INDIA PROVIDES CLARIFICATION ON PRINCIPAL PURPOSE TEST – GRANDFATHERING UNDER INDIA-MAURITIUS DTAA CONTINUES TO APPLY

India's Central Board of Direct Taxes has on 21 January 2025 issued a guidance note on the application of the Principal Purpose Test ("PPT") under India's double taxation avoidance agreements. This guidance confirms Mauritius' longstanding role as a recognised, efficient, and secure investment route into India and is very welcome news for the international investment community and for the Mauritian international financial centre.

The PPT, which seeks to curb revenue leakage by preventing treaty abuse, is a key provision of the Multilateral Convention to Implement Tax Treaty Related Provisions to Prevent Base Erosion and Profit Shifting ("BEPS") which entered into force in India on 01 October 2019 ("MLI"). The PPT provides that if the obtaining of a benefit under a double taxation avoidance agreement ("DTAA") was one of the principal purposes of setting up the arrangement that sought to obtain that DTAA benefit, the benefit would be denied. The exception would be where the benefit sought is in accordance with the object and purpose of that DTAA.

India and Mauritius signed a protocol in 2024 (the "2024 Protocol") to ensure alignment with the BEPS recommendations, which had the effect of introducing the PPT. However, the 2024 Protocol created a degree of uncertainty around the application of the PPT which led to the 2024 Protocol being put on hold pending further clarification. The guidance helps to provide welcome clarity.

Determining whether the PPT applies will depend upon an objective assessment of the relevant facts and circumstances and the new guidance makes clear that the PPT provision should be applied prospectively.

The guidance also importantly clarifies that it is not intended that the PPT should interact with India's treaty-specific bilateral commitments in the form of grandfathering provisions under its DTAA with certain countries including Mauritius. In the Mauritian context, this means that the grandfathering provisions in the India-Mauritius DTAA remain outside the purview of the PPT provision and are instead governed by the specific provisions of the India-Mauritius DTAA. This means that preexisting investments in shares acquired before 01 April 2017 will, in the case of the India-Mauritius DTAA, retain the DTAA benefits.

This Indian confirmation mean that Mauritian structures that invest into India will enjoy the benefits of the India-Mauritius DTAA, without facing the jeopardy of not satisfying the PPT, provided they comply with the Mauritian tax residence certificate rules and on the basis that the structures comply with the aim of the DTAA to promote the making of investments. This is a welcome clarification and serves to reinforce Mauritius' role as a leading investment partner for India.

Contact International Proximity:

For further information on the issues which are covered in this note, please contact:

Suzanne Gujadhur Bell
sgujadhur@internationalproximity.com Tel: +230 401 2302
Ashish Jagarnath Tel: +230 401 2310
ajagarnath@internationalproximity.com
Business Development
businessdevelopment@internationalproximity.com

This paper, and the facts and opinions expressed in it, has been prepared in good faith from published information. No warranty or representation is made to its accuracy or completeness, and no liability is accepted in respect of its contents or the consequences of reliance upon any statements, opinions or conclusions contained in it. A number of complex legal and tax issues arise from it, and the recipient should take professional advice on these matters before considering any further action. This paper is confidential and may also be privileged. It should not be copied or used for any purpose, nor should its contents be disclosed to any other person without the written permission of International Proximity.

International Proximity 2025