April 21, 2022
2022-5413

Mauritius amends income tax regulations regarding 80% income exemption for investment dealers and defining specialized software and systems

The Income Tax (Amendment) Regulations 2022 (ITR 2022) amended the Income Tax Regulations 1996 on 6 April 2022, as published in Government Notice No. 77 of 2022.
The amendments address: (i) the conditions for an 80% income exemption for licensed corporate investment dealers; and (ii) the nature of the specialized software and systems for the purposes of the double deduction introduced in 2021.

Conditions for 80% exempt income

Under the 2021/2022 Budget, 80% of the income of a licensed corporate investment dealer is exempt from income tax. The exemption only applies if the company satisfies the prescribed conditions. The overarching condition is that the company must have its core income generating activities (CIGA) in Mauritius. In the context of an investment dealer, this is consistent with the activities which lead to a company being classified as an investment dealer under section 29 of the *Securities Act*.

Investment dealer

Section 38(ao)(ii)(B)(IV) of the *Finance (Miscellaneous Provisions) Act 2021* (FMPA 2021) amended item 41(a) of Sub-part C of Part II of the Second Schedule to the Act so that 80% of the income of an investment dealer licensed by the Financial Services Commission (FSC) is exempt from income tax if it satisfied the prescribed conditions as from the year of assessment 2022/2023.
For an investment dealer, the CIGA are as follows:
Acting as an intermediary in the execution of securities transactions on behalf of other persons; trading in securities as principal for own account with the intention of reselling these securities to the public; underwriting or distributing securities on behalf of an issuer or a holder of securities.

Implications

- It is important to note that the CIGA for an investment dealer are comparable to the businesses referred to in section 29(1) of the *Securities Act*.
- Mauritius does not have a capital gains tax regime; furthermore, any trading profits on the sale of securities are exempt from tax. Hence, any related profit realized by the investment dealer in its capacity as a principal is totally exempt from tax.
- In the event the investment dealer acts as an intermediary, the profit realized on the sale of the shares should still be exempt from tax. It is anticipated that the business arrangements between the parties reflect the fact that the investment adviser is an intermediary so that it is legally obliged to pass on any profits realized on the disposal of securities transactions on behalf of other persons. Otherwise, there is the risk that an exempt profit becomes a taxable profit when an investor engages the services of an investment dealer.
- Section 38(ao)(ii)(B)(V) of the FMPA 2021 amended item 42(a) of Sub-part C of Part II of the Second Schedule to the Act so that 80% of the income from the leasing of locomotives and trains, including rail leasing, is also exempt as from the year of assessment 2022/2023. Item 42 of Sub-part C of Part II already applied to a company engaged in aircraft and ship leasing so that there was no need to update the CIGA requirements on the basis that the CIGA on leasing activities are generally the same, irrespective of the nature of the leased assets.

Other changes

The regulations were also amended to correct certain incorrect cross-referencing to the *Income Tax Act* (the Act).
The Income Tax (Amendment of Schedule)(No. 2) Regulations 2020 effectively reclassifies the sequential orders of a number of exempt income, as depicted in the below table.

	Item reference in Sub-part C of Part II of the Second Schedule to the Act	
	Before	After
Relevant income	Income Tax (Amendment) (No. 2) Regulations 2020	
Reinsurance and reinsurance brokering activities	44	46
Leasing and provision of international fiber capacity	45	47
Sale and financing arrangement, asset management and its spare parts and aviation services related thereto	46	48
Income from the operation of the E-Commerce platform	47	49

Regulation 3(a) and (b)(iii) to (vi) of ITR 22 has updated the principal regulations to reflect the correct item in Sub-part C of Part II of the Second Schedule to the Act and it is for this reason that the effective date of this change is the year of assessment 2020/2021, the year ended 31 December for a company with a basis year that is consistent with the calendar year.

Specialized software and systems: qualifying expenses for extra deduction

Section 38(o) of the FMPA 2021 introduced section 65B in the Act to enable a company to benefit from a double deduction on any expenditure on the acquisition of "specialized software and systems." The new section 65B(3) of the Act specifically provides that the term "specialized software and systems" would be prescribed. The extra deduction applies as from 1 July 2021.

The regulation on the definition of "specialized software and systems" was awaited for by the business community considering that the law specifically provides that the definition would be prescribed. The specific exclusion of certain expenses in that definition should also assist companies in understanding the types of expenses that do not qualify for the double deduction. Considering the inherent dynamism of the Information Communication and Technology sector, the need to have adequate documentation is of significant importance. Such documentation should provide the maximum particulars on the nature of the software and systems. Further regulations may be issued on the characteristics of any specialized software and systems.

New regulation 23P

The new regulation broadly provides the following: (i) the amount eligible for the extra deduction; (ii) timing of expenditure; (iii) use of the software; (iv) the components of the software; (v) cases where software is considered as specialized software (positive list); and (vi) cases where a software is not considered as a software (negative list).

The new regulations provide that the specialized software shall: (i) be acquired on or after 1 July 2021; (b) be used in business for income producing activities; and (ii) have a lifetime exceeding one year.

The term software comprises the following:

- Non-customized software available to the general public under a non-exclusive license
- Software acquired from a third-party contractor who is at economic risk should the software not perform
- Software that is leased
- Such other type of software as may be approved by the Minister

The eligible deduction shall be in respect of the cost of:

- Purchase or lease of the software
- Installation of the software on the taxpayer's computer hardware
- Configuration of the software to the taxpayer's needs

The expenses qualifying for the extra deduction must exceed Rs100,000, with a maximum of Rs100 million in any year.

The positive list

Specialized software shall include software used in relation to:

- Additive manufacturing
- Optimization of manufacturing processes, including production planning and execution
- Robotics
- Artificial intelligence
- Simulation
- Augmented and virtual reality
- Horizontal and vertical system integration
- Industrial Internet of things
- Cybersecurity
- Big data and analytics, including efficient data sharing
- Cloud technology
- Digitization outreach to customers
- Enable Work from Home
- Improve energy efficiency
- Engineering tools
- Product life cycle management

The negative list

Qualifying expenditure for the double deduction does not include expenditure on:

- Hardware
- Operating system software
- Software performing general and administrative functions such as payroll, bookkeeping, personnel management, spreadsheet, word processing, presentation tools or in providing non-computer services such as accounting, banking services and auditing
- Programming software
- Database software

- Basic Enterprise Resource Planning and Customer Relationship Management software
- Websites
- Mobile applications
- Gaming software, including computer games
- Point of sale system

Implications

- The new regulation provides that the software should be meant for income producing activities. Under the general rule on the deductibility of expenses, the expenditure must be exclusively incurred in the production of the gross taxable income of the company. In the context of annual allowances, the asset must also be used for the purposes of the gross taxable income of the company. Where the software is used for the purposes of the exempt income of the company, the extra-deduction would not apply.
- With the specific nature of computer software, it may happen that the software is no longer in use before the expiration of one year after its acquisition. Such instances should not impact the extra deduction insofar as the company can demonstrate the reasons for such circumstances.
- The fact that the extra deduction applies to the lease of software implies that the software does not have to be owned by the company. Clarification is required on software that is used by a company in the context of an operating lease arrangement. Section 65B(1) of the Act does provide that the software has to be acquired by the company so that any software acquired by a company under a finance lease arrangement should automatically qualify for the extra deduction.
- A company may have overpaid tax under the Advance Payment System, where the extra deduction exceeds the taxable profit for any of the quarters ended 30 September and 31 December 2021 and the quarter ended 31 March 2022.

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