Mauritius VAT and the international business landscape

26 Oct 2016

In brief

The increasing trend in the international trade of goods and services is compelling all tax jurisdictions to adapt their VAT legislations to ensure that their tax base is not being eroded; Mauritius is no exception. Most countries are adopting the destination principle in an attempt to protect their taxing rights. While the rules for the supply of goods are straightforward and practical due to border/custom controls, those governing the international trade of services/intangibles are more complex. This edition of tax times explores the issue of double imposition of VAT on cross border trade in services.

In detail

Most countries are adopting the destination principle in an attempt to protect their taxing rights, that is, VAT is imposed and collected where consumption takes place. For example, the cross border movement of goods are subject to VAT in the jurisdiction where the goods are delivered as exports from one country are free of VAT and imports are taxed in the country of destination at the domestic rate. However, while the rules for the supply of goods are straightforward and practical due to border/custom controls, those governing the international trade of services/intangibles are more complex.

In general, VAT on the import of services and intangibles is collected through the reverse charge mechanism, that is, the person receiving a service from abroad accounts for VAT through a process of self declaration and recognizes both input and output VAT on the transaction.

A foreign supplier of services needs to register for VAT in Mauritius if the supplier has a presence in the country through a permanent establishment. However, this is not necessarily the case in all circumstances as Mauritius also adopts the destination principle in respect of digital businesses.

Tax Ruling 57 specifies that, where internet related services are being supplied to a person in Mauritius (that is, digital services) and such services are being performed or utilized in Mauritius, the foreign supplier needs to register for VAT and comply with the local reporting obligations if his turnover exceeds the registration threshold. Where the registration threshold is not met, VAT is applicable through the reverse charge mechanism.

The end result is same for the MRA, whether through the registration of the foreign supplier in Mauritius or the process of reverse charge.

The OECD’s Committee on Fiscal Affairs (“CFA”) has issued guidelines on the destination principle to assist jurisdictions to shape their VAT frameworks to cope with the increase in the volume and complexity of cross border trade in services/intangibles.

The objective of the CFA Guidelines is to facilitate international trade in services/intangibles through maintaining the following:

a. Neutrality, that is, eliminate the VAT burden throughout all intermediary stages until the service is delivered to the final consumer (who will bear the VAT cost);

b. Simple compliance procedures to alleviate the tax collection burden placed on businesses;

c. Clarity and certainty for both businesses and tax administrators; and

d. Robust controls to tackle evasion and avoidance.

Since the introduction of VAT in September 1998, the destination principle has been applied in Mauritius in respect of services received from abroad through the reverse charge mechanism. Whilst the principle of reverse charge is long established in Mauritius, the Finance Act 2016 (“FA2016”) has recently introduced some changes and brought a new perspective to this concept, with the broadening of its application.

Previously, only a VAT registered person receiving a supply of service from abroad was required to apply reverse charge and account for VAT in Mauritius on behalf of the foreign supplier. The FA2016 has widened this application to non-VAT registered persons, including companies and unincorporated businesses.

The merit of this new provision is that it now brings on an equal footing both local and foreign suppliers of services for all businesses, whether registered for VAT or not. Under the old regime, foreign suppliers of services were not subject to VAT (except under the reverse charge provision for VAT registered persons) while similar supplies by domestic suppliers were subject to VAT. The difference in the VAT treatment and burden placed on businesses; and similar situations carrying out similar transactions should be subject to similar levels of taxation. However, the new provision under the FA2016 may lead to the double imposition of VAT/GST.

On the other hand, one can also foresee issues with this provision. The CFA Guideline 2.2 stresses that “Business in similar situations carrying out similar transactions should be subject to similar levels of taxation.” However, the new provision under the FA2016 may lead to the double imposition of VAT/GST.

The application of the destination principle in respect of the supply of services means that a supplier will need to charge VAT to a foreign client if the service is being consumed/utilized in the country of the supplier even though the customer may be located abroad. In such situation, the foreign client may suffer VAT in two jurisdictions, thus a double hit!
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For example, if a domestic holding company in Mauritius (typically non-VAT registered) pays management fees to a third party in a foreign country to oversee its foreign operations and VAT has been applied as consumption is in the country of origin, such a company in Mauritius will suffer a double hit in respect of the input VAT now being recognized. See the illustration.

<table>
<thead>
<tr>
<th>NON-VAT REGISTERED PERSON</th>
<th>VAT REGISTERED PERSON</th>
</tr>
</thead>
<tbody>
<tr>
<td>Foreign Supplier USD</td>
<td>Mauritius Company USD</td>
</tr>
<tr>
<td>Local VAT (Assume 20%)</td>
<td>200</td>
</tr>
<tr>
<td>Cost of import of service</td>
<td>- 1,200</td>
</tr>
<tr>
<td>Reverse charge provision (15% as output VAT)</td>
<td>- 180</td>
</tr>
<tr>
<td>Claim for input vat under reverse charge provision</td>
<td>- - (180)</td>
</tr>
<tr>
<td>Total Cost of import of service</td>
<td>- 1,380 - 1,200</td>
</tr>
</tbody>
</table>

The issue of double imposition of VAT can be far reaching. Marketing fees, sales commission fees, portfolio management fees, procurement fees paid to foreign suppliers by non-VAT registered persons are likely to suffer the same unintended consequences of this new piece of legislation as those services are likely to be consumed in the country of origin and VAT applied thereon.

Whilst the CFA Guidelines is not intended to interfere with the sovereignty of a country and its ability to implement rules to limit or deny the recovery of input VAT, tax administrations should follow good tax principles to preserve neutrality. The provisions being introduced under FA2016 should be assessed against this principle!

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For more information, please see contact details on the website
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