

Facts

C is based in the Bahamas and forms part of the D group of companies.

D is engaged in the oil and gas industry, with exploration and production operations across the world, including the following countries in Africa: Congo Republic, Democratic Republic of Congo, Gabon and Cameroun.

The entities operating in Africa are currently held by intermediate holding companies in the Bahamas.

D is now considering either to re-domicile the intermediate holding companies in Mauritius or to set-up new entities in Mauritius to take-over the investment holding functions.

The Mauritius-incorporated companies would hold the majority shareholdings of the operating entities ("**Op Co**"). Each of the Mauritius entities ("**Hold Co**") would be expected to hold a Global Business Licence ("**GBL**") to be issued by the Financial Services Commission.

Hold Co, as tax residents of Mauritius, will be subject to income tax in Mauritius at the rate of 15% on dividend received from the respective **Op Co**. However, they will be eligible to claim:

- (i) either a 80% partial exemption on the foreign dividends to be received from **Op Co** under the provisions of the Income Tax Act, provided relevant substance requirements are satisfied; or
- (ii) ~~(i)~~ credit for foreign taxes suffered on the foreign dividends in **Op Co** jurisdictions in the form of withholding tax, underlying tax and / or tax sparing relief, under the provisions of the Income Tax Act and the Income Tax (Foreign Tax Credit) Regulations 1996, whichever is more beneficial.

Op Co in each of the African countries exploit oil and gas concessions and are subject to tax either on the basis of local tax legislations or based on specific one-to-one agreements entered with the respective African Governments.

A Production Sharing Contract ("**PSC**") is entered into by **Op Co** with the relevant African government. Such a contract/agreement between the relevant government and Z finds its legal basis under appropriate revenue legislations in the relevant African countries which may

provide for a Mining Royalty and corporate income tax to be paid *in-kind* through the delivery of specific quantity of oil barrels to the respective government tax authorities.

Under such a PSC, the relevant government gives **Op Co** the right to explore a specific area (i.e a concession) in search of oil or gas deposit. Once oil or gas is discovered, subject to completion of formalities with the relevant governments, exploitation of the concession is initiated.

Cost stop

During the exploration stage, all the exploration costs are borne by **Op Co**. However, when production is initiated, a part of the oil/gas production is allocated to reimburse both the exploration and exploitation costs to **Op Co**. This is termed in technical jargon as "Cost Oil" or "Cost Gas" and is capped at a fixed percentage of the hydrocarbon production level, a level called the "Cost Stop" and defined in the contracts.

Profit Oil

The surplus of hydrocarbon production, after deduction of the Mining Royalty payment to the relevant government and the Cost Oil or Cost Gas to **Op Co** is called the Profit Oil and is shared between **Op Co** and the relevant government at agreed proportions. The share of the relevant government is named "State Profit Oil". Where the Cost Oil or Cost Gas is higher than the Cost Stop, the unrecovered costs of **Op Co** are usually carried forward to subsequent years.

The valuation of such profit is ascertained through a mechanism agreed with the relevant African government. In this connection, the relevant government determines an Official Price of the hydrocarbon which in practice is an average of the hydrocarbons sales of the relevant period. This Official Price is also referred to as the Agreed Selling Price.

Excess Oil

Where the Cost Oil is lower than the Cost Stop, the difference, i.e. the Excess Oil, is shared between **Op Co** and the relevant government at agreed ratios that may differ from that of the Profit Oil.

Super Profit Oil

The contracts may also provide for a threshold of the Official Price, known as "High Price". Where the 'Agreed Selling Price' is higher than the 'High Price', the profit generated by the

excess is referred to as the Super Profit Oil and is shared between the relevant government and **Op Co** using a different sharing ratio from that used for the allocation of the Profit Oil. The share of the relevant government is referred to as the “State Super Profit Oil”.

Payment in-kind

Op Co is required to pay to the relevant government: a Mining Royalty and the corporate income tax. The corporate income tax may be included in and covered by the State Profit Oil. The Mining Royalty and State Profit Oil may be paid *in-kind* in terms of oil barrels.

Royalty fees are payable, in kind, at values representing agreed percentages of gross revenue (e.g. 15% of gross revenue). As regards corporate income tax, called “Tax Oil” when included and covered in the State Profit Oil / Super Profit Oil, it is paid by **Op Co** *in-kind* (in terms of oil barrels or gas volumes) at the applicable rate of corporate income tax.

The Mining Royalty and the State Profit Oil/State Super Profit Oil (including the corporate income tax when included and covered in the Profit Oil/Super Profit Oil) are paid on a monthly basis. **Op Co** submits monthly provisional tax returns to the relevant tax authority to account for the tax payments.

Therefore, the Tax Oil is not paid separately by **Op Co** but is included in the government’s share of the Profit Oil and Super Profit Oil.

In **Op Co** books, the share of **Op Co** Profit Oil and/or Super Profit Oil is considered to be net of taxes and is normally grossed up in the financial statements prepared and audited under the applicable accounting standards.

The annual tax returns of **Op Co** are also submitted to the relevant tax authorities based on the above-mentioned principles. The annual tax returns are appropriately stamped, dated and signed by the relevant tax authority.

Points at issue

- (i) Whether, in respect of foreign dividends to be received by X from **Op Co**, **Hold Co** will be eligible to claim credit for underlying tax suffered, under the Income Tax Act and the Income Tax (Foreign Tax Credit) Regulations 1996, against their respective Mauritius tax liabilities, on the basis of the corporate income tax (i.e. Tax Oil) suffered by **Op Co** *in-kind* in the relevant African countries; and

- (ii) in the affirmative, whether it would be sufficient to substantiate the claim for the above-mentioned underlying tax credit on the basis of the following documentary evidence:
 - (a) Certificate of confirmation of shareholding from the secretary of **Op Co** confirming the percentage of shareholding held by **Hold Co** in **Op Co**;
 - (b) Copies of audited financial statements of **Op Co**; and
 - (c) Copies of **Op Co** annual tax returns filed in the relevant African countries, duly stamped and signed by the relevant tax authorities?

Ruling

On the basis of the facts provided -

- (i) the corporate income tax paid *in-kind*, in terms of barrels of petrol, falls within the meaning of 'foreign tax' as defined in the Income Tax Act. Therefore **Hold Co** will be entitled to claim credit for the underlying tax suffered in accordance with the provisions of the Income Tax (Foreign Tax Credit) Regulations 1996 provided they have not claimed partial exemption on the foreign dividends received; and
- (ii) in support of its claim under (i) above, **Hold Co** will be required to produce, for the purposes of the provisions of regulations 7 and 8 of the Income Tax (Foreign Tax Credit) Regulations 1996, documentary evidence as follows:
 - (a) Certificate of confirmation of shareholding from the Secretary of **Op Co** confirming the percentage of shareholding held by **Hold Co** in **Op Co**;
 - (b) Copies of **Op Co** annual tax returns filed in the relevant African countries –
 - (i) duly stamped and signed by the relevant tax authorities; and
 - (ii) showing separately the amounts of the State Profit Oil/State Super Profit Oil and the Corporate Income Tax.
 - (c) Copies of audited financial statements of **Op Co**; and
 - (d) Certificate from the relevant foreign tax authorities in respect of the monetary value of the Corporate Income Tax paid *in-kind*.