

Tax Alert

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Protocol amending the Mauritius-India Double Taxation Avoidance Agreement

On 07 March 2024, Mauritius and India signed a second protocol (the Protocol) amending the Mauritius-India Double Taxation Avoidance Agreement (DTAA). These important amendments are in line the OECD/G20 Base Erosion Profit Shifting (BEPS) recommendations.

Preamble

The Protocol amends the preamble of the DTAA which now states that the parties intend to eliminate double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this DTAA for the indirect benefit of residents of third States).

Principal Purpose Test (PPT)

The Protocol inserts a new key article: to provide that a benefit under the DTAA shall not be granted in respect of an item of income if it is reasonable to conclude that obtaining treaty benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the DTAA.

Effective date

The Protocol will enter into force once Mauritius and India have completed the procedures required under their respective local laws to bring the Protocol into force. The provisions of the Protocol shall have effect from the date of entry into force, without regard to the date on which the taxes are levied or the taxable years to which the taxes relate.

Our comments

Mauritius ratified the OECD Multilateral Instrument (MLI) in 2019 which covered all of its bilateral DTAA's to incorporate the BEPS minimum standards, with the exception of Mauritius-India DTAA and Mauritius-Australia DTAA.

Our comments (continued)

This Protocol now incorporates BEPS minimum standards under the Mauritius-India DTAA as well.

In the context of capital gains, the Indian anti-abuse provision i.e. General Anti-Avoidance Rules (GAAR) has a grandfathering provision i.e. it does not apply to capital gains arising from transfer of investments made before 1 April 2017. A similar provision has not been introduced in the PPT in the Protocol.

Further, the language of the PPT clause is wider than the Indian GAAR provisions. The GAAR treats the transaction as an 'impermissible avoidance arrangement' when the 'main purpose' of the transaction is to obtain a tax benefit. However, the PPT clause denies tax treaty benefit to the transaction if taking such benefit is 'one of the principal purposes' of the transaction.

To give more context, under the DTAA, shares of an Indian company acquired before 1st April 2017 by a resident of Mauritius benefit the grandfathering provision (ie exemption from Indian capital gains tax irrespective of when the sale arises). Such exemption continues to be applicable, but will henceforth be subject to meeting the PPT.

Similarly, the favourable articles such as the dividend and the interest articles - where the rates of withholding taxes are amongst the lowest, compared to the rates under other Indian DTAA's - remain unchanged. However, these benefits will be subject to meeting PPT and the existing beneficial ownership test under the DTAA.

Our comments (continued)

Investors that have invested in India through the Mauritius International Financial Centre (IFC) are advised to review their structures if necessary and to adequately document the commercial rationale for their investment structures, to ensure they have adequate economic substance in Mauritius. A number of incentives and products are available within the Mauritius IFC to help investors build economic substance in Mauritius.

It may be noted that in the context of the date of effect of the Protocol, it has been stated that it would be 'without regard to the date on which the taxes are levied or the taxable years to which the taxes relate.' Use of this expression may raise concerns as to whether this proposed Protocol can be made applicable to any tax proceedings pertaining to the past years. A clarification from the authorities on this should allay these concerns.

It is also recommended that the authorities come up with guidance on the application of PPT and the level of substance required by Mauritius entities to be eligible to the DTAA benefits, including the grandfathering provision for pre-2017 investments.

How we may help?

Our Tax specialists are available to discuss the relevance and impacts of the Protocol to your business.

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This document is based on our interpretation of the current tax laws and international tax principles. These laws and principles are subject to change occasioned by future legislative amendments and court decisions. You are therefore cautioned to keep abreast of such developments and are most welcome to consult us for this purpose.

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