

Standard Chartered – Publicised tax avoidance strategy

January 2015

Summary

Standard Chartered is a UK FTSE-100 listed bank with an extensive presence across Africa, Asia and the Middle East. The bank offers a wide-range of banking services in 15 African countries¹. It has operated on the continent for 150 years and is a well-recognised brand both in African business circles and among consumers.

The bank plays an important role in providing financial services for growing economies on the continent. In its report “Impact on Africa” it states it supports 1.9 million jobs in Sub-Saharan Africa and in 2013 supported trade worth USD7.2 billion².

Evidence seen by ActionAid International shows the bank published an article by a Mauritius-based financial firm describing a tax avoidance strategy in its publication **Standard Chartered Insights 2013/2014: Maximising Business Opportunities in Asia, Africa and the Middle East – a Treasury Guide**. The strategy can be used to legally avoid tax in some of the poorest countries in the world and was contained within an article authored by Cim Tax Services managing director Gary Gowrea.

The article highlights the tax benefits of structuring investments through Mauritius in order to legally avoid capital gains tax and withholding tax. This strategy could be used by companies to legally avoid potentially hundreds of millions of dollars of tax on a single deal. In the example of

Mozambique it would theoretically reduce Capital Gains Tax from 32 percent to 0 percent. Among other countries potentially affected are **Nigeria, Kenya, Uganda,** and **Zimbabwe** depending on the specifics of their taxation treaties with Mauritius.

Although it does not endorse the strategy, by publishing it Standard Chartered contributed to a conversation among companies about how to avoid tax in some very poor countries. According to ActionAid International research, almost half of all investment into developing countries goes through tax havens³. Meanwhile the OECD estimates that developing countries lose three times more to tax havens than the amount they receive in aid each year⁴. This is money that could otherwise be used to pay for schools, hospitals and transport infrastructure and to reduce aid-dependency.

The need for African nations to improve revenue collection is widely recognised. For example, a major report by the High Level Panel on Illicit Financial Flows for the African Union chaired by former President of South Africa Thabo Mbeki will examine how African nations can prevent the loss of billions of dollars of tax revenue – which could otherwise be invested in vital services. To be clear, ActionAid International is not suggesting that the use of the investment structure described in the Cim article is unlawful or would constitute an “illicit financial flow”.

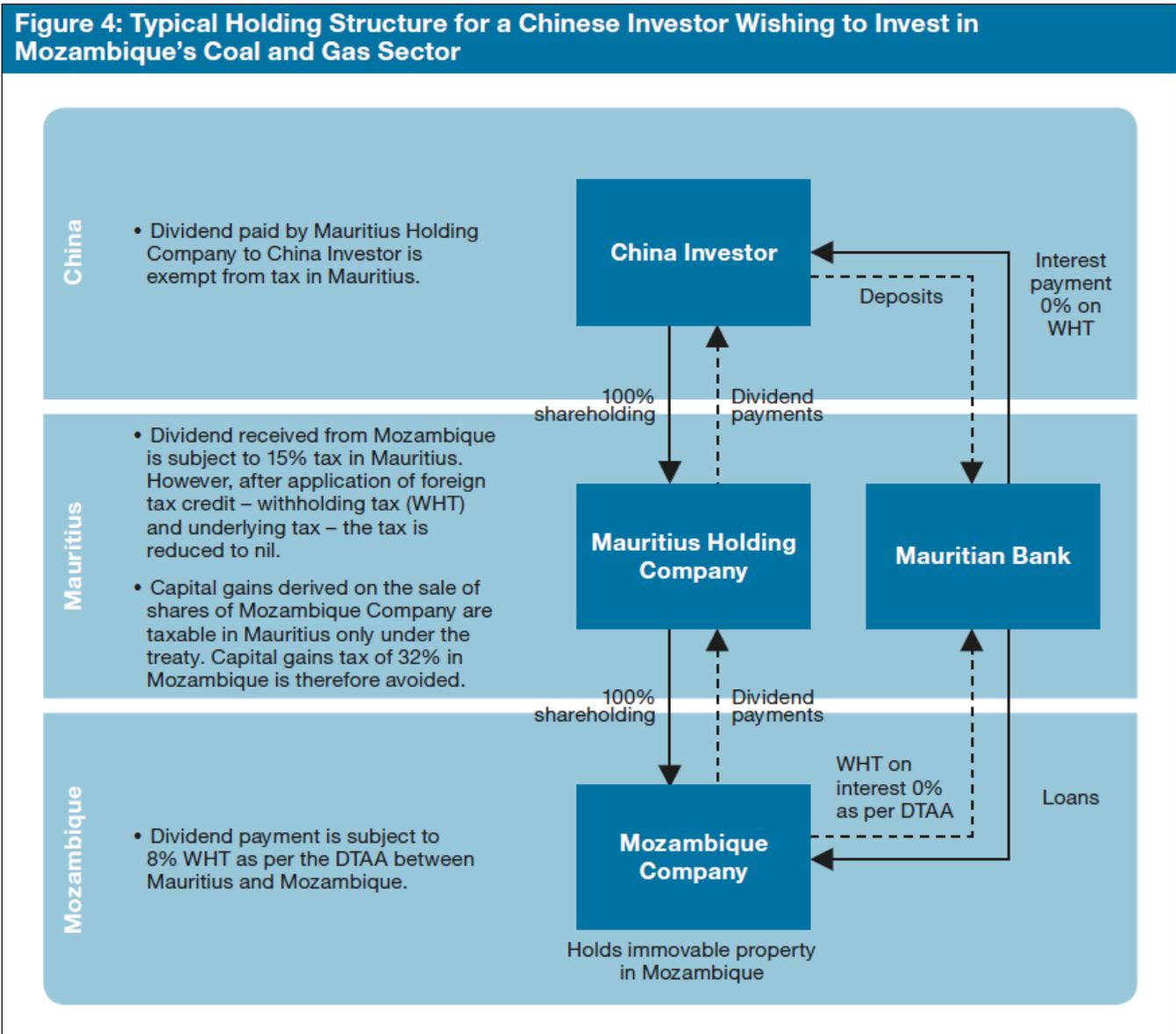
Standard Chartered states that the Cim article does not constitute the Bank’s own advice or opinion, and that it does not itself promote tax avoidance products to its customers.

The evidence

The ActionAid International allegation relates to a tax avoidance strategy published in the journal **“Standard Chartered Investment Insight 2013/14”**. This publication consists of articles written by external contributors offering investor information

and opinion. The tax avoidance strategy appeared in an article entitled **“Mauritius: An Investment Gateway to Africa”** and was written by Mauritius-based financial company Cim Tax Services.

Figure 4: Typical Holding Structure for a Chinese Investor Wishing to Invest in Mozambique’s Coal and Gas Sector



The article explains that tax can be avoided by structuring investments through Mauritius-based holding companies in order to take advantage of the island's network of tax treaties (referred to in the strategy as Double Taxation Avoidance Agreements (DTAAs).)

There is no suggestion that the structure included by CIM in the article is particularly innovative or unusual, or that its use by any given taxpayer is unlawful. In fact ActionAid International has found a previous instance where a very similar structure was advised by a major accountancy firm⁵.

The authors of the article advise investors that “adequate substance and commercial rationale be included in the structure to avoid any potential challenge by tax authorities”.

However ActionAid International believes that the structure could be used where there is little or no commercial rationale for doing so other than to avoid tax.

The article states that:

“an essential ingredient [of Mauritian investment] beyond the commercial rationale is the tax arbitrage a company can benefit from”. Expanding on the taxation advantages of Mauritius, the article goes on to say:

“Based on the beneficial withholding tax rate that the treaties provide as well as the flexible Income Tax Act provisions, various structuring possibilities are available, such as an investment holding platform or regional treasury, or a structure holding intellectual property rights.”

The strategy is designed to be used in different ways in a range of countries which have tax treaties with Mauritius. Mauritius has recently embarked on a significant expansion of its network of tax treaties with African nations and currently has more than 40 either agreed, signed or awaiting ratification with countries including **Mozambique, Kenya, Zambia, Uganda, Zimbabwe, and Nigeria**⁶. The amount of money that can be avoided using a similar strategy will vary depending on the specifics of individual tax treaties.

The key advantages of the tax avoidance structure described in the article, which uses the example of Mozambique, are:

1. Capital Gains Tax

Using the structure, a company could reduce its capital gains tax from 32 percent to no tax at all.

This single tax avoidance strategy could potentially be worth hundreds of millions of dollars to a company. As an example of the amount of money potentially involved – in 2014 the oil and gas company Anadarko was reported to have paid Mozambique US\$520 million in capital gains tax at the standard rate of 32% following a transaction which yielded a capital gain of US\$1,625,000,000⁷.

The report describes the capital gains tax advantages for companies operating in Africa as follows:

“An increasing number of African states are starting to impose capital gains tax. However the DTAAs [tax treaties] in force in Mauritius restrict taxing rights of capital gains to the country of the seller of the assets. Since there is no capital gains tax in Mauritius, the potential tax savings for a Mauritius registered company are significant.”

2. Withholding Tax

Using the structure advised in the strategy could potentially lead to a 60 percent saving in withholding tax. In Mozambique, the rate of withholding tax on dividends and interest is 20 percent. But by using a holding company incorporated in Mauritius this rate can be reduced to 8 percent.

The report describes the overall benefits of this form of tax avoidance to companies operating in Africa as follows.

“The majority of African states impose some withholding tax on dividends paid out to non-residents. These vary between 10 percent and 20 percent. The DTAAs [tax treaties] in force in Mauritius limit withholding taxes on dividend[s]”.

What the companies told us:

We wrote to both Standard Chartered and Cim Tax Services asking them to respond to our allegation. Below is the text of the statements they sent us.

Standard Chartered Statement:

“Standard Chartered does not consider this article to be the advice of the bank. There is a clear disclaimer on the back of the report that says “The opinions expressed in this publication are not necessarily those of either the publisher, Standard Chartered Bank nor the institutions for which the contributing authors work or by which they have been commissioned”.

“Standard Chartered is one of the largest corporate tax payers in Africa. In 2013, across our 15 Sub-Saharan businesses we paid US\$182m in Corporation tax. An independent report, ‘Banking on Africa’, found that Standard Chartered’s support for our clients underpins \$1.8 billion of annual tax payments in Sub Saharan Africa, equivalent to 1.1% of the entire tax receipts received by governments in the region.”

“Our tax position is very clear. We do not enter into transactions whose sole purpose is to minimise or reduce tax cost. Similarly, we do not promote tax avoidance products to our customers. We set out country-by-country tax information in respect of the year ended 31 December 2013 on our [website](#).”

Cim Tax Services Ltd Statement:

“The article in question makes mention of a wide range of benefits for companies and investors seeking to use Mauritius as an investment and trading hub for Africa; the tax treatment of certain financial receipts could be just one of these benefits. Mauritius and other developing African countries have entered into mutually beneficial bi-lateral agreements designed to promote and increase the flow of Foreign Direct Investment to support the sustainable development of these countries.”

Conclusion

Standard Chartered clearly provide developing economies with high-quality financial services that in turn generate jobs and reduce poverty.

But by publishing this strategy – Standard Chartered contributed to a culture whereby companies are exploring ways to pay minimal tax on their profits in very poor countries. Tax avoidance costs developing countries billions of dollars a year in lost revenues..

Taxation treaties remain a key tool currently in use by large companies wishing to avoid paying tax on their operations in Africa. Mauritius is in the process of rapidly expanding its network of taxation treaties – and there remain risks that these treaties will continue to expose developing countries to further loss of tax revenues.

By Richard Grange

With assistance from Nadia Harrison

1. <https://www.sc.com/en/sustainability/performance-and-policies/impact-reports/africa-day.html>

2. <https://www.sc.com/en/sustainability/performance-and-policies/impact-reports/sub-saharan-africa-report.html>

3. http://www.actionaid.org.uk/sites/default/files/publications/how_tax_havens_plunder_the_poor_2.pdf

4. <http://www.theguardian.com/commentisfree/2008/nov/27/comment-aid-development-tax-havens>

5. http://www.actionaid.org.uk/sites/default/files/publications/deloitte_in_africa_1.pdf

6. <http://www.lowtax.net/information/mauritius/mauritius-tax-treaty-introduction.html>

7. <http://allafrica.com/stories/201404150130.html>

Mauritius:

An Investment Gateway to Africa

Based on the beneficial withholding tax rate that the treaties provide as well as the flexible Income Tax Act provisions, various structuring possibilities are available, such as an investment holding platform or regional treasury, or a structure holding intellectual property or rights.

Investment Promotion and Protection Agreements

As an African nation, Mauritius has signed Investment Promotion and Protection Agreements (IPPAs) with 15 African member states. The IPPA typically offers the following guarantees to investors from contracting states:

- Free repatriation of investment capital and returns;
- Guarantee against expropriation;
- Most favoured nation rule with respect to the treatment of investment, compensation for losses in case of war, armed conflict, riots, etc.; and
- Arrangement for settlement of disputes between investors and the contracting states.

Based on the beneficial withholding tax rate that the treaties provide as well as the flexible Income Tax Act provisions, various structuring possibilities are available, such as an investment holding platform or regional treasury, or a structure holding intellectual property or rights.

The Finance Act 2012 has amended the Financial Services Act 2007 to add two activities to the Mauritius offering – global headquarters administration and global treasury activities. Schedule 2 part II and part III sets out that that at least three services must be performed for three related entities, be it in the treasury or administrative field. Even if the activities are provided to global business

companies, these are deemed to be a foreign source and get the benefit of the foreign tax credit mechanism.

Figure 4 depicts a typical holding structure that can be set up in Mauritius. We have taken an example of a Chinese Investor wishing to invest in the emerging coal and gas sector in Mozambique. The financing of the Mozambique Company can be done either through debt or equity.

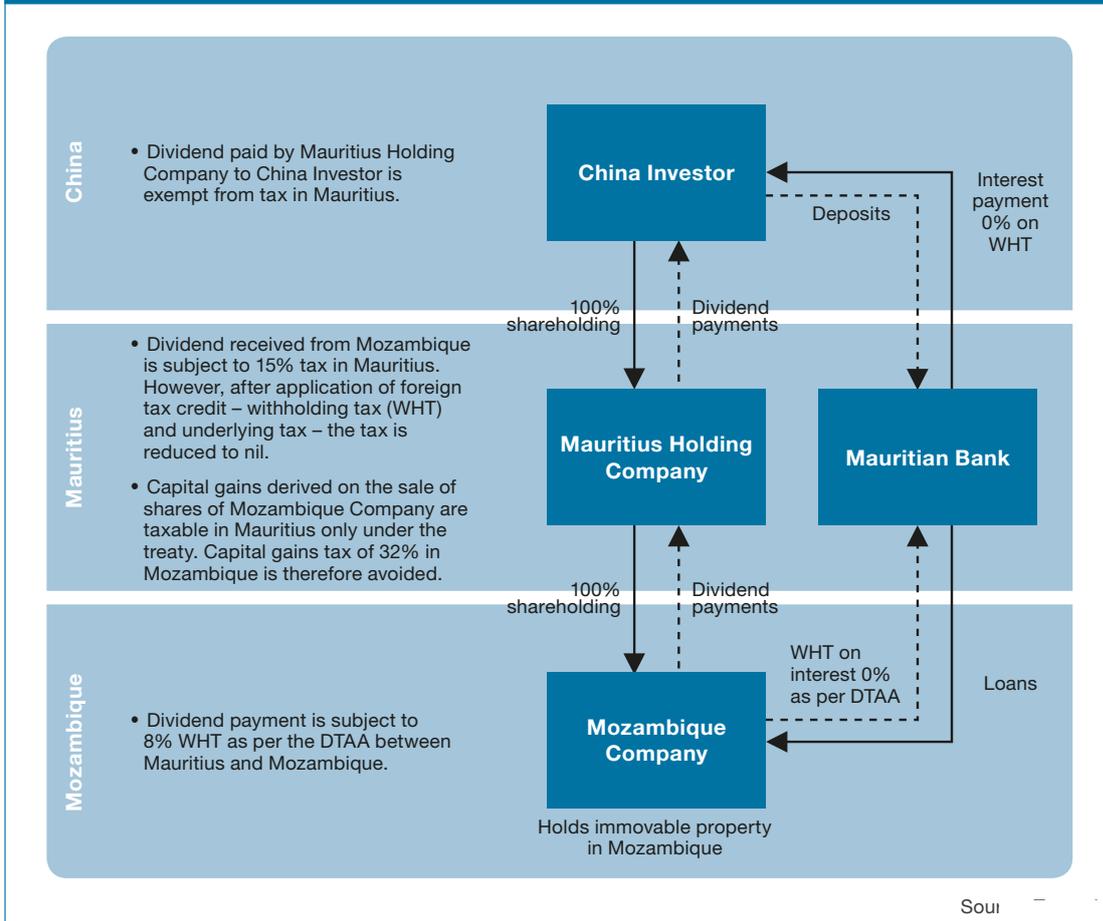
i) **The Chinese Investor can invest in equity in the Mauritius Holding Company, which in turn invests in the Mozambique Company.**

The advantages of this structure are:

- As per the tax treaty between Mauritius and Mozambique, dividend paid to the Mauritius Holding Company will be subject to a reduced withholding tax rate of 8% in Mozambique.
- With the application of the foreign tax credit mechanism, the effective tax for the Mauritius Holding Company will be reduced to nil.
- Mauritius has the exclusive right to tax any gains derived by the Mauritius Holding Company on the sale of shares held in the Mozambique Company.
- As opposed to other tax treaties signed by Mozambique, Mauritius has exclusive rights to tax capital gains on the sale of shares held in the Mozambique Company even if the assets of the Mozambique Company

Mauritius:
An Investment Gateway to Africa

Figure 4: Typical Holding Structure for a Chinese Investor Wishing to Invest in Mozambique's Coal and Gas Sector



- consist principally of immovable property.
- As there is no capital gains tax in Mauritius, gains are not taxed at all.
- Dividends paid by the Mauritius Company to the Chinese Investor will be exempt from tax in Mauritius.
- An advance pricing agreement can be obtained from the Mauritius Revenue Authority under Article 25 of the treaty

between Mauritius and Mozambique.

ii) The Chinese Investor can also finance the Mozambique Company partly through a back-to-back loan.

- The Chinese Company deposits money in a Mauritian Bank.
- The Mauritian bank provide a loan to the Mozambique Company.

- Under the treaty, interest paid by the Mozambique Company to the Mauritian Bank is free of any withholding tax.
- Alternatively, the same result can be achieved if the Chinese Investor invests the money as equity in the Mauritian Company, which then deposits the money in the Mauritian Bank.
- Interest derived by the Mauritius Company from

Mauritius:

An Investment Gateway to Africa

the Mauritian Bank will be exempt from tax in Mauritius.

- However, Mozambique does have thin capitalisation rules which provide that loans from related foreign corporations must not exceed twice the corresponding equity in the borrowing Mozambican corporation.
- Although the loan is from the Mauritian Bank, which is a non-related party, it is advisable to keep a debt to equity ratio of 2:1.

While we have taken the example of an investor from a country that does not have a tax treaty with Mozambique, the structure can also be used by investors from treaty countries like India and South Africa, as the advantages

provided by the Mauritius-Mozambique tax treaty are not available under the South Africa-Mozambique or India-Mozambique tax treaty.

Caution must be taken in light of greater convergence toward the adoption of anti-avoidance rules by developed and emerging nations. It is strongly advised that adequate substance and commercial rationale be included in the structure to avoid any potential challenge by tax authorities. In many cases, the returns on investment will be yielded in the future. However, it is important to provide substance to the Mauritius Company well before there is any claim for treaty benefits.

Conclusion

Mauritius continues to be used as a platform for investment into Africa and Asia and to reinforce its reputation as a jurisdiction of substance through its network of IPPAs, DTAAAs and other such agreements. A testimony to this is the December 2012 visit from International Monetary Fund Managing Director Christine Lagarde, which resulted in the signing of a memorandum with the Government of Mauritius to locate the Africa Training Institute in Mauritius. As reported in the press, the Australian Agency for International Development and the Chinese authorities have also pledged support for this initiative.

About the Author

Gary Gowrea



Gary Gowrea is Managing Director at Cim Tax Services. He has more than 15 years of experience in international tax and advises on tax structures set up by multinational corporations, fund managers and high net worth individuals. He is also a member of the operational committee of Global Institutional Investors Forum and sits on various committees dealing with fiscal matters as well as double taxation avoidance agreements. He has been a speaker at several local and international conferences and is a Member of the Society of Trust and Estate Practitioners (UK) and the International Fiscal Association. Mr Gowrea is a Fellow of the Association of Chartered Certified Accountants (UK) and holds a Diploma in International Taxation. He completed his MSc in Accounting from De Monfort University in Leicester, UK.