April 2017 to 1st April 2019, a benefit of 50% reduction in corporate tax rate subject to satisfaction of the Limitation of Benefits (LOB) clause has been provided for. To satisfy the LOB test, a company must not be a shell/conduit company; it must have an active business with a minimum business expenditure of 1,500,000 Mauritian Rupees in the immediately preceding 12 months prior to the transaction in Mauritius and action in Mauritius and the primary purpose of the transaction must not be to avail treaty benefits under the Indo-Mauritius DTAA.

Many think that the protocol has given a final blow or rather a deadly blow to the industry. Is there an avenue other than the one around which both countries have agreed to negotiate?

While the unamended treaty definitely served the purpose of promoting Foreign Direct Invesment into India, there will be a paradigm shift in the future. It remains to be seen how far the impact will go.

From the statements from the Government, it does not appear that any other negotiation regarding the treaty is currently taking place and the amended protocol in all likelihood sets the tone for engagement for the foreseeable future. While the treaty has taken away the benefits on capital gains, the lower rate on debt investments will act as a succour as far as the industry is concerned.

It must be remembered that the Indian debt markets are still under-developed and there is a huge potential for increase in the debt investments in India. The treaty changes will definitely help in facilitating that.

Of course, one could have hoped that the treaty only introduced a limitation of benefit article and kept the capital gains tax provision as it was. Having said that, considering the political pressures and negotiations involved, the Indian government has taken a strong stance that the benefits for capital gains tax will not be extended in any treaty.

Now that the DTAA is no more what it was up to now, what should be the next step for people operating in the industry?

The next step would be to focus more on making the best of the lower cap on interest and the requirements for local spending in Mauritius. Currently, as things stand, investments through Mauritius are less uncertain and less likely to be questioned under GAAR. It is also better protected by the grandfathering clause compared to the India-Singapore DTAA.

The P-note industry is likely to take a downturn though. Mauritius may emerge as a better debt jurisdiction than even Netherlands in light of the low withholding tax on interest rates and the added benefit of CCDs still qualifying for the benefits of capital gains tax exemption under the India-Mauritius DTAA.

Does Africa stand as an alternative that can possibly compensate what Mauritius is bound to lose following its approval of the new protocol?

Mauritius still remains an attractive jurisdiction to route investments especially outbound investments into Africa and a few other places. It is possible that Africa could serve to add to the fund flows through Mauritius as it has a very wide tax treaty network with African countries. It is definitely an option which will be used, since Africa today stands where India was two decades back.

Another point of concern expressed mainly by operators of the global business is about the source-based taxation of interest income on bank. What could possibly be the impact of this measure on international banks that can witness a loss of income as a consequence of this measure?

There has been a bit of give and take on the interest provision in the treaty. While there is a source based taxation introduced for banks, the amount of inflow from Banks inMauritius on debt investment is not significant.

The greater investments come from portfolio investors and financial institutions. To that extent, the benefits derived by Mauritius on the interest provisions are much more than what they have given up on.

Let's accept for a while to view the whole issue from the standpoint of India. What are the reasons that have caused India to review an agreement with a partner that has proved to have been an active source for redirecting global investment to India for more than 30 years?

There has been a lot of political and public pressure to plug what is perceived as a tax loophole. The current government has also possibly felt the need to widen its tax base to fund many of its ambitious initiatives. Considering that India is still the fastest growing economy, it appears the Government is of the view that fund flows will not reduce even if subject to higher taxation, particularly from alienation of shares in Indian companies.

In some quarters over here, it is thought that Mauritius did not get a fair share from India following the signature of a new protocol. Did Mauritius deal on a level playing field with India?

While there appears to be some give and take for both sides from the terms of the amended protocol, it does appear to us that the Indian Government has achieved its goals through the amended DTAA. How much of what was negotiated for was unattained by Mauritius is something we are not aware of and therefore we cannot comment on that aspect. However, Mauritius has turned itself into the preferred debt jurisdiction over Netherlands as mentioned above through the signing of this protocol.

Another argument that has been canvassed is that Mauritius could have refused to sign the protocol and waited for the GAAR to come into operation next year. What are the pros and cons of this strategy?

The pros of that strategy would have been that capital gains exemption would have still been available. However, without the grandfathering clause, all investments would have been subject to great uncertainty as it is now with the India-Singapore DTAA and with issues around GAAR, it would have led to a lot of confusion and increased risk. The lower cap on interest would not have been available as well.

Would you, in view of the changes that will occur, invite investors to come and use Mauritius as a pathway for investment to India?

While there will be significant loss (though not complete loss) insofar as equity investments are concerned, there will be increased debt based investments and investments through hybrid securities that should still flow through Mauritius into India. Further, existing investors will also be comforted with the fact that their current investments are being grandfathered.

> «The next step would be to focus more on making the best out of the lower cap on interest».

L'ACTU EN CHIFFRES

Infographie : JD Maxwell Marie. Journaliste : Karen Walter. Source : Statistics Mauritius

Tourisme : recettes de Rs 54 milliards en 2016

Le Bureau national des statistiques vient de mettre à jour son tableau de bord. Ceci regroupe les principaux indicateurs des secteurs clés tel que le tourisme.