India
The Tax Treaty Changes With
MAURITIUS

Mauritius based entities that Invest in India – from Private Equity investors, VC funds, and investment pass-through vehicles (which issue participatory notes) will start to see taxation apply to them from April 1, 2017. This is due to a treaty change between India and Mauritius.

Currently, if you are a foreign investor, you can invest in Indian companies – both listed and unlisted. When you sell them, you would pay capital gains taxes in India (as many NRIs do) and some of those gains are withheld before you get the money.

But till now, there were **Double Taxation Avoidance Agreements (DTAAs)** which are treaties between India and certain countries that allowed a certain type of gain – Capital Gain on the sale of shares or property – to be untaxed in India. This applied to entities coming from Mauritius, Cyprus and Singapore. So if you brought the money in "through" a Singapore, Mauritius and Cyprus entity, then the sale of shares would not be taxed at all, since none of these countries charged any capital gains taxes.

MAURITIUS WAS THE EASIEST.

All you had to do to get zero tax on your investments – both listed and unlisted – was simply to set up a shell entity in Mauritius. The tax treaty didn't differentiate between a Company that was actually operating in Mauritius versus a company that was only set up there to get tax benefits. So for a few thousand dollars, you could get a Mauritius entity and invest through it into Indian stocks and shares, and never pay capital gains taxes anywhere.

WHY NOT SINGAPORE?

Why not Singapore? Singapore had both "objective" and "subjective" restrictions on who got this treaty benefit – for one, the Singapore entity needs to spend Sing$ 200,000 a year in Singapore – an amount that would easily deter the tax shopper from creating such entities only for tax benefits. Subjective rules also exist which can disallow a company if the tax authority feels this entity was created only to get tax benefits.

Mauritius was thus the easiest entity to create your little tax avoidance intermediary. And scores of people used it. Almost all the big banks have a Mauritius intermediary that owns shares either for themselves or on behalf of customers, with the primary advantage being tax.

From April 1, 2017, any shares that are purchased, by Mauritius entities, will see capital gains taxes in India.

Meaning, if you already own those shares, you will not be taxed on their sale. (So shares bought before April 1, 2017 are exempt like they are now). This is where the process has been **grandfathered**.

01.04.2017 to 01.01.2019

Also, if you bought these shares after 2017, and sell them before April 1, 2019, **you get taxed only HALF of the domestic tax rate**. For two years, there's some sort of a discount.

And There's a Limitation Too

To get the lower tax benefit (between 2017 and 2019) you still have to qualify under the Limitation of Business (LOB) principle – meaning:

- You can't just be based in Mauritius for Tax purposes
- You have to spend Rs. 27 lakh rupees (15 lakh Mauritian rupees) per year in Mauritius

If you don't qualify, you don't get the lower tax (for two years). After that, the LOB doesn't matter – anyway you pay full tax.

01.04.2019 Onwards

After April 1, 2019, shares sold that were bought after 1/4/2017 will **attract the full domestic tax rate**.