

This Chapter covers:

- Transactions attracting VAT
- Place of Supply
- Items on which VAT is not levied
- No VAT on Transfer of Ownership of Business
- Rate of VAT
- Zero Rated Items
- Difference between Zero rate and No VAT

### **Transactions attracting VAT (Sec. 5-1)**

VAT is applicable on the following transactions:

- Supply of goods or services within the state of Nepal
- Import of goods or services inside the state of Nepal, and
- Export of goods or services from the state of Nepal

This shows VAT as territorial tax, which means VAT is collected on import, export or transaction in/from/within Nepal. If a transaction is outside the territory of Nepal, VAT is not applicable on such transaction.

For example, in case Mr. A, Nepalese Citizen, imports goods from America and sells it in India; VAT is not applicable on such transaction. Similarly, VAT is applicable in import at custom frontier (as transaction place is deemed to be at custom frontier) and not before the goods reaching custom frontier.

Moreover, in case of export; VAT is levied at the sales from Nepal. For example, in case of transaction of goods by a UK branch of a garment manufacturer of Nepal within UK, VAT is not applicable on UK sales; but on sales from Nepal, i.e. CIF-Custom Frontier Nepal price in Nepal.

**Transaction outside Nepal:** If any person (whether registered in Nepal), having permanent inhabitant in Nepal or is citizen of Nepal or otherwise similar, deals in goods or services beyond above three geographical territory described above; the person is not required to charge any VAT on its transaction. But, in case the person, conducting transaction outside, Nepal brings the goods into Nepal (example EXW purchase); custom frontier is deemed to be the place of transaction.

For the purpose of determining where the goods or services are supplied, the determination of place of supply is an important matter. In case the place of supply of transaction is in Nepal, VAT is applicable on such transaction; but not when the place of supply is outside Nepal. In case of export of goods, the place of supply is considered at Custom Frontier.

### **Place of Supply**

As explained above, place of supply is important to determine whether VAT is applicable on any transaction or not. The following are the rules for determining the place of supply of goods or services:

#### 1. Place of Supply of Goods (Rule 15)

The place of supply of goods is as follows:

- a. **Sale or Transfer of Movable Goods:** In the case of transfer/sales of movable goods, the place where such goods are sold or transferred.
- b. **Immovable Goods:** In the case of any immovable goods, the location of which can't be transferred even if their ownership is changed, the place where such goods are located.
- c. **Imported Goods:** In the case of imported goods, entry customs point in Nepal.
- d. **Self-consumption:** In case any manufacturer or vendor supplies the goods to itself, the place where the producer or vendor of such goods resides.

#### 2. Place of Supply of Services (Rule 16)

The place of supply of a service shall be the place where the benefit of that service is received.

**IMF Provisions related to place of supply**

IMF has developed a model VAT law for a hypothetical country naming it as Vatopia. The place of supply as suggested by it is as follows:

**12. Place of supply**

1. Subject to this Act, a supply of goods takes place where the goods are delivered or made available by the supplier or, if the delivery or making available involves the goods being transported, the place where the goods are when the transportation commences.
2. A supply of thermal or electrical energy, heating, gas, refrigeration, air conditioning, or water takes place where the supply is received.
3. Subject to this section, a supply of services takes place at the location of the supplier's place of business from which the services are supplied.
4. The supply of the following goods or services takes place where the recipient uses or obtains the advantage of the goods or services:
  - *transfer or assignment of a copyright, patent, license, trademark, or similar right;*
  - *the service of a consultant, engineer, lawyer, architect, or accountant, the processing of data or supplying information, or any similar service;*
  - *an advertising service;*
  - *the obligation to refrain from pursuing or exercising taxable activity, employment, or a right described in this subsection;*
  - *the supply of personnel;*
  - *the service of an agent in procuring for the agent's principal a service described in this subsection;*
  - *the leasing of movable property (other than transport property);*
  - *radio and television broadcasting services; or*
  - *Electronically-supplied services.*
5. The supply of cultural, artistic, sporting, educational, or similar activities, or services connected with movable goods, takes place where the service is physically carried out, unless the service is described in subsection (4).
6. The supply of services connected with immovable property takes place where the property is located, unless the service is described in subsection (4).
7. A supply of services of, or incidental to, transport takes place where the transport occurs, unless the service is described in subsection (4).
8. Services supplied from a place of business in Vatopia which would be treated as supplied outside Vatopia under subsections (4) – (7) are considered as supplied in Vatopia and are considered as exported from Vatopia for purposes of Schedule I.

**Items on which VAT is not levied (Sec. 5-3)**

The VAT Act, 2052 has exempted VAT on certain items and exempted collection of VAT on transactions satisfying certain conditions.

**1. Exemption from levying Value Added Tax**

VAT is exempt on goods and services listed in schedule 1 of VAT Act as per Sec. 5 (3) of the Act, which states- "Notwithstanding anything written in Sec. 5 (1), VAT shall not be applied on goods and services listed in Schedule 1 of the Act. There shall be no input tax credit and refund of in case VAT is paid on purchase of such items".

This means, VAT is exempted on goods or services listed in Schedule 1 of the Act. No VAT shall be levied on such items. These items are not VAT applicable.

However, there are some items in Group 11 of Schedule 1 on which VAT is levied on output, but the registered party is entitled to refund of specified amount collected as VAT by it. This matter is dealt in Chapter 17 of this book as "Special Provision of refund of Collected VAT".

The effect of such exemption to the persons dealing such goods or services is as follows:

- a. The person is not required to fulfill any formalities of VAT Act, if s/he is dealing only in such goods or services listed in Schedule 1.
- b. The facility of *Input Tax Credit* in purchase of goods or services that are used for exempted items is not allowed.
- c. The person shall not collect any VAT on sales of such goods or services.
- d. There is no requirement of Registration for VAT purpose, nor other requirements of submitting any returns or payment of tax for the persons dealing only in such items.

## 2. Transfer of ownership of business (Sec. 5A)

This is the case when VAT is not collected while conducting a taxable transaction. It means, the transaction is taxable but the person selling the business is exempted from levying VAT.

Under either of the following two conditions, value added tax will not be applicable on the *transfer of ownership of a business*:

- (a) When a registered person sells its business to any other registered person; or
- (b) A business is transferred to any inheritor after the death of an owner.

*Responsibility of Transferee to maintain safe custody of records as per Law and to bear liabilities of Tax on assessments of Transactions conducted before such Transfer*

In case a registered person transfers the whole of its business to any other registered person, the transferor is not required to charge tax on the transfer, if Form of Schedule 4 has agreed and submitted with the Tax Officer. In this case, VAT liability due or assessment of further tax liability in due course of time as per the provisions of VAT Act by Tax Officer after assessing the transactions of the transferor, or VAT credit in the hand of transferor shall be shifted to the transferee.

Similarly, the transferee shall maintain such books, accounts and records as required under the VAT law for the transactions conducted by the transferee till the period prescribed by the VAT law.

## 3. Exemption through Special Decision of Council of Ministers:

Government of Nepal, by issuing a notification in Nepal Gazette, may exempt certain items from the application of VAT. Similarly, in case of import of goods, the Council of Ministers may waive to levy VAT at the custom frontier by publishing a notification in Nepal Gazette.

## Rate of VAT (Sec. 7)

Sec. 7 (1) of the Act specifies a single rate of VAT of 13% for all items on which VAT is applicable. But in fact, the rates of VAT are as follows:

- |   |        |
|---|--------|
| • Items specified in Schedule 1 of the Act                          | No VAT |
| • Items specified in Schedule 2 of the Act                          | 0%,    |
| • For all other items (not specified in Schedule 1 or 2 of the Act) | 13%    |

## Zero Rated Items

Schedule 2 of VAT Act contains lists of items on which VAT is levied at Zero Percent, which is termed as “Zero Rated Items” in this book. In fact, true no VAT items are Zero Rated Items. For all these items, the output VAT is 0% and the person is entitled to input VAT credit on such items, which means the VAT paid on purchases are refundable, and thus, there is no VAT component on sales of such items. The zero rates are sometimes called as *exemption with credit*. Schedule 2 provides a list of transactions those to be charged at 0%.

The list of such items is as follows:

1. **Export of goods:** In case it is proved that the supply is made as follows:
  - a. Goods exported from Nepal;
  - b. Goods stored on a flight that has a destination outside Nepal; or
  - c. Goods stored on an international flight having destination outside Nepal for retail sales, or supplies or consumption.
2. **Services provided to any person outside Nepal:**
  - a. A supply of services by a person resident in Nepal to a person residing outside Nepal. The recipient of service shall have no business establishment, agent or legal representative acting on such person’s behalf in Nepal.
  - b. A supply of *goods or service* by a registered person to a person residing outside Nepal.
3. **Import of goods or services by person entitled to diplomatic or duty privilege:** Import of goods or services on recommendation of Ministry of Foreign Affairs by following persons:
  - Accredited diplomat individual or diplomatic agency or
  - Any individual working in diplomatic agency, which is entitled to duty exemption office.
4. **Projects exempted under any Treaty or Agreement effective on the date of enactment of VAT Act:**

Any purchases of goods from a registered dealer in Nepal by any person to whom exemption of sales tax was provided as per the agreement with a project till the agreement is in force, on recommendation of the related project, the person shall avail the zero VAT facility.
5. **Supply to Industries in Special Economic Zone:**

Sales of raw materials and finished goods to any industry established at special economic zone set up as per prevailing law.

**6. Production & Supply of Battery related to production of Solar Energy:**

Sales of battery required for plants and equipments for use in production of solar energy duly approved by Alternative Energy Promotion Centre by a domestic producer *directly* to the solar power producing unit.

**7. Supply to hydroelectric project:**

Sales of plants, equipments and parts thereof, machineries, penstock pipe or iron leaf used to manufacture penstock pipe required for hydro power project **produced by a domestic producer** and **directly supplied by the producer itself to the project** upon approval of Alternative Energy Promotion Centre or Department of Electricity, as the case may be.

**8. Refund of VAT paid on Raw Materials:**

The VAT paid on raw materials used to carve statue, idol, paintings, or similar handicrafts items by small and cottage industries; the products of which are exported through approved export houses is refundable.

**9. Refund of VAT in case of purchase of scooter to be used by Incapacitated persons:**

In case of import of scooter by a disabled individual or purchase of scooter from local supplier, the VAT paid by the owner shall be refunded by Transportation management office in case of import and by IRD in case of local purchase when the scooter is registered in the name of such person on recommendation of Ministry of Female, Children and Social Welfare or concerned District Administration Office

**10. Special Provision related to refund of VAT introduced by Finance Bill 2072:**

- a. The VAT paid by hydroelectricity projects that are eligible to Zero rated VAT, which are constructed and operated by Consumer Group formed without any objective to generate profit based on Community or the projects that failed to entertain Zero rated facility (Including projects that have completed work through contract), as per the procedures prescribed by Inland Revenue Department on recommendation of Alternative Energy Promotion Center in case of projects approved from AEPC and on recommendation of Electricity Development Department in case of other Small Hydropower Projects.
- b. Notwithstanding anything written in VAT Act 2052, the VAT claimed till 2072 Poush end shall be refunded to the Small Hydropower Projects

**Difference between Zero Rate Vs No VAT**

Basis	Zero Rate	No VAT
Rate of VAT	VAT is levied at Zero Percent	VAT is not levied at all
VAT Invoice	A VAT Invoice shall be issued as per the format prescribed by VAT regulation	VAT Invoice shall not be issued at all
Registration Requirement	The person dealing in Zero rated items shall be registered for VAT purpose.	The person dealing exclusively in No VAT items is relieved from registration formality
Other formalities as per the Act	The person dealing in Zero Rated Items shall observe other formality as per VAT Act, such as- maintenance of sales and purchase register duly certified from Tax Officer, submission of VAT return, etc.	The person dealing exclusively in No VAT items is relieved from all formalities to be observed as per the Act
List of Items	List of Zero rated items are prescribed in Schedule 2 of the Act	List of No VAT items are prescribed in Schedule 1 of the Act, but Schedule 1 also contains some VAT applicable items on which the producer is entitled to refund of VAT collected by it.

**Test Your Understanding**

1. State whether "True" or "False":
  - a. No tax is to be levied for a supply of services by a person residing in Nepal to a person outside Nepal who has no business transaction in Nepal. *(1 Marks, CAP II, July 2015)*
  - b. 'No VAT' and 'Zero VAT' have the same meaning as VAT in both the cases is zero. *(2 Marks, CAP II, June 2014)*
2. Nepali Rice Mill Industries purchases the rice in the husk (Dhan) to produce the rice. The Chitawan based mill sales its packed rice to the local markets. The company has the following transactions from Bhadra 2071 to Chaita 2071.
 

Sales	Rs. 3,000,000
Dhan purchase	Rs. 2,000,000
Machinery purchase	Rs. 2,500,000 (Net of VAT)
Factory construction	Rs. 5,500,000 (Payment to the Contractor)

State the relevant provisions for VAT implications on this case with references to the VAT Act, 2052 and VAT Rules, 2053. *(5 Marks, CAP II, July 2015)*
3. A lawyer practicing in Nepal provides consultancy service to a legal firm in United Kingdom. The legal firm of the UK used that service to release a person in USA. Where is the place of supply of services as per VAT Act/Rules? *(5 Marks, CAP II, Dec 2012)*
4. Cosmos P. Ltd. having its registered office in Jawalakhel, Lalitpur transferred some goods costing Rs. 1 Million to its branch at Bangladesh. In the same month, the Bangladesh branch transferred some goods costing Rs. 500,000 to its head office in Nepal. Gross Profit Margin of head office is 20% and that of branch is 25%. The profit of branch is consolidated at the end of each FY in books of Head Office.  
Discuss the VAT impact on above transactions. *(5 Marks, CAP II, June 2012)*
5. State the place of supply in the following cases: *(5 Marks, CAP II, June 2012)*
  - Sale of Movable Goods
  - Immovable Goods
  - Imported Goods
  - Self-Consumption
  - Service
6. Tax Accountant of Subhashree & Co. contends the term "Zero VAT" and "No VAT" having the same meaning. As a Tax Expert, express your opinion within the framework of VAT Act 2052. *(5 Marks, CAP II, Dec 2011)*
7. A dealer manufactured goods worth Rs. 10 Million, which were exempt under Schedule 1 of the VAT Act. Out of total purchase, partial goods were VAT attractive and partial exempted goods. Exempted goods worth Rs. 7 Million were used for the production of goods, which were exported. The dealer claims that all the exports are Zero rated and he is entitled to claim full tax credit on export.  
Consider his claim to set off the VAT paid by him on inputs. *(4 Marks, CAP II, Dec 2010)*
8. Examine applicability of VAT. *(10 Marks, CA Final, June 2004)*
  - a. Service provided by a hospital owned by medical college.
  - b. Consultancy services rendered to a programme of United Nations.
  - c. A digital camera costing Rs. 50,000 brought by a person coming from abroad.
  - d. Production license fee to company providing spirit.
  - e. Passenger service-fee charged by airport authority.
9. Distinguish between
  - a. Zero VAT and No VAT *(5 Marks, CA Final, Dec. 2007)*
  - b. Exempted goods & Zero rated goods *(4 Marks, CA Final, June 2005)*
10. Whether the following goods or services are included in Schedule 1 of the VAT Act: *(CA Final, June 2006)*
  - i) Pesticide
  - ii) Photocopy papers purchased for newspaper
  - iii) Services of life insurance
  - iv) Jute bags
11. An industry producing export oriented plastic products has produced 2000 kgs of plastic products during the year 2061-62. The industrial norms for input output ratio is of 5% where as during the year 2061-62 the actual input output ratio of the industry is calculated as 7%. The tax officer in his assessment for the year and has treated the extra shortage of 2% as goods produced and sold in the market and charged VAT and penalty on the amount. Advise on the matter. *(CA Final, June 2006)*
12. State with reasons in short about applicability of VAT in the following cases: *(15 Marks, CA Final, June 2008)*
  - a. Medical services by a private nursing home working for profit.
  - b. Magnesium Hydroxide imported by the pharmaceutical industries.
  - c. Bottles and Cartoons imported by the pharmaceutical industries.

- d. Primary educational services by private schools recognized by the government.
  - e. Sale of writing paper.
  - f. Paintings sold by shop-keeper to a foreigner locally.
  - g. Entrance fee to zoo.
  - h. Charges for transport by cable car.
  - i. Chemical fertilizers imported from Japan.
  - j. Tractor used by brick maker to transport bricks.
  - k. Vessels for household use.
  - l. Oxygen gas supplied to hospitals.
  - m. Vegetables salad (a mixture of cut vegetables) and fruits sold by a hotel to its guest.
  - n. Tea chest for packing tea.
  - o. Essence of clove and cinnamon.
13. Somany Marble Industries Kathmandu is a manufacturer of polished marble. In fiscal year 2063/64, the company had supplied some marbles to Embassy of Japan for construction of their office in Kathmandu. The Company issued tax invoice for the cost of marble as per VAT Act and rules. The Company also collected transportation charges from the Japanese Embassy for which it did not issue tax invoice arguing that VAT is exempt on transportation charges as mentioned in Section 9 of Schedule 1 to VAT Act, 2052. The Tax Officer wants to assess VAT on the transportation charges collected by the Company. State, giving reasons, the tenability of the tax officer's view. *(5 Marks, CA Final, June 2008)*
14. State with reasons for applicability of VAT for the following: *(10 Marks, CA Final, June 2009)*
- a. Taxable goods sold to a unit establish in SEZ.
  - b. Packed & dried preserved fish.
  - c. Marine Insurance.
  - d. Raw Wool.
  - e. Raw material for manufacturing of Intra Oculars Lenses.
  - f. Medical Syringe & Needles.
  - g. News print paper.
  - h. Carton & bottles imported by Pharmaceuticals Industries.
  - i. Tea Chest for packaging of Tea.
  - j. Vaccines for medical treatment.
15. Under what circumstances VAT is exempt on Transfer of Ownership of Transactions under VAT Laws. Explain the procedures for such transfer under VAT Act, 2052. *(5 Marks, CA Final, Dec 2009)*
16. State the applicability of VAT in the following cases: *(5 Marks, CAP III, June 2011)*
- a. Fresh Water P. Ltd. is operating a business of supplying water in tanker
  - b. Reinsurance of General Insurance
  - c. Cargo Service for import
  - d. Ujyalo Hydropower Development co. Ltd. operates its business of hydropower generation and consultancy on hydropower construction in PAN for income tax purpose only. Its consultancy income for the year 20X1/X2 is Rs. 30 Lakhs. Would your answer be different if the consultancy income was Rs. 51 Lakhs?