Global Tax Alert

South Africa and Mauritius sign MOU making it possible for revised treaty to come into effect in 2016

The revised Double Taxation Agreement (treaty) between South Africa and Mauritius is likely to come into effect on 1 January 2016, following the signing of the memorandum of understanding (MOU) between the two countries on 22 May 2015. The remaining action to bring the treaty into effect is the completion of the relevant Mauritian domestic procedures and exchange of a diplomatic instrument of ratification. If the process is completed by Mauritius this year (which is expected, following pressure from South Africa), the treaty will have effect as of 1 January 2016.

By way of background, the revised treaty stipulates that in the case where by reason of the application of the generic residency criterion (residence, place of management or any other criterion of a similar nature), a person other than an individual is a resident of both Mauritius and South Africa, the competent authorities of these countries shall by mutual agreement endeavor to settle the question and determine the mode of application of the treaty to such person. In the absence of such agreement, the person would be considered to fall outside the scope of the treaty. This blanket disallowance of treaty benefits created a lot of uncertainty as the treaty did not prescribe the decision framework and factors that the competent authorities needed to consider in order reach a mutual agreement.

The MOU provides that the competent authorities must consider the place of effective management, the place of incorporation, and any other relevant factors. In line with the 2010 Organisation for Economic Co-operation and Development (OECD) Commentary to the Model Convention, the MOU provides that the competent authorities must consider:

- Place where meetings of the board of directors or equivalent body are usually held, the CEO and other senior executives carry on their activities, the senior day to day management is carried on, headquarters are located, accounting records are kept
Law of the country governing the legal status of the person

Factors as listed in paragraph 24.1 of the 2014 OECD Commentary (Article 4, paragraph 3), as may be amended by the OECD Base Erosion and Profit Shifting (BEPS) Action 6 final report. Action 6 deals with the prevention of the granting of treaty benefits in inappropriate circumstances

Any such other factors that may be identified and agreed upon by the competent authorities

Other key changes in the revised treaty are as follows:

- The dividends tax rate remains the same (at 5%), to the extent that the participation threshold of 10% is met. If the participation threshold is not met, the applicable rate has been reduced to 10% from 15%. The South African domestic dividends tax rate is 15%.

- Tax on interest will now be increased to 10% subject to certain exceptions. The current treaty provides for a zero tax on interest (exclusive tax in a resident state). South Africa introduced withholding tax on interest from 1 March 2015 at a domestic tax rate of 15%.

- Royalties will now be taxed at a rate of 5%. The existing treaty provided for a zero tax on royalties (exclusive tax in a resident state). South Africa’s domestic withholding tax on royalties is 15%.

- The tax sparring provision was removed. South Africa will therefore only provide foreign tax credits for actual Mauritian tax paid.

- Currently, the capital gains article does not provide for taxing land-rich shares (i.e., shares in a company that substantially holds immovable property). The revised treaty provides that land-rich shares are taxable in South Africa the same way as immovable property held directly.
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