Updates on the tax treaty between India and Mauritius and impact on Singapore

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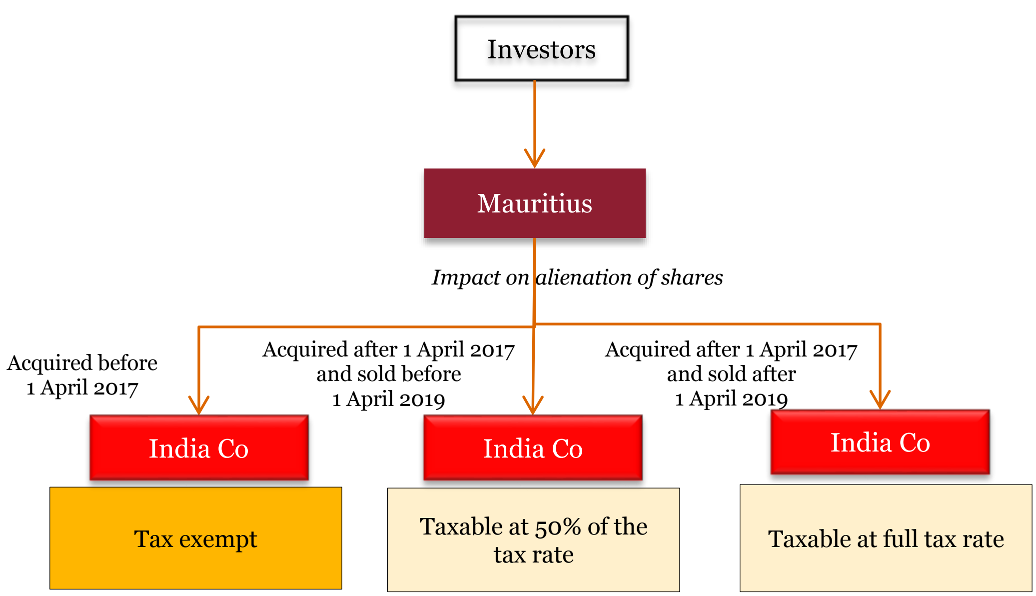
Current provisions

The current double tax agreement between India and Mauritius (the "India-Mauritius treaty") provides, *inter alia*, an exemption from tax in India on capital gains earned by a tax resident of Mauritius. Such capital gains are subject to tax based on residency rules, thereby giving taxation right to Mauritius. An exemption is available under the double tax agreement between India and Singapore read with the 2005 Protocol (the "India-Singapore treaty"), subject to the satisfaction of the Limitation of Benefit (LOB) conditions. However, this exemption is contingent upon the availability of similar benefit to a tax resident of Mauritius under the India-Mauritius treaty.

Amendments per the Press Release dated 10 May 2016

Based on the Press Release issued by the Government of India on 10 May 2016, India and Mauritius have signed a protocol amending the India-Mauritius treaty, giving India the right to tax capital gain on the alienation of shares in an Indian company. The changes are illustrated in the flowchart below:



The key amendments emerging out of the Press Release are as follows:

- The Protocol gives India taxation rights on capital gains arising from alienation of shares acquired on or after 1 April 2017 in an Indian resident company.
- Shares acquired prior to 1 April 2017 will be grandfathered.
- For capital gains arising during the transition period from 1 April 2017 to 31 March 2019, the tax rate will be limited to 50% of the domestic tax rate in India, subject to the LOB conditions.
- Taxation in India at full domestic tax rates will take effect from 1 April 2019 onwards.
- The LOB article clarifies that a resident of Mauritius (including a shell/conduit company) will not be entitled to the benefit of a 50% reduction in the tax rate if it fails the “main purpose” and “bona fide business” test. A Mauritius resident is deemed to be a shell/conduit company if its total expenditure on operations in Mauritius is less than Indian Rupees 2,700,000 or Mauritius Rupees 1,500,000 (approximately USD 40,000) in the immediately preceding 12 months.
- Taxation of interest income for banks - Interest arising in India and derived by Mauritian resident banks will now be subject to tax in India and accordingly, will be subject to withholding tax in India at the rate of 7.5% with respect to debt claims or loans made after 31 March 2017. However, interest income from debt claims existing on or before 31 March 2017 shall continue to be exempt from tax in India.
- The Exchange of Information Article has been updated as per international standard.
- The Protocol also includes a provision for assistance in collection of taxes, source-based taxation of other income, among other changes.

Impact on India-Singapore treaty

Article 6 of Protocol under the India-Singapore treaty provides that the residency based taxation right on capital gains is co-terminus with the similar rights available under the India-Mauritius treaty. Therefore, the amendment to the India-Mauritius treaty could also impact the capital gains tax treatment of Singapore residents. It remains to be seen how the changes will impact the application of the India-Singapore treaty.

Singapore is a well regulated and substantial financial centre in the Asia-Pacific region. India is seeking to attract foreign investments to maintain its growth trajectory and infrastructure needs. It is imperative that the strengths and needs of both Singapore and India are complemented to achieve an optimum solution for the business community. One tool for this purpose is to retain the capital gains exemption clause under the India-Singapore treaty. Only time will tell how this pans out. In the meantime, as the dust settles, global investors will need to examine their investments into India, and see what next steps need to be taken to address potential tax implications.

Your PwC Contacts

If you have any questions or require any assistance, please do not hesitate to reach out to your usual PwC contacts. You can also contact Anuj Kagalwala or Abhijit Ghosh on this matter.

Anuj Kagalwala
Partner, Financial Services
anuj.kagalwala@sg.pwc.com
+65 6236 3822

Abhijit Ghosh
Partner, India Desk
abhijit.ghosh@sg.pwc.com
+65 6236 3888