

INVESTING INTO AFRICA: COMPARISON BETWEEN SOUTH AFRICAN HEADQUARTER COMPANY AND MAURITIAN GBC1 REGIME

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Section 9I of the Income Tax Act 58 of 1962

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Statement

Research dissertation presented for the approval of Senate in fulfilment of part of the requirements for the Postgraduate Diploma: Tax Law in approved courses and a minor dissertation. The other part of the requirement for this qualification was the completion of a programme of courses.

I hereby declare that I have read and understood the regulations governing the submission of Postgraduate Diploma: Tax Law dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

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10 February 2014

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Summary of abbreviations used

1. "Act" means Income Tax Act 58 of 1962
2. "BRICS" means Brazil, Russia, India, China, and South Africa.
3. "CFC" means Controlled Foreign Company as defined in section 9D of the Act
4. "COMESA" means the Common Market for Eastern and Southern Africa
5. "DTA" means double taxation agreement
6. "FSA" means Financial Services Act 2007 of Mauritius
7. "FSC" means Financial Services Commission of Mauritius
8. "FSD" means Financial Surveillance Department
9. "GBC1" means Global Business Company category 1
10. "GBC2" means Global Business Company category 2
11. "GBL" means Global Business Licence
12. "GMT" means Greenwich mean time
13. "HQC" means headquarter company
14. "IHC" means Intermediary Holding Company
15. "IOR-ARC" means Indian Ocean Rim – Association for Regional Cooperation
16. "IPPA" means Investment Promotion and Protection Agreements
17. "JSE" means Johannesburg Stock Exchange
18. "MIGA" means Multilateral Investment Guarantee Agency
19. "MOBAA" means Mauritius Offshore Business Activities Authority
20. "SADC" means Southern African Development Community
21. "SARB" means South African Reserve Bank
22. "STC" means Secondary Tax on Companies
23. "TAA" means Tax Administration Act
24. "TRC" means a tax residency certificate

1. Introduction

In the 2010 Budget review The South African National Treasury announced it intended to create a business environment that would promote South Africa as a gateway to investment into Africa.¹ As such a headquarter company regime would be considered.

With globalisation and free movement of capital internationally countries are pursuing holding company regimes to attract investment to, and through, their shores. At the forefront are countries such as Belgium, Denmark, Luxemburg, Mauritius, the Netherlands, Singapore and the United Kingdom.² Following the 2010 Budget review South Africa has now joined this group.

Headquarter companies and Holding Companies are commonly used by multinational groups in their group tax planning. As such, Intermediary Holding Companies (hereinafter referred to as "IHC") are established to benefit from a country's double tax agreement (hereinafter referred to as "DTA") network, as well as other advantages offered by a country's tax regime.³

Briefly an IHC is generally interposed between the ultimate shareholder and operating companies. They are thus holding companies and subsidiaries at the same time. They are also normally set up in a jurisdiction other than that of the ultimate shareholder and operating company and hold the interests in the operating company. For example the ultimate shareholder may be

¹ National Treasury *Budget review* (2010) 78

² T Legwaila 'Tax characteristics of an ideal holding company location' (2012) available at <http://www.saflii.org.za/za/journals/DEJURE/2012/3.pdf> accessed on 2 January 2014.

³ R Bennett *An evaluation of how the new headquarter company tax provisions in South Africa should be amended to result in a direct benefit to the fiscus* LLM (University of Pretoria) (2012) 2

located in Luxembourg, the IHC is located in Mauritius and the operating company is located in Namibia.

The South African National Treasury first considered a corporate headquarter and holding company regime from the recommendation of the Katz Commission in 1997.⁴ The Katz Commission acknowledged that encouraging the formation of international corporate headquarters and holding companies located in South Africa would be advantageous to the economy in two ways. Firstly it would encourage local investors to expand offshore without sending scarce human resources abroad. Secondly, it would encourage foreign investors to expand into Africa via South Africa.⁵

The Katz Commission⁶ analysed the environment in which South Africa was competing by considering conditions conducive to international holding companies in fifteen countries in Europe and Asia. Tax havens in numerous countries were also considered. However due to South Africa's geographic proximity, regional superiority as regards infrastructure, and common cause with Africa, South Africa was viewed as an attractive location for these type of companies for operations in Africa and especially Sub-Saharan Africa.

Mauritius has long established itself as a favourable IHC jurisdiction, especially for investments into Africa. Following South Africa's introduction of a headquarter company regime the question which needs to be asked is whether the current legislation does enough to persuade an international investor to choose South Africa instead of Mauritius or any other country.

This minor dissertation undertakes to compare the current South African headquarter regime with that of Mauritius. Mauritius has been studied due to

⁴ Katz Commission *Fifth Interim Report of the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa* par 7.1

⁵ Katz Commission *Fifth Interim Report of the Commission of Inquiry into Certain Aspects of the Tax Structure of South Africa* par 7.1.1

⁶ Katz Commission par 7.1.6

its similarities with South Africa. Like South Africa it is an African country, it is a developing country, it has long been recognised as an IHC jurisdiction and it is a member of the Southern African Development Community (SADC).

2. Considerations in establishing an IHC

The selection of an IHC location is an important component of international tax planning for multinational groups. The choice of location involves a complex decision making process taking into consideration the individual circumstances of the specific multinational group. The tax system plays a major role in this decision making process but it is by no means the only consideration.

2.1 Tax Considerations

The Katz Commission⁷ identified the following as key fiscal attributes of a regime conducive to the formation of international holding companies:

- A reasonable DTA network;
- The exemption of offshore corporate dividend income from local income tax;
- The exemption of other defined offshore corporate income from local income tax;
- The absence of local corporate capital gains tax;
- Low or no local withholding tax on dividends paid to shareholders;
- An efficient local tax rulings system; and
- No tax on head office services rendered at the head office to the multi-national group.

⁷ Katz Commission par 7.1.4 and 7.1.5

2.2 Non Tax Considerations

Although tax is an important consideration, operational factors are equally important in determining the place of business for an IHC. Consideration must be given to infrastructure, transportation networks, communication networks, availability of labour, labour skills, language, political stability, the ability to repatriate profits freely, an effective banking system, the legal system and a convenient time zone.⁸

3. Mauritius

3.1 Introduction

Mauritius is a small island situated in the Indian Ocean to the east of Madagascar and is four hours ahead of Greenwich Mean Time (GMT) and has a population of approximately 1.29 million.⁹ The official language is English but most people are bilingual and are equally fluent in English and French. Creole and a number of oriental languages are also spoken.¹⁰ The Mauritian currency is the rupee (MR).

Mauritius is a sovereign state within the British Commonwealth and is a multi-party democracy. The head of state is the President of the Republic who is elected by the National Assembly.¹¹

⁸ T Legwaila 'Tax characteristics of an ideal holding company location' (2012) available at <http://www.saflii.org.za/za/journals/DEJURE/2012/3.pdf> page 82 accessed on 30 January 2014.

⁹ Statistics Mauritius, available at <http://statsmauritius.gov.mu/English/StatsbySubj/Pages/Populationjanjun13.aspx> accessed on 11 January 2014

¹⁰ Discover Mauritius, available at http://www.mauritius.net/general_info/index.php accessed on 11 January 2014

¹¹ Mauritius: Country and Foreign Investment Regime, available at <http://www.lowtax.net/lowtax/html/jmucfir.html> accessed on 11 January 2014

Mauritius has a hybrid legal system and is a mixture of English Common Law and French Civil Law. Company and procedural law is based on English law. The Supreme Court of Mauritius is the highest court in the republic.¹² Over the past ten years commercial legislation has undergone dramatic changes to cater for onshore and offshore activities. Examples of amended legislation are the Companies Act 2001, the Securities Act 2005, the Financial Services Act 2007 and the Insolvency Act 2009 have all been promulgated to make Mauritius more appealing for potential investors.¹³

Over the course of four decades, Mauritius has grown from an isolated mono-crop dependent country into a services-led economy enjoying sustained growth. The Mauritian economy rests on five pillars, namely sugar, tourism, textile, financial services and Information and Communication Technology.¹⁴ Mauritius is a dynamic economy and is well served by business and communications infrastructure. The government actively encourages foreign investment and offshore activity and to ensure regulation established the Financial Services Commission which replaced the Mauritius Offshore Business Activities Authority (MOBAA) in 2001. These bodies regulate foreign direct investments, trust services, trading and pooled or mutual fund programmes.¹⁵ As a result of the governments pursuance of foreign investment there is a very clear distinction between the 'onshore' and 'offshore' sectors. Foreigners need specific permission from the Prime Minister's office before they can own shares in an onshore

¹² Mauritius: Country and Foreign Investment Regime, available at <http://www.lowtax.net/lowtax/html/jmucfir.html> accessed on 11 January 2014

¹³ C&A Law , available at http://www.calaw.mu/en/mauritian_legal_system.html accessed on 11 January 2014

¹⁴ BDO Mauritius, available at <http://www.bdo.mu/about-mauritius.php> accessed on 11 January 2014

¹⁵ Mauritius: Country and Foreign Investment Regime, available at <http://www.lowtax.net/lowtax/html/jmucfir.html> accessed on 11 January 2014

company, while Mauritians are barred from taking part in offshore activities.¹⁶

As English is the official language, communication is not a barrier for business in Mauritius. Based on the latest rankings, Mauritius was ranked 20 out of 189 countries in terms of ease of doing business and 1st out of 47 African countries.¹⁷

3.2 Mauritius Corporate Tax System

The administration of the Income Tax Act is governed by the Income Tax Act 1995.¹⁸ Mauritius runs a self-assessment tax system based on the residence concept. A Mauritian tax resident is liable to tax on their worldwide income while a non-resident is taxed on Mauritian source income. A company is treated as resident in Mauritius if it is incorporated in Mauritius or has its central management and control in Mauritius.¹⁹

The Income Tax Act does not itself define the meaning and scope of the concept “central management and control” however the current practice is that the tax authorities will refer to United Kingdom case law to determine what constitutes “central management and control”. The case law refers to the origin of the decision making process in running the operations of the company. Thus, if the key decisions in running the company are taken in Mauritius the company will be tax resident in Mauritius.²⁰

¹⁶ Mauritius: Country and Foreign Investment Regime, available at <http://www.lowtax.net/lowtax/html/jmucfir.html> accessed on 11 January 2014

¹⁷ World Bank *Doing Business 2014*, available at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB14-Full-Report.pdf> accessed 11 January 2014

¹⁸ Mauritius Revenue Authority, available at <http://mra.gov.mu/> accessed on 14 January 2014

¹⁹ Income Tax Act 1995, Section 73(b).

²⁰ Business Consult, available at <http://www.businessconsult.mu/bc/> accessed on 14 January 2014

The current corporate tax rate in Mauritius is 15% on taxable income making it a low tax jurisdiction. The average global statutory corporate tax rate according to the Paying Taxes study was 24.2% in 2012.²¹ To enhance the attractiveness of setting up a holding company in Mauritius, the Mauritian government provides for the application of Global Business Licences for Mauritian incorporated companies which are owned by non-residents. On receiving such status the maximum corporate tax rate is reduced to 3% and in some cases depending on the withholding tax levied in a foreign jurisdiction could be reduced to 0%. This is discussed in detail below.

3.3 Companies holding Global Business Licences

The Global Business Licence (GBL) is a special tax regime implemented by the Mauritian government to attract foreign direct investment into Mauritius. There are two licences which can be applied for: the GBL1 and the GBL2.²² A company awarded a GBL1 or GBL2 are known as Global Business Companies (GBC). A GBC is regulated and licensed by the Financial Services Commission of Mauritius (FSC).²³

In order to obtain a GBL1 or GBL2 specific requirements must be met. The ownership of a GBC is restricted to non Mauritian residents and the offshore business activities must be conducted with persons who are not resident²⁴

²¹ Corporate Income Tax – a global analysis, available at http://www.pwc.com/en_GX/gx/paying-taxes/pdf/pwc-corporate-income-tax-report.pdf accessed on 18 January 2014.

²² Mauritian Revenue Authority, available at <http://mra.gov.mu/> accessed on 18 January 2014.

²³ Financial Services Act of 2007, see Section 71(1).

²⁴ For the purposes of determining residency for an individual in Mauritius. A “resident” is an individual who has his domicile in Mauritius, but does not include an individual who is only in Mauritius for temporary purposes nor does it include an individual who is not present in Mauritius for more than 183 days in the relevant income tax year or for more than 270 days

in Mauritius and in non-Mauritian currency. A GBC may also not hold immovable property, other than an office space to conduct its business if necessary, in Mauritius. It may also not hold any share, debenture, security or any interest in a domestic company or have a Mauritian currency bank account unless it is solely used for normal day to day business transactions in Mauritius.²⁵

According to the FSC, a company applying for a GBL must pass the ultimate business purpose test which assesses whether the applicant will be conducting business outside Mauritius. In applying this test to an application for a GBL, the FSC assesses whether the ultimate purpose of the applicant's proposed activity is an investment to be made or a service to be provided outside Mauritius.²⁶

As stated in section 1 above, an IHC is incorporated as a company and interposed between a foreign operating company and the ultimate holding company. An IHC can therefore be incorporated in Mauritius holding a global business license as it does not have to trade in Mauritius nor hold immovable property in Mauritius.

3.3.1 Global Business Company 2 (GBC2)

A GBC2 is a private company²⁷ incorporated under the Companies Act 2001. The company must be wholly owned by persons not resident in Mauritius and operate exclusively outside Mauritius. The legislative regime

over three consecutive fiscal years. See Mauritius Revenue Authority, available at <http://mra.gov.mu/> accessed on 18 January 2014.

²⁵ Financial Services Act of 2007, see Section 73

²⁶ Financial Services Commission, *Fact Sheet Global Business* available at <http://www.fscmauritius.org/media/88149/fact-sheet-on-global-business-fsc-final-22-march-2013.pdf> accessed 18 January 2014

²⁷ See section 71(3) of the Financial Services Act of 2007

governing a GBC2 is more flexible than a GBC1.²⁸ A GBC2 may either be setup with direct incorporation with limited by shares or by guarantee or simply unlimited. A GBC2 may also be a Limited Life Company. In order for a GBC2 to obtain a global business licence category 2 (GBL2) it must adhere to the following:²⁹

- It must be a private company incorporated under the Companies Act 2001;
- Shall not conduct business with persons resident in Mauritius or in Mauritian currency;
- Not hold immovable property in Mauritius;
- Not invest on the Mauritian Stock Exchange;
- Not offer the Mauritian public subscription for shares;
- Not hold any share, debenture or any interest in companies registered in Mauritius other than an GBC1;
- Shall not engage or conduct business activities outlined in the Fourth Schedule of the FSA namely: banking, financial services, asset management, credit finance, registered office facilities, secretarial services, nominee services, trustee services by way of business or funds management;
- Have a registered office and registered agent registered in Mauritius.

Following the above outlined restrictions a GBC2 is generally used to carry on the actives such as non financial consultancy, IT services, logistics, marketing, shipping, ship management, passive investment holding and once off transactions using a special purpose vehicle. In addition the FSC have the authority to approve any additional activities upon application.³⁰

²⁸ HSBC, *Mauritius: A Guide to Global Business* available at https://www.hsbc.co.mu/1/PA_ES_Content_Mgmt/content/website/documents/guide_to_global_business.pdf accessed on 19 January 2014

²⁹ See section 71 to section 79 of the Financial Services Act of 2007

³⁰ Alliance Mauritius: *Global Business Licence Company 2* available on <http://www.alliance-mauritius.com/gbl2-company,29.html> access on 19 January 2014

3.3.1.1 Taxation of a GBC2

A GBC2 is deemed not to be a tax resident of Mauritius and is therefore not liable to pay tax on any income to the Mauritian authorities. As the GBC2 is deemed to be a non resident it cannot benefit from the Mauritian DTA network³¹ and as such is not the ideal company to use as an IHC.

3.3.2 Global Business Company 1 (GBC1)

Governed under the Financial Services Act 2007 (FSA) and Companies Act 2001 a GBC1 is a Mauritian entity which holds a valid global business licence and which carries on an approved qualified global business activity outside Mauritius as approved by the FSA.³² A GBC1 may be locally incorporated or may be registered as a branch of a foreign company. The business of a GBC1 must be conducted in foreign currency other than for day-to-day transactions and must not do business in Mauritius, other than to take professional advice, employ local labour, and to rent property.³³

A GBC1 can be a company limited by shares or by guarantee. It can be incorporated with a minimum of one director and a minimum of one shareholder. At least one director must be resident in Mauritius at all times. A GBC1 is required to be a tax resident of Mauritius if it is to take advantage of the Mauritian DTA network it has signed with 39 countries worldwide.³⁴

³¹ HSBC, *Mauritius: A Guide to Global Business* available at https://www.hsbc.co.mu/1/PA_ES_Content_Mgmt/content/website/documents/guide_to_global_business.pdf accessed on 19 January 2014

³² Financial Services Commission, *Fact Sheet Global Business* available at <http://www.fscmauritius.org/media/88149/fact-sheet-on-global-business-fsc-final-22-march-2013.pdf> accessed 18 January 2014

³³ Mauritius GBC1 Company. available at <http://www.lowtax.net/lowtax/html/jmucos.html#gbc1> accessed 19 January 2014

³⁴ Mauritius Revenue Authority, *Double Taxation Agreements* available at <http://www.mra.mu/index.php/taxation/double-taxation-agreements> accessed on 18 January 2014

As one of the main criteria's in incorporating an IHC in a particular country is to access the DTA network, a GBC1 is the ideal company structure to use as an IHC.

The FSC provides that no person may conduct any qualified global business activities unless that person holds a valid GBL1.³⁵ A qualified global business for the purposes of a GBL1 is any business or activity including financial business activities. The Second Schedule to the FSA³⁶ lists the following activities which qualify as financial business activities: assets management, credit finance, custodian services (non-CIS), distribution of financial products, factoring, leasing, occupational pension scheme, pension fund administrators, pension scheme management, retirement benefits scheme, superannuation funds, registrar and transfer agent and treasury management. In terms of the FSC a GBC1 may only undertake global business activities as set out in the business plan filed with the FSC at the time of application for the licence.³⁷ Any change to a business plan or business activities undertaken by a GBC1 must be notified to the FSC.

3.3.2.1 Tax Residency of a GBC1

A GBC1 is required to be a tax resident of Mauritius³⁸ and must therefore apply for a tax residency certificate (TRC). Once a TRC has been approved a GBC1 can benefit fully from the Mauritian DTA network. To be eligible for a TRC, the 'central control and management' of the GBC1 must be

³⁵ See section 71(2) of the Financial Services Act of 2007

³⁶ See Financial Services Act of 2007

³⁷ Financial Services Commission, *Fact Sheet Global Business* available at <http://www.fscmauritius.org/media/88149/fact-sheet-on-global-business-fsc-final-22-march-2013.pdf> accessed 18 January 2014

³⁸ See Section 71(1) of the Financial Services Act of 2007

conducted in Mauritius.³⁹ 'Central control and management from Mauritius' is established if the following applies:⁴⁰

1. The company must have at least two resident directors in Mauritius;
2. The company must at all times have its principal bank account in Mauritius;
3. The registered office and statutory records must at all times remain in Mauritius;
4. The company's auditor's must be in Mauritius;
5. The company's board meetings must include the two Mauritian directors and initiated and chaired from Mauritius. All major decisions must be seen to be taken from Mauritius.

In order to ensure the GBC1 is tax resident in Mauritius the above requirements must be met. If an investor incorporates a GBC1 to act as an IHC and the above requirements are not met this could result in the GBC1 being liable to a higher rate of tax in Mauritius namely 15% instead of 3% and the investor might face additional tax consequences in their home country.

3.3.2.2 Taxation of a GBC1

The corporate tax rate in Mauritius is currently 15%⁴¹ on profits. However this rate can be reduced by any foreign tax paid in the source country or by applying a presumed tax credit.

³⁹ Business Consult Mauritius, available at http://www.businessconsult.mu/bc/?page_id=20 accessed on 25 January 2014

⁴⁰ See Section 71(4) of the Financial Services Act of 2007

⁴¹ Mauritian Revenue Authority, available at <http://mra.gov.mu/index.php/taxation/corporate-taxation> accessed 26 January 2014

a) Foreign tax credit

A foreign tax credit is a mechanism used to reduce or eliminate double taxation where the same income is subject to tax in more than one country. The foreign tax credit is granted in the resident taxpayer's country and generally reduces the domestic tax payable by the foreign tax paid. In order to apply for a foreign tax credit the taxpayer must have actually paid the tax. Section 77 of the Mauritian Income Tax Act of 1995 provides for the foreign tax credit and states the following:

Credits in respect of foreign tax

(1) Where a taxpayer derives income which is subject to foreign tax, the amount of foreign tax so paid shall be allowed as a credit against income tax payable in Mauritius in respect of that income.

(2) The credit in respect of foreign tax shall, in the case of a dividend, include credit for any foreign tax imposed on the profits out of which that dividend is directly or indirectly paid.

(3) The Minister may, by regulations, provide for the implementation of the provisions of this section and for the granting of credit for foreign tax in such manner and on such conditions as he thinks fit.⁴²

If the tax paid in the foreign source country is equal to or greater than the Mauritian corporate rate of 15% then the effective tax rate will be reduced to nil in Mauritius.

b) Presumed tax credit

A GBC1 has the option of applying a presumed foreign tax credit which is available via the Mauritian tax legislature. A presumed tax credit is not based on taxes actually paid and is an alternative to the foreign tax credit discussed above.

⁴² Section 77 of the Mauritian Income Tax Act of 1995

The Mauritian tax legislation provides for a presumed tax credit of 80% of the Mauritian tax chargeable where no documentation is held to support the payment of foreign tax. As a result, only 20% of the income is taxable at 15% resulting in an effective tax rate of 3%.⁴³

3.4 Aspects that make Mauritius a popular IHC jurisdiction

Multinational organisations have for many years seen Mauritius as the preferred gateway to invest into Africa and other countries worldwide due to its investment and business platform it provides. One of the main reasons investors choose Mauritius is due to the tax system specifically catering for the interposition of holding companies to hold investments in foreign jurisdictions.⁴⁴

Mauritius combines the traditional advantages of an offshore financial centre (no capital gains tax, no withholding tax, no exchange controls and free repatriation of profits and capital) with the distinct advantages of an extensive network of DTAs.⁴⁵

A GBC1 as discussed above has access to Mauritius' DTA network as a result of it being a tax resident. Mauritius currently has 39⁴⁶ signed treaties

⁴³ Kross Border: Mauritius tax credit, available at <http://krossborder.com/mauritius/tax.html> accessed on 26 January 2014

⁴⁴ T Legwaila 'Tax characteristics of an ideal holding company location' (2012) available at <http://www.saflii.org.za/za/journals/DEJURE/2012/3.pdf> pg 12 accessed on 2 January 2014.

⁴⁵ Investec Trust (Mauritius) Limited: Mauritius as a gateway for investment into Africa, available at www.intestetrust.com accessed on 26 January 2014

⁴⁶ Australia, Barbados, Belgium, Botswana, Croatia, Cyprus, Sri Lanka, France, Germany, India, Italy, Kuwait, Lesotho, Luxembourg, Madagascar, Malaysia, Monaco, Mozambique, Namibia, Nepal, Oman, Pakistan, Bangladesh, People's Republic of China, Rwanda, Senegal, Seychelles, Singapore, South Africa, State of Qatar, Swaziland, Sweden, Thailand, Tunisia, Uganda, United Arab Emirates, United Kingdom, Zambia, Zimbabwe. Mauritius Revenue Authority: Available at <http://www.mra.mu/index.php/taxation/double-taxation-agreements>

with countries around the world of which 14⁴⁷ are in force and a further 5⁴⁸ are waiting ratification with African countries.⁴⁹ In addition, as Mauritius' tax legislation has been tailored to attract foreign direct investment the effective tax rate for a GBC1 of between 3% and nil depending on individual circumstances with regard to foreign tax credit utilisation makes the tax regime very attractive compared to other tax jurisdictions.

In addition to the DTA network, as Mauritius does not have exchange control, transfer pricing or controlled foreign company (CFC) regulations⁵⁰ it adds to the ease of doing business in Mauritius. An important point to take note of is that CFC rules in South Africa will apply to shareholders of a GBC1 if South African residents collectively hold more than 50% of the shares in the GBC1.

Being an African nation, Mauritius has signed Investment Promotion and Protection Agreements (IPPAs) with a number of African countries. Although Mauritius also has significant tax advantages to offer through its network of DTAs, the existence of IPPAs is perhaps an even more important advantage for investors who wish to invest in African countries where there might be a real or perceived increased risk of nationalisation or confiscation of assets. The IPPAs encourage and protect investments by minimising the possibility of any deprivation of investments due to nationalisation or confiscation of assets. In the worst case scenario, any deprivation of investments will have to be justly compensated and the agreements provide

⁴⁷ Botswana, Lesotho, Madagascar, Mozambique, Namibia, Rwanda, Senegal, Seychelles, South Africa, Swaziland, Tunisia, Uganda, Zambia, Zimbabwe.

⁴⁸ Congo, Egypt, Gabon, Kenya, Nigeria

⁴⁹ Mauritius Revenue Authority, *Double Taxation Agreements* available at <http://www.mra.mu/index.php/taxation/double-taxation-agreements> accessed on 18 January 2014

⁵⁰ Trust (Mauritius) Limited: Mauritius as a gateway for investment into Africa, available at www.intestctrust.com accessed on 26 January 2014

arrangements for the settlement of disputes between investors and the contracting states. Mauritius currently has IPPAs with 20⁵¹ African countries. 5⁵² of these are signed and in force and the remaining 15 are signed but awaiting ratification.

Mauritius is a member of a World Bank agency called Multilateral Investment Guarantee Agency (MIGA). MIGA provides non-commercial guarantees (effectively political insurance) for cross border investments in developing countries. Companies incorporated in Mauritius are eligible for MIGA guarantees. The guarantees protect investors against the risks of transfer restrictions, expropriation, war and civil disturbances, breach of contract and failure to honour sovereign financial obligations.⁵³

In addition to the above Mauritius is also a member of all the main African regional organisations which provide access to markets in the African region such as the African Union, the Southern African Development Community (SADC), the Common Market for Eastern and Southern Africa (COMESA) and the Indian Ocean Rim – Association for Regional Cooperation (IOR-ARC).⁵⁴

In addition to the fiscal advantages which Mauritius has to offer, there are a number of additional non fiscal advantages which should be taken into account. Mauritius is a well regulated business jurisdiction which has a good

⁵¹ Benin, Botswana, Burundi, Cameroon, Chad, Comores, Congo, Ghana, Guinea, Kenya, Madagascar, Mauritania, Mozambique, Nigeria, Rwanda, Senegal, South Africa, Swaziland, Tanzania, Zimbabwe. Afrasia Bank, available at http://www.afrasiabank.com/pdf/Mauritius_The_Gateway_to_Africa_and_Asia.pdf accessed 30 January 2014

⁵² Burundi, Madagascar, Mozambique, Senegal, South Africa.

⁵³ Investec Trust (Mauritius) Ltd: Mauritius as a gateway for investment into Africa. Available at www.investectrust.com

⁵⁴ Investec Trust (Mauritius) Ltd: Mauritius as a gateway for investment into Africa. Available at www.investectrust.com

record of adherence to international standards of best practice and offers a convenient time zone location. Mauritius also enjoys an abundance of professional service providers at a relatively low cost, an educated and multilingual workforce, with English and French being the main business languages, as well as economic and political stability. Mauritius has a hybrid legal system consisting of English and French law, and the Privy Council in England is still the final court of appeal.⁵⁵

4 South Africa

4.1 Introduction

South Africa, officially the Republic of South Africa is located at the southern tip of the African continent and shares its borders with Namibia, Botswana, Zimbabwe, Mozambique and Swaziland. South Africa is situated in a convenient time zone being two hours ahead of Greenwich Mean Time (GMT +2). South Africa is a nation of diversity, with a population of nearly 52 million⁵⁶ and a wide variety of cultures, languages and religious beliefs. The various ethnic groups in South Africa are African, white, coloured and Indian/Asian with the predominant religion being Christianity.⁵⁷

South Africa has 11 official languages: Afrikaans, English, isiNdebele, isiXhosa, isiZulu, Sepedi, Sesotho, Setswana, siSwati, Tshivenda, and

⁵⁵ Mauritius: Country and Foreign Investment Regime, available at <http://www.lowtax.net/lowtax/html/jmucfir.html> accessed on 30 January 2014

⁵⁶ South African population, available at <http://www.southafrica.info/about/people/population.htm#.Uu4Sgj2Syik> accessed 2 February 2014

⁵⁷ South Africa Geography, available at http://www.lowtax.net/lowtax/html/south_africa/south_africa_country_and_foreign_investme nt.asp#population accessed 1 February 2014

Xitsonga. English and Afrikaans are the main languages used for business purposes.⁵⁸

The Constitution of South Africa is the supreme rule of law in the country. The primary sources of South African law are Roman-Dutch mercantile law and personal law with English Common law.⁵⁹

South Africa is an emerging market with a well developed financial and legal sector. Telecommunications are the best developed on the continent⁶⁰ and the road infrastructure network is well maintained. South Africa's ports and shipping handle most of the country's exports and are transit hubs for trade to the Americas, Europe, Asia and Africa's east and West coasts.⁶¹ In addition, South Africa has 10 main airports and three international airports.

South Africa has developed a well regulated banking system that compares favourably with many industrialised countries. According to the latest World Economic Forum Competitive Survey 2012/13, South African banks are rated 2nd out of 144 countries for soundness, while the country was rated 3rd for financial sector development. Currently, the South African banking industry consists of 17 registered banks, 2 mutual banks, 12 local branches

⁵⁸ South Africa Geography, available at http://www.lowtax.net/lowtax/html/south_africa/south_africa_country_and_foreign_investment.asp#population accessed 1 February 2014

⁵⁹ South Africa Law, available at http://en.wikipedia.org/wiki/South_Africa#Politics accessed 2 February 2014

⁶⁰ South Africa Business Environment, available at http://www.lowtax.net/lowtax/html/south_africa/south_africa_country_and_foreign_investment.asp#population accessed 2 February 2014

⁶¹ South Africa Business Environment, available at http://www.lowtax.net/lowtax/html/south_africa/south_africa_country_and_foreign_investment.asp#population accessed 2 February 2014

of foreign banks, and 41 foreign banks with approved local representative offices.⁶²

According to the World Bank's doing business report for 2014 South Africa was ranked 41st out of 189 countries in terms of doing business and 3rd out of 47 African countries.⁶³ Only Mauritius and Rwanda were above South Africa in terms of African countries surveyed.

4.2 South African Corporate Tax System

Prior to 2001 South Africa applied the source basis of tax meaning amounts were only subject to tax if they were from a South African source. The residence of a taxpayer was irrelevant. The source basis of tax was replaced by a residence basis for years of assessment commencing on or after 1 January 2001.⁶⁴ In terms of this basis South African residents are taxable on their worldwide income, regardless of the source of the income.

A company is regarded as a South African resident if it is incorporated in South Africa or if it has its place of effective management in South Africa.⁶⁵ An important point to note is that if a person, which includes a company, is deemed to be a resident of another country for the purposes of the

⁶² The Banking Association of South Africa, available at <http://www.banking.org.za/index.php/our-industry/2012-south-african-banking-sector-overview/> accessed 2 February 2014

⁶³ World Bank *Doing Business 2014*, available at <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB14-Full-Report.pdf> accessed 11 January 2014

⁶⁴ P Haupt *Notes on South African income tax* 33ed (2014) 24

⁶⁵ See section 1 of the Act of the definition of "gross income" read with definition of "resident". For a detailed discussion of residence requirements for companies in South Africa see South African Revenue Service *Interpretation Note 6: Resident: Place of Effective Management (Persons Other Than Natural Persons)(2002) para 3*. Also see South African Revenue Service *Discussion paper on Interpretation Note 6 Place of Effective Management (2011)*.

application of a double tax agreement which South Africa has with another country they are deemed not to be a resident of South Africa.⁶⁶

South Africa's corporate tax is currently 28%. The average global statutory corporate tax rate according to the Paying Taxes study was 24.2% in 2012.⁶⁷ As has been discussed above Mauritius has a corporate tax rate of 15% which can be reduced to a maximum of 3% if a GBC1 company is chosen. Capital gains are taxable at an effective rate of 18.648% for resident companies while non resident companies are only liable to capital gains on disposal of assets attributable to immovable property located in South Africa⁶⁸, subject to DTA provisions.

With regard to dividend distributions, South Africa implemented dividends tax with effect from 1 April 2012 at a flat rate of 15%⁶⁹. It replaced the secondary tax on companies (STC) which was levied at a flat rate of 10%. The dividends tax is a withholding tax, borne by the shareholder and applies only to dividends from South African companies and dividends from foreign companies listed on the South African stock exchange.⁷⁰

In addition to the above, the South African tax system contains provisions that impose tax on CFCs⁷¹ and foreign dividends⁷². The South African tax legislature also contains anti avoidance provisions such as transfer pricing⁷³ and thin capitalisation provisions.⁷⁴

⁶⁶ See section 1 of the definition of "resident"

⁶⁷ Corporate Income Tax – a global analysis, available at http://www.pwc.com/en_GX/gx/paying-taxes/pdf/pwc-corporate-income-tax-report.pdf accessed on 18 January 2014.

⁶⁸ See para 2(2) of the Eighth Schedule of the Act

⁶⁹ See section 64E of the Act

⁷⁰ P Haupt *Notes on South African Income Tax* 33ed (2014) 456

⁷¹ See section 9D of the Act

⁷² See section 10B of the Act read with para (k) of the definition of "gross income"

⁷³ See section 31(2) of the Act

Similar to the Mauritian tax regime, the South African tax regime grants credits for foreign taxes levied by foreign countries⁷⁵ and has an advanced tax ruling system⁷⁶ which will give taxpayers certainty in applying the tax laws in a particular proposed situation.

Exchange control in South Africa is monitored by the South African Reserve Bank (SARB). Every transaction in South Africa that involves a movement of money into or out of the country is regulated by the exchange controls.⁷⁷ The SARB delegate some of their authority to local authorised dealers, such as banks, who supervise transactions on their behalf. In the case of companies, payments made to or received from a foreign party are governed by the regulations and transfers may only occur once approval has been granted by SARB or the authorised dealer. Loans granted by foreign investors are also subject to exchange control.⁷⁸

4.3 Background to the new headquarter company regime

In the 2010 Budget review The South African National Treasury announced it intended to create a business environment that would promote South Africa as a gateway to investment into Africa. The Explanatory Memorandum of the Taxation Laws Amendment Bill 2010 stated the following.⁷⁹

⁷⁴ See section 31 of the Act read with South African Revenue Service *Draft Interpretation Note on Thin Capitalisation*

⁷⁵ See section 6quat and section 6quin of the Act

⁷⁶ See Tax Administration Act No.28 of 2011 chapter 7

⁷⁷ South African Reserve Bank *Exchange Control* available at <http://www.resbank.co.za/> accessed 2 February 2014

⁷⁸ Exchange Control Regulations available at <http://www.moneytransfersouthafrica.org/foreign-exchange-regulations/> accessed 2 February 2014

⁷⁹ National Treasury *Explanatory Memorandum of the Taxation Laws Amendment Bill, 2010* pg 77

South Africa is the economic powerhouse of Africa. South Africa's location, sizable economy, political stability and overall strength in financial services make South Africa an ideal location for the establishment of regional holding companies by foreign multinationals. Furthermore, South Africa's network of tax treaties provides ready access to other countries in the region. South Africa is therefore a natural holding company gateway into the region.

The tax proposals regarding the new headquarter company (HQC) regime were introduced into the South African tax system via the Taxation Laws Amendment Act, No.7 of 2010 (TLA 2010) and came into effect from 1 January 2011.

In the Explanatory Memorandum to the TLA 2010 three sets of tax rules were identified as barriers that may prevent South Africa from encouraging the establishment of headquarter companies. These barriers were.⁸⁰

- Controlled foreign company (CFC) rules:

Firstly, the application of the CFC regime means that foreign shareholders of a South African holding company will be exposed to a double administrative tax burden if their home country also has CFC rules. It is also questionable whether the application of South Africa's CFC rules makes any sense if the bulk of the holding company's funds originate from abroad.

- Tax on outgoing dividends:

At the time the explanatory memorandum of the TLA 2010 was published, secondary tax on companies (STC) was still levied at 10%

⁸⁰ National Treasury *Explanatory Memorandum of the Taxation Laws Amendment Bill, 2010* pg 77

on the outgoing dividends from a South African resident company. Going forward, the new dividends tax would have imposed a withholding tax of 15% on any dividends declared by such company.

- Thin capitalisation rules:

If the South African holding company is financed with debt capital, the thin capitalisation rules as set out in section 31 of the Act serve as another critical barrier. The thin capitalisation rules are especially problematic if the foreign investor makes loans to the holding company with the holding company on-lending those funds to another foreign location. Application of thin capitalisation to this arrangement would most likely leave the holding company with non-deductible interest payments owed to the foreign investor while being saddled with corresponding includible interest income from the on-lending.

The memorandum proposed the following to alleviate the aforementioned barriers:⁸¹

- Foreign subsidiaries of a qualifying holding company will not be treated as a CFC merely because the holding company has significant equity interests in those foreign subsidiaries. This will be established by deeming the holding company to be a foreign resident and will result in the CFC status of a foreign subsidiary of a qualifying holding company to be determined based on the indirect ownership of the qualifying holding company's shareholders.⁸² Only if these indirect owners are more than 50% South African will the foreign subsidiary qualify as a CFC. If the foreign subsidiary qualifies as a CFC, the attribution of the tainted income of CFC will take place at the shareholder level of the qualifying holding company.

⁸¹ National Treasury *Explanatory Memorandum of the Taxation Laws Amendment Bill, 2010* pg 78

⁸² Section 16 of the TLA 2010 specifically excluded a headquarter company from the definition of a CFC in section 9D of the Act

- Dividends declared by a holding company will not be subject to STC,⁸³ or subsequently, the new dividends tax as the holding company will be deemed to be a foreign resident resulting in the dividends potentially qualifying for the participation exemption.
- The holding company will not be deemed to violate the thin capitalisation rules merely because of the existence of back-to-back cross-border loans. For the purposes of transfer pricing rules, the holding company does not have to take into account any foreign loans it receives which are subsequently on lent to foreign subsidiaries in which it holds at least 20% of the equity shares.⁸⁴ However, interest incurred on such loans will be ring-fenced and deductible only against interest earned on loans advanced to foreign subsidiaries.⁸⁵
- Foreign creditors of the qualifying holding company will be exempt from the pending withholding tax on interest in respect to back-to-back loans,
- Headquarter companies will be deemed to be foreign residents for the purposes of reorganisation rollover relief and may subsequently not benefit from the provisions. This was entered in order to discourage companies from artificially qualifying as holding companies.

⁸³ Section 64B of the Act was amended by section 68 of the TLA 2010

⁸⁴ Section 56 of the TLA 2010

⁸⁵ Section 38 of the TLA 2010

The criteria for qualifying as a HQC was set out in section 1 of the Act. A company had to comply with the following:⁸⁶

- Each shareholder (whether alone or together with any group company) must hold 20% or more of the ordinary shares and voting rights in the HQC;
- 80% or more of the costs of the assets of the HQC must be attributable to interests in ordinary shares in and loans and IP licensed to foreign companies in which the HQC (whether alone or together with any group company) holds at least 20% of the ordinary shares and voting rights;
- 80% or more of the total receipts and accruals (in the form of dividends, interest, royalties, management fees and disposal proceeds) of the HQC must derive from qualifying foreign companies.

The first two requirements from the above must be satisfied for each day of the HQC existence. This 'uninterrupted' requirement applied to existing companies seeking to enter into the new regime as of the effective date i.e. 1 January 2011 and to new companies established after that date. The 'uninterrupted' requirement did not however apply in respect of the third point above.

The Taxation Laws Amendment Act, No. 24 of 2011 (TLA 2011) introduced amendments to the headquarter company regime. The most significant changes were the insertion of section 9H in the Act⁸⁷ and the deletion of the headquarter definition from section 1 of the Act which became the new section 9I of the Act.⁸⁸

⁸⁶ National Treasury *Explanatory Memorandum of the Taxation Laws Amendment Bill, 2010* pg 78

⁸⁷ See section 26 of the TLA 2011

⁸⁸ See section 27 of the TLA 2011

Section 9H of the Act sets out the taxation provisions in regard to a change in residence, ceasing to be a CFC or becoming a headquarter company. In terms of this section a company which selects to become a headquarter company will be required to sell all its assets (subject to certain exemptions) at market value immediately prior to a change in residency occurs. Immediately thereafter, the company will then be required to acquire these assets at market value.⁸⁹

4.4 Current headquarter company regime

A headquarter company (HQC) is any company which is South African tax resident⁹⁰ but is treated like a non-resident company. In order for a company to be a HQC an election must be made for each year of assessment⁹¹ and so can be changed in the next year of assessment. When a normal company elects a HQC status it is treated as having become non-resident in that year⁹² which can result in various 'exit taxes' being incurred.

In order for a company to qualify as an HQC the following requirements must be met:⁹³

- each shareholder in the HQC, whether alone or together with any other company forming part of the same group of companies as that

⁸⁹ See section 9H of the Act

⁹⁰ See section 9I of the Act read with definition of "resident". A company is resident in South Africa if it is incorporated, established or formed in South Africa, or its place of effective management is in South Africa. A company will not be resident in South Africa if a double tax agreement deems it to be a resident of another country. For a detailed discussion of residence requirements for companies in South Africa see South African Revenue Service *Interpretation Note 6: Resident: Place of Effective Management (Persons Other Than Natural Persons)(2002) para 3*. See also South African Revenue Service *Discussion paper on Interpretation Note 6 Place of Effective Management (2011)*.

⁹¹ See section 9I(1) of the Act

⁹² See section 9H of the Act

⁹³ See section 9I(2) of the Act

shareholder, must hold 10% or more of the equity shares and voting rights in the HQC for the entire year of assessment;

- 80% or more of the cost of the total assets of the HQC at year end (and of all previous years) must have been attributable to one or more of the following:
 - any interest in equity shares in;
 - any debt owed by; or
 - any intellectual property that is licensed by that HQC to; any foreign company in which the HQC (alone or together with any other company forming part of the same group of companies as the HQC) held at least 10% of the equity shares and voting rights ('qualifying shareholding'); and

- If the gross income of the HQC exceeds R5 million in the year of assessment, 50% or more of that gross income must consist of the following:
 - rental, dividends, interest, royalty or service fees paid or payable by any foreign company in which the HQC held a qualifying shareholding; or
 - proceeds from the disposal of any qualifying shareholding in a foreign company; or
 - proceeds from the disposal of any intellectual property that was licensed to a foreign company in which the HQC held a qualifying shareholding.

- The HQC must submit annual information to National Treasury in the manner and form prescribed by the Minister of Finance.⁹⁴

⁹⁴ See section 9l(4) of the Act

4.5 Taxation of an HQC

As the HQC is a South African tax resident it will be subject to the South African income tax rate currently 28% on all its normal income however it will qualify for an exemption from income tax in respect of foreign dividends it receives from a foreign company in which it holds a qualifying interest.⁹⁵ This exemption is known as the participation exemption.

4.5.1 Dividends paid and received

As stated in section 4.2 above South Africa implemented dividends withholding tax which is levied at 15%.⁹⁶ A dividend declared by a HQC to its shareholders is not subject to dividends tax⁹⁷ as a dividend paid by an HQC is defined as a 'foreign dividend'.⁹⁸ In terms of section 10B of the Act dividends received by shareholders of the HQC will be exempt from income tax under the participation exemption as each shareholder will hold at least 10% of the equity and voting rights in the HQC.

4.5.2 Royalties

Royalties paid by a South African resident to a non-resident are currently subject to a withholding tax of 12%⁹⁹ unless a DTA applies. With effect from 1 January 2015 the withholding tax will increase to 15%. A payment made by an HQC to a non-resident is exempt from the withholding tax.¹⁰⁰

⁹⁵ See section 10B of the Act

⁹⁶ See section 64E(1) of the Act

⁹⁷ See section 64E(1) of the Act

⁹⁸ See section 10B(1)(b) of the Act

⁹⁹ See section 49B of the Act

¹⁰⁰ See section 49D(b) of the Act

Royalty payments made by an HQC to a non-resident are subject to ring-fencing provisions¹⁰¹ where the royalty deduction claimable for the year of assessment is limited to the amount received or accrued from any foreign company in which the HQC holds the qualifying shareholding. Any disallowed expense can be carried forward to the next and succeeding years of assessment until it is used up.¹⁰²

4.5.3 Interest

Interest paid by an HQC to a non-resident will be exempt from interest withholding tax when it comes into effect from 1 January 2015 if the amount paid to the non-resident is in respect of financial assistance granted to the HQC.¹⁰³

Interest payments made by an HQC to a foreign lender are subject to ring-fencing provisions¹⁰⁴ if the financial assistance¹⁰⁵ received has been provided by a foreign lender who is not a company or the foreign lender is a company in which the HQC holds a qualifying shareholding. The ring-fencing restricts the interest deduction claimable for the year of assessment to the amount of interest income received from the on-lending of the financial assistance to a foreign company in which the HQC holds the qualifying shareholding. Any disallowed interest can be carried forward to the next and succeeding years of assessment until it is used up.¹⁰⁶

¹⁰¹ See section 20C(2A) of the Act

¹⁰² See section 20C(3) of the Act

¹⁰³ See section 50D(1)(a)(i)(cc) of the Act

¹⁰⁴ See section 20C(2) of the Act

¹⁰⁵ See definition of 'financial assistance' in section 31 of the Act. 'Financial assistance' means any loan, advance or debt.

¹⁰⁶ See section 20C(3) of the Act

4.5.4 Transfer pricing and thin capitalisation

A HQC will be subject to thin capitalisation rules contained in section 31 of the Act. For purposes of determining whether a HQC is thinly capitalised, foreign loans received by the HQC and on-lent to foreign companies in which the HQC holds a qualifying shareholding will be left out of the calculation. This exclusion however comes at a price as the interest incurred on such loans will be ring-fenced as discussed above. The transfer pricing rules will not apply to the following transactions:¹⁰⁷

- financial assistance granted to a HQC by a non-resident provided the financial assistance is directly applied by the HQC to provide financial assistance to a foreign company in which the HQC holds a qualifying shareholding. Therefore, interest-free loans to qualifying foreign companies will not be susceptible to transfer pricing adjustment whereby interest is imputed on the loans for tax purposes.
- financial assistance granted by a HQC to a foreign company in which the HQC holds a qualifying shareholding; or
- transactions relating to the granting of the use, right of use or permission to use any intellectual property¹⁰⁸ where, *inter alia*, such right of use is granted by a foreign person to the HQC and the HQC does not make use of the intellectual property other than to grant that right of use to any foreign company in which the HQC holds a qualifying shareholding.

¹⁰⁷ See section 31(5) of the Act

¹⁰⁸ As defined in section 23I(1) of the Act

4.5.5 Controlled foreign company (CFC)

The CFC status of a foreign company will be determined by reference to the indirect ownership of the HQC's shareholders.¹⁰⁹ Only if the indirect shareholders are more than 50% South African will the foreign company qualify as a CFC. If the foreign company qualifies as a CFC, income attribution will occur at the level of the South African shareholders of the HQC. This result will be achieved by treating the HQC as a foreign resident for purposes of South Africa's CFC rules.

4.5.6 Capital Gains

A HQC is a South African resident and if it holds the relevant qualifying shareholding in a foreign company it is entitled to disregard any capital gain or capital loss upon disposal of such equity shares it holds in the foreign company.¹¹⁰ This exemption does not apply if 80% or more of the market value of the equity shares of the foreign company, at the time of disposal, is attributable directly or indirectly to an interest in immovable property in South Africa.

4.5.7 Exchange Control

In terms of SARB a HQC will be treated, for exchange control purposes, as a non-resident company, other than for reporting obligations.¹¹¹ On this basis transactions between South African entities and a HQC will be viewed as transactions with non-residents. A HQC may invest offshore without any exchange control restrictions and furthermore borrow without restriction

¹⁰⁹ See definition of 'Controlled foreign Company' in section 9D of the Act.

¹¹⁰ See para 64B(2) of the Eighth Schedule to the Act

¹¹¹ See section B2(B)(vi)(d) of the Exchange Control Rulings issued to Authorised Dealers

from abroad.¹¹² These funds may also be deployed locally or offshore since these transactions are regarded as occurring outside South Africa.

A HQC which meets the following shareholding and assets criteria may register with the Financial Surveillance Department (FSD) to invest offshore without restriction:¹¹³

- no shareholder in the HQC, whether alone or together with any other company in the same group of companies, may hold less than 10% of the shares and voting rights;
- the shares and/or debt of the HQC may not be listed on the Johannesburg Stock Exchange (JSE) nor may the shares in the HQC be directly or indirectly held by a shareholder with shares or debt listed on the JSE;
- no more than 20% of the HQC shares may be directly or indirectly held by residents; and
- at the end of each financial year, at least 80% of the assets, excluding cash, cash equivalents and debt with a term of less than one year, of the HQC must consist of foreign assets.

The above requirements must be adhered to for the duration of the year of assessment as well as all previous years of assessment if the registration with the FSD is to remain valid.¹¹⁴

With regard to reporting requirements to the FSD the HQC must report the extent of the offshore investments for statistical purposes, including, *inter*

¹¹² See section B2(B)(vi)(e) of the Exchange Control Rulings issued to Authorised Dealers

¹¹³ See section B2(B)(vi)(a) of the Exchange Control Rulings issued to Authorised Dealers

¹¹⁴ See section B2(B)(vi)(b) of the Exchange Control Rulings issued to Authorised Dealers

alia, the source of the funds, new or existing funds, destination of funds and loan funds from local sources.¹¹⁵

4.5.8 Double Taxation Agreements

As a HQC is a tax resident it has access to the DTA agreements entered into between South Africa and member states. Currently South Africa has 21¹¹⁶ treaties which are in force with African countries and another 3¹¹⁷ are in the process of negotiation. In addition to the treaties with African countries South Africa has an additional 53¹¹⁸ treaties which are in force with the rest of the world.

4.5.9 Advance tax rulings

One of the key fiscal attributes of a regime conducive to the formation of international holding companies as outlined in the Katz Commission¹¹⁹ was an efficient local tax ruling system to give certainty to the tax treatment of transactions.

The Tax Administration Act No. 28 of 2011 (TAA) provides for binding private rulings, binding general rulings, binding class rulings and non-

¹¹⁵ See section B2(B)(vi)(c) of the Exchange Control Rulings issued to Authorised Dealers

¹¹⁶ South African Revenue Service: *Africa DTA* available at [http://www.sars.gov.za/Legal/International-Treaties-Agreements/DTA-Protocols/Pages/DTAs-and-Protocols-\(Africa\).aspx](http://www.sars.gov.za/Legal/International-Treaties-Agreements/DTA-Protocols/Pages/DTAs-and-Protocols-(Africa).aspx) accessed 6 February 2014

The countries are: Algeria, Botswana, Democratic Republic of Congo, Egypt, Ethiopia, Ghana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Nigeria, Rwanda, Seychelles, Sierra Leone, Swaziland, Tanzania, Tunisia, Uganda, Zambia and Zimbabwe.

¹¹⁷ Cameroon, Morocco and Senegal

¹¹⁸ South African Revenue Service: *Africa DTA* available at [http://www.sars.gov.za/Legal/International-Treaties-Agreements/DTA-Protocols/Pages/DTAs-and-Protocols-\(Rest-of-the-World\).aspx](http://www.sars.gov.za/Legal/International-Treaties-Agreements/DTA-Protocols/Pages/DTAs-and-Protocols-(Rest-of-the-World).aspx) accessed 6 February 2014

¹¹⁹ Katz Commission par 7.1.4 and 7.1.5

binding opinions¹²⁰ which can be issued by the Commissioner for the South African Revenue Service. The advance ruling system can provide potential investors with a high degree of certainty regarding a proposed transaction which will reduce their business risk.

5 Conclusion

Mauritius has long established itself as a favourable IHC jurisdiction especially for investment into Africa due to its DTA network. While the introduction of a HQC regime in South Africa will likely not result in the demise of Mauritius as an IHC jurisdiction it at least provides investors with a suitable alternative.

Mauritius is an attractive jurisdiction for incorporating an IHC due to its GBC1 being subject to an effective income tax rate of 3%, which can be reduced to nil in certain circumstances as discussed above in section 3.3.2.2, on its worldwide income, it is not taxable on capital gains arising on the disposal of foreign shareholdings and can benefit from the Mauritius's double tax treaties. If Mauritius is evaluated in terms of the ideal holding company jurisdiction criteria¹²¹ Mauritius compares very favourably. However, Mauritius is seen as a low tax or no tax jurisdiction and can be associated with a tax haven¹²² due to it being an offshore financial centre. This reputation could influence potential investors who are sensitive to negative coverage of offshore financial centres.

South Africa's HQC regime provides international investors with an alternative to Mauritius when looking to incorporate a IHC. South Africa has almost double the amount of tax treaties in force compared to Mauritius.

¹²⁰ See Chapter 7 Advance Rulings of the Tax Administration Act No.28 of 2011

¹²¹ See section 2 of this minor dissertation

¹²² Deloitte promotes Mauritius as a tax haven to avoid big payouts to poor African nations available at <http://www.theguardian.com/business/2013/nov/03/deloittes-tax-savings-investments-in-poor-countries> accessed 7 February 2014

South Africa has double tax treaties with, amongst others, Nigeria, Tanzania and Ghana whereas Mauritius does not. South Africa also, like Mauritius, has double tax treaties with Brazil, China and India who are part of BRICS and which South Africa is a member. However, the HQC criteria are onerous to comply with and trading income is subject to corporate tax of 28% compared to a maximum of 3% in Mauritius. Tax relief ¹²³ available to the HQC and its shareholders results in no tax leakage on the receipt of dividends and disposal proceeds.

In summation both Mauritius and South Africa offer favourable jurisdictions to incorporate an IHC, ultimately the choice of jurisdiction must be decided on a case by case basis.

Below is a high level comparison of the two regimes which have been discussed above.

Area of Comparison	South African HQC	Mauritius GBC1
Ease of qualification	<ul style="list-style-type: none"> • HQC must be tax resident in South Africa • Each shareholder of the HQC must hold at least 10% of equity and voting rights • At the end of each year, 80% or more of the cost of the total assets of the HQC must comprise of equity in, debt against, or IP licensed to, foreign companies in which the HQC holds at least 10% • 50% of the HQC gross income must comprise income from foreign 	<ul style="list-style-type: none"> • GBC1 must be tax resident in Mauritius • The company must have at least two Mauritian directors who attend all directors meetings • The company must have a Mauritian bank account • Its accounting records must be kept in Mauritius • Financial statements for the company must be audited in Mauritius • A tax residence certificate must be applied for annually

¹²³ Meaning the participation exemption

	<p>subsidiaries if the gross income of the HQC exceeds R5 million</p> <ul style="list-style-type: none"> • An annual election to be treated as a HQC is required • Annual reporting is required 	
Taxation of trading income	Subject to the corporate tax rate of 28%	Taxable at a maximum rate of 3% which can be reduced to nil depending on foreign withholding taxes levied.
CGT on disposal of shares in foreign subsidiaries	Exempt from CGT on gains from the sale of any equity stake of 10% or more	No CGT payable
Dividends received from foreign subsidiaries	Exempt	Taxable at a maximum rate of 3% which can be reduced to nil depending on foreign withholding taxes levied
Dividends declared to shareholders	Exempt from dividends withholding tax	Mauritius does not have dividends withholding tax
Interest received	Taxable at corporate tax rate of 28%	Taxable at a maximum rate of 3% which can be reduced to nil depending on foreign withholding taxes levied
Interest paid on borrowings	<ul style="list-style-type: none"> • Exempt from interest withholding tax • Interest paid by HQC on money borrowed to on-lend to foreign subsidiaries is tax deductible against interest received from subsidiaries 	Mauritius does not levy interest withholding tax
Transfer pricing	Transfer pricing provisions will not apply to funding transactions of foreign subsidiaries. In all other cases it will apply	Mauritius does not have transfer pricing rules
Exchange control	Exchange control will not apply to investing abroad or borrowing from abroad.	Mauritius does not have exchange control

CFC rules	Subsidiaries of the HQC will not be CFCs in relation to the HQC. However, the CFC rules could apply to shareholders of the HQC if SA residents collectively hold more than 50% of the shares in the HQC.	Mauritius does not have CFC rules. However, CFC rules could apply to shareholders of a GBC1 if South African residents collectively hold more than 50% of the shares in the GBC1
DTA	Currently has 21 treaties which are in force with African countries	Currently has 14 treaties which are in force with African countries
IPPAs	Currently has 16 signed with African countries but only 2 are in force	Currently has 20 signed with African countries but only 5 are in force

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