PRICEWATERHOUSECOOPERS

Tax times*
Mauritius

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Tax practice

Tax treatment of foreign exchange gains and losses

1. The Law

Tax is payable on income that has been derived. Income is deemed to be derived when it has been earned or has accrued.

2. Taxation Principle

It is a well established principle of taxation that profits are not earned and losses do not accrue until they are realised, i.e. tax is imposed on "true" profits and deduction is allowed for "true" losses. Consequently, an unrealised profit or loss is not taken into account in determining the tax liability.

3. Foreign exchange gains and losses – the practice

Foreign exchange differences may be classified into 2 categories:
- capital and revenue and
- realised and unrealised

Under the Income Tax Act, any expenditure of a capital nature is not deductible and likewise any receipt of a capital nature is not taxable. Capital gains/losses, whether realised or unrealised, are therefore not taken into account in determining the taxable income of a person. This is confirmed in Commissioner's ruling 30B.

Whether a transaction is capital or revenue in nature depends on the facts and circumstances of each case.

As regards foreign exchange gains or losses on revenue account, these are recognised as income or allowed as a deduction only when realised, on the basis of established tax principles. Translational gains/losses on foreign exchange are notional differences (unrealised) and are thus not taxable nor tax deductible.

4. Ruling 33 of the Commissioner of Income Tax

The above practice had existed until recently when the Commissioner took a different stand on the method of taxing unrealised exchange differences in one of his rulings, Ruling 33 issued in November 2003. It reads as follows –

"TR 33

Point 1: Taxation of Exchange Differences

Facts

A company incorporated in Mauritius holds a Category 1 Global Business Licence (GBC 1) for the purpose of holding investments of a group overseas. It intends to invest primarily in securities in some countries denominated in a currency other than its reporting currency viz US Dollars (USD). At year end, the company may have in its balance sheet amounts due to and from brokers in different countries. The company may also have surplus cash in the bank account in these countries in the relevant underlying currencies for a number of reasons.

The debtors, creditors and cash balances at year end denominated in a currency other than the reporting currency will need to be translated at year end rates in accordance with generally accepted accountancy principles. This would result in exchange differences which would be taken to the statement of operations as results for the year.

Point at issue

Whether the exchange differences resulting from the above would be considered as a deduction or income, as the case may be, in computing the company's chargeable income.

Ruling (issued in November 2003)

The calculation of profits for tax purposes should start with a consideration of the accounts drawn up in accordance with accepted principles of commercial accounting.

If the accounts of the GBC 1 company prepared in accordance with the Companies Act and generally accepted accountancy principles have to take account of translation profits and losses then these profits and losses should also be taken into account for tax purposes unless there are particular reasons relevant to the case in question, including whether they are in respect of capital items, for taking a different view.

In deciding what generally accepted accountancy principle is for this purpose, regard should be had in particular to IAS 21 – "The effects of changes in Foreign Exchange Rates" and to published accountancy practices."

5. Comments

Changes in tax laws providing for new methods of taxation are often accompanied by transitional provisions addressing issues that may subsequently arise. The stand taken by the Commissioner in Ruling 33 constitutes a departure from a long standing administrative practice giving rise to several questions. For example, it is not known as from which year the ruling applies, what treatment should be given to previous years' gains and losses, whether a taxpayer is compelled to or he may opt not to adopt the new method of recognising unrealised gains/losses, etc.

Let us hope that these issues will be dealt with and other relevant information and explanation will be provided in one of the Income Tax Department's Statements of Practice, the publication of which has been provided in the Finance Act 2005.

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Tax briefs

Australia

The federal Government is expected to introduce an anti-money laundering bill to parliament by October. Experts on the subject indicated that about $15 billion in "dirty money" was being laundered in Australia each year.

India

A major tax payer friendly initiative in the shape of Advance Ruling has been taken by the State of Haryana in its VAT Act. Many other states are also proposing to incorporate provisions of advance ruling in their proposed VAT law.

United States

A bi-partisan group of Senators is backing new legislation that will eliminate the ill-conceived and ever-expanding Alternative Minimum Tax system by the end of the decade at a cost of $611 billion.

Saudi Arabia

The Saudi Arabian General Investment Authority (SAGIA) is studying new proposals to attract foreign investment, including exemption of investment projects from income tax for 15 years.

Russia

The Russian government has approved Finance Minister Alexey Kudrin's plan for an amnesty on undeclared funds, which is set to commence in 2006.

Korea

The Korean National Tax Service revealed recently that it will step up the number of tax investigations carried out on foreign companies operating in Korea in a bid to counter loss of tax revenues arising from international tax planning.

Mauritius

The Mauritian government is hopeful of relaunching discussions with the Indonesian government regarding the lapsed Double Taxation Avoidance Agreement between the two countries, said Finance Minister Rama Sithanen in a recent press conference.

Update on
New Income Tax Measures

On 30 August 2005, the Minister of Finance in his speech to the National Assembly, announced certain measures relating to Income Tax in Mauritius:

- Confirmation that there is no requirement for global businesses to gross up foreign sourced income when claiming the presumed foreign tax credit;
- Establishment of a Consultative and Advisory Committee on Taxation and Investment Agreements (CACTIA) which will provide a forum for exchange of views among stakeholders; and
- The extension of the 60% tax credit on equity-investment in spinning, weaving and dyeing companies to equity investment in companies engaged in the knitting of fabrics.
  - The threshhold required to qualify for this special tax credit will also be lowered from Rs60m to Rs10m.
  - The deadline for investment will be extended to 30 June 2008; and
  - The tax credit will be available to both new and existing companies.

Tax treaties

The India - Singapore Tax Treaty Revisited

- On 29 June 2005, India and Singapore signed the Comprehensive Economic Co-operation Agreement (CECA) which became effective from 01 August 2005. As part of CECA, some major amendments were made to the India/Singapore tax treaty signed in 1994 to bring it in line with the India/Mauritius tax treaty. As a reminder to our readers, in spite of the fact that the India/Mauritius tax treaty was signed by two sovereign states way back in 1982, the treaty has come under constant attack from the Indian tax administration over the last decade. Anyway, it is comforting to note that a tax treaty which was frowned upon and threatened for termination yesterday is used as a model today.

- The amendments include the reduction of withholding tax on royalties from 15% to 10% compared to 15% under the India/Mauritius tax. However, the most important change is in respect of capital gains. Thus, gains from the disposal of shares are now taxable only in the beneficiary's country of residence. Formerly, only gains from the sale of shares of companies other than property companies were taxable in the country of residence. With this amendment, capital gains derived by a Singapore based company from sale of investments in Indian companies in general may be repatriated free of Indian capital gains tax.

- In this respect, therefore, Mauritius and Singapore have been brought to the same level playing field and will remain so as long as the capital gains tax provision in the India/Mauritius treaty is not modified.

- However, a "Limitation of Benefits" clause has been introduced whereby no exemption from capital gains tax will be available to shell/conduit companies that are organized only to take advantage of this tax concession. A company will not be considered as a shell/conduit company if it is listed on a recognized stock exchange of its country of residence or if its total annual expenditure on operations is at least S$ 200,000 or Indian Rs 5,000,000.

- From a tax perspective, we believe that this new protocol will not induce typical Mauritius investment holding companies to migrate to Singapore as such companies normally hold Indian shares as investments or for control purposes rather than for resale and as such expect to earn dividends rather than capital gains. Furthermore, the annual operational expenditure threshold of S$ 200,000 will clearly act as a deterrent as the cost of operations in Mauritius is much less. For the same reasons, the protocol is not likely to cause a shift to Singapore for new investment holding companies.

- Collective investment vehicles on the other hand would have the choice between Mauritius and Singapore and given that capital gains from sale of investments constitute their main income stream they can benefit from the capital gains tax exemption in India in either case. However, we are still uncertain as to whether such gains will be regarded as normal trading income by the Inland Revenue Authority in Singapore and if so whether it will be taxable when received in Singapore. We expect to address this question in our next issue.

Quote:

"Income tax returns are the most imaginative fiction being written today."

Herman Wouk

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Tax Basics

Key concepts, definitions and regulations

Statements of Practice – A must for modern tax administrations

It has always been said that passing the law is easy but implementing it is another matter. This is also true for taxation laws. The laws for levying taxes are voted in parliament by the people's representatives and compliance with such laws should not pose any problem. However, this is rarely the case in practice.

The complexity of tax schemes and the perceived lack of transparency in their operation have always led taxpayers to react in a hostile manner against the tax authorities as well as against the finality of the taxes themselves. The result is a high rate of non-compliance with the laws.

Modern tax administrations all over the world have therefore been taking numerous measures in an attempt to improve relationship with taxpayers thereby creating conditions favourable for obtaining a better participation from them for tax collection. One of these has been the publication of Statements of Practice.

Mauritius is following suit and, as a first step, Government has amended the Income Tax and VAT Acts through the Finance Act 2005 to provide for their publication. This measure has been much acclaimed by tax professionals and the taxpaying public in general. Though certain explanatory notes and circulars are already in existence, it is felt that information on practice and procedures adopted by the tax authorities are still much lacking.

Now that the law has been voted, the Income Tax and VAT Departments would not be taking long to issue the first Statements. The tax authorities no doubt receive numerous suggestions and complaints from the public in their day-to-day activities.

Professional tax advisers too are in constant contact with their clients and may be in a better position to know their qualms and predicaments.

Tax authorities and tax advisers should therefore join hands to make Statements of Practice as successful as possible both in their making and application. True it is that there are a lot of provisions which need to be addressed in this context but it would appear that the following have been of much concern in the past both for tax advisers and for the taxpaying public and may be considered in priority –

- procedures for the examination of returns and accounts
- procedures for the examination of books and records and the carrying out of field audits
- policy on the imposition of penalties, surcharges and interests
- recognition of foreign exchange differences as income/loss for income tax purposes and as supply for VAT purposes
- the basis for computing income where a non-30 June return date is contemplated
- methods for computing and taking foreign tax credit

If we were to have a look at Code of Practice, COP8-Special Compliance Office Investigations, published by the Inland Revenue (UK), for example, we would be able to appreciate the extent of information contained therein – it not only lays down the reasons why the investigation is carried out but also the approach that the tax authorities adopt in carrying out the investigation. Alongside, the document also clearly draws attention to all the rights and obligations of both the tax authorities and the taxpayer and does not miss to provide whatever advice is necessary to the taxpayer to safeguard his interest. The principles laid down in the four canons of taxation enunciated more than 200 years ago by the well-known economist Adam Smith seem to have found a prominent place in the document.

If prepared and published in a plain language with the required information and necessary guidance, statements of practice will go a long way towards improving taxpayer-tax administrator relationship and facilitating tax collection.

Useful Links

Ministry of Finance, Mauritius
www.mof.gov.mu

Inland Revenue, UK
www.hmrc.gov.uk

Tax Basics

Key concepts, definitions and regulations

Personal Taxation

What are the Income Tax rates in Mauritius?

The tax rates detailed below are applicable on income derived as from 1 July 2004. These rates are applied to an individual's chargeable income (basically, income including emoluments and fringe benefits less deductions and reliefs):

Chargeable Income	Rate of tax
On the first Rs 25,000	10%
On the next Rs 25,000	20%
On the next Rs 450,000	25%
On the remainder	30%

Did you know?

Where an individual deriving emoluments exceeding Rs 400,000 fails to submit a return, he shall be liable to pay a penalty of Rs 5,000 per month or part of the month up to a maximum of Rs 50,000.

Corporate Taxation

What are the allowable deductions with respect to marketing and promotional expenses?

A company engaged in tourism or export activities may, in an income year, deduct from its gross income twice the amount of any expenditure incurred in that income year on overseas marketing, export promotion including participation in international trade fairs, overseas advertising and preparation of tenders for the export of goods and services.

Are pre-operational expenses allowable deductions?

If a company is incorporated on or after 1 July 1993 and is a tax incentive company, it shall be allowed a deduction from its gross income of the pre operational expenses incurred.

VAT

For how long should you keep your VAT invoices?

The VAT legislation requires that a VAT registered person who issues VAT invoices, ordinary invoices and receipts shall keep legible copies thereof, either on computer or otherwise, in chronological order.

Every copy of the invoices has to be kept for a period of at least 5 years after the completion of the transaction to which it relates, and has to be made available to VAT officers for control purposes.

International Taxation

Foreign Tax Credits

A Corporation subject to tax on its foreign income is entitled to a tax credit in respect of any foreign tax paid on such income. The credit is however limited to Mauritian tax applicable to that income.

Where the foreign income includes dividends, credit is allowed both for withholding tax and underlying tax provided that the recipient company holds at least 5 percent of the share capital of the company paying the dividends.

Credit for underlying tax is given on a multi-tier basis. Mauritian domestic law also provides for tax sparing relief whereby credit is allowed for foreign tax deemed to be paid though not actually paid. For the purpose of claiming and maximising foreign tax credit, a taxpayer may compute the amount of foreign tax by referring to all foreign source income together or to each item of such income separately whichever is to his advantage.

Global Business Companies, engaged in international business activity, are liable to tax at a rate of 15 percent. Where they are not able to show evidence that foreign tax has been charged on their foreign income, they will be presumed to have paid foreign tax amounting to 80 percent of the Mauritian tax chargeable with reference to that income.

This provision limits the tax liability of such companies to an effective rate of 3 percent.

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PricewaterhouseCoopers Mauritius **(www.pwc.com/mu)** was created on 1 July 1998, following the merger of Price Waterhouse and Coopers & Lybrand.

PricewaterhouseCoopers in Mauritius is recognised as a thought leader and a change initiator, offering the resources of a global organisation combined with detailed knowledge of local issues.

With over 200 professional staff, we serve a large number of multinational companies doing business in Mauritius, a cross section of the local business community as well as public institutions.

Tax Services

Assessment and appeals
- Attending to assessments and processing objections
- Preparation of appeal documents
- Representation at tax appeal tribunals

Corporate (Income) Tax services
- Preparation, review and filing of tax returns
- Monitoring compliance with filing and payment deadlines
- Correspondence or meetings with authorities to finalise tax assessments

International Assignee Solutions
We provide expatriates with tailor made tax planning and tax compliance services.

Value Added Tax services
- Advice on VAT compliance obligations
- Preparation, review and filing of tax returns
- Monitoring compliance with filing and payment deadlines
- Correspondence or meetings with authorities to finalise tax assessments

Tax Health Checks
We carry out tax health checks to provide assurance on compliance with Income tax, PAYE, social security and VAT.

Tax Advisory and Planning services
This includes general tax issues including:
- Mergers and Acquisitions
- Restructuring
- Disposals
- Value Added Tax
- International taxation
- Customs and excise duties
- Stamp duty

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