CHAPTER 10

VAT ON IMPORTS AND EXPORTS

A. Introduction

This chapter relating to VAT and international trade transactions (i.e., import and export) is a special treatment goods, property and services (Chapters 1 and 2). Imports are supplies of goods brought into the country or services rendered therein while the exports are goods sent or services rendered outside. Hence, the destination rules discussed in the early chapters are very important in discussing import and export transactions.

Imports generate significant VAT revenues but international transactions, notably the zero-rating of exports, can also pose major compliance and administrative challenges for tax offices and taxpayers. In particular, the distinction between goods and services becomes very important in international trade. The following summarize the discussions of VAT on international trade transactions in previous chapters.

- *Destination rule:* VAT is imposed on imports while exports are excluded from the domestic VAT burden through *zero-rating*. VAT is also neutral in applying the same VAT rate to domestic and international trade or supplies.

- *VAT on goods:* Customs agencies impose import VAT on imported goods and zero-rate exports (a) on behalf of domestic tax agencies; and (b) under the same laws or regulations that apply to tariffs and other customs duties, levies or taxes.

- *VAT on services:* VAT is imposed on services where they are rendered—exported services are zero-rated while, under the *reverse charge* rule summarized in a bullet point later, imported services [including those rendered locally by foreigners] are subject to VAT.

- *VAT on (fixed) property:* Supply of property is subject to VAT where it is located. The supply of taxable domestic property is subject to VAT but not those located outside. The VAT on goods and services related to fixed property depends on the (a) location of the property; and (b) substantive or incidental nature of those supplies.

- *Input tax credit (ITC):* Registered businesses can claim the import VAT they pay as ITC, provided they relate to sales of taxable supplies. While both registered and non-registered persons pay import VAT, only the former can claim it VAT as ITC.

- *Reverse charge rule*: It is difficult to enforce the law against foreigners for services they render locally. Services are intangible and not subject to control by customs offices. Hence output VAT on imported services is self-assessed by the registered domestic recipient who can claim it in reverse (a *reverse charge*) as ITC.

Chapter 10 discusses the general rules for imposing VAT on imports and for zero-rating exports while Chapter 11 discusses special transactions. Sections B to D discuss the customs rules as they relate to the destination principle for processing or "clearing" imports and exports of goods. Section E discusses the filing of domestic VAT returns to reflect the import and export values. Sections F and G discuss VAT on imports and exports of services and on fixed property.

B. Importance of the destination principle

This section summarizes a number of issues relating to the destination rule discussed in Chapter 2 because they are important to imports and exports of goods and services.

- In general, imports of goods and services are subject to VAT while exports are excluded through application of a zero VAT rate (unless stated, exports are taxable under the origin rule or principle only).

- Exempt goods and service are exempted when exported and, unless stated otherwise, the ITC would be blocked or apportioned (see Chapter 6). In general, customs laws exempt imports of personal goods from VAT and tariffs—in all foreign trade or migration categories, provided they are in non-commercial quantity.

- Some countries zero-rate domestic supplies, *in lieu* of exemption, to alleviate the VAT burden on socio-economic grounds. As noted in Chapter 6, many countries subject the same classification of imports and domestic supplies to this concession.

VAT is neutral but some countries restrict the exemption or zero-rating to only supplies of unprocessed food produced locally. Besides this, the VAT rules are often straightforward for imports and exports of goods. *In contrast, the rules are more difficult for imported services.*

C. Imports and exports of goods

The VAT on imports and exports of goods is administered by customs offices on behalf of the domestic tax agency. The procedures for customs "clearance", "entry" or "declaration" in customs offices are the same or similar for VAT, excise duty and tariffs or customs duty.

Classification of goods in international trade

In addition to being classified as taxable or exempt supplies, goods are usually categorized further in customs tariffs to conform to the Harmonized Commodity Description and Coding System (HS Code) of the World Customs Organization (WCO).

Classification under VAT laws: As noted in Chapter 1, VAT laws classify the supply of goods as taxable (including zero-rating) or non-taxable (i.e., exempt and relief) supplies.

- *Taxable (standard rated) goods:* The imports of goods attract a single standard rate [higher or lower in some cases] and constitute most of the supplies subject to VAT.
- *Taxable (zero rated) goods:* countries typically zero-rate exports [but some apply a zero rate to certain basic imports and domestic supplies to provide relief from VAT].
- *Exempt goods:* Unlike zero-rating, no rate is applied to exempt goods because they fall outside the VAT rate regime.

In principle, VAT is neutral between foreign and domestic trade. In practice, however, there could be variations that include the restriction of exempt or zero-rated supplies in some VAT laws to unprocessed agricultural goods *produced locally* (in principle, a tariff).

HS Code classification: Customs tariffs schedules classify goods further to conform to WCO's HS Code. Table 1 below shows the high-level codes.

Table 1: HS Code classification or chapters

HS Classification	Description of Commodities
01 – 05	Animal and animal products
06 – 15	Vegetable products
16 – 24	Foodstuffs
25 – 27	Mineral products
28 – 38	Chemical and allied industries
39 – 40	Plastics and rubbers
41 – 43	Raw hides, skins, leather & furs
44 – 49	Wood and wood products
50 – 63	Textiles
64 – 67	Footwear and headgear
68 – 71	Stone and glass
72 – 83	Metals
84 – 85	Machinery and electricals
86 – 89	Transportation
90 – 97	Miscellaneous (Optical, photographic, furniture, toy, sports equipment, etc)
98 – 99	Services

The HS classifications improve transparency in accounting for VAT and compiling trade statistics. The main headings may be sub-classified further (e.g., 6-8 digits) to include the taxable, exempt or zero-rated categories in VAT and customs laws.

Types of customs declaration

Customs agencies charge and administer the VAT on imports and exports of goods under the same laws as tariffs and other customs duties, taxes and levies. *VAT laws often state that the VAT on imports and exports shall be administered as though it were a customs duty or tariff.* The principal methods of "clearing" goods in international trade include—

- *domestic consumption or use:* importers declare goods meant for domestic (including personal) use, consumption or application as taxable, exempt or zero-rated;

- *exports:* export declarations mean the goods are destined outside the country and subject to zero-rating under the relevant customs rules;

- *warehousing:* customs laws allow taxpayers to hold goods in a registered or bonded warehouse prior to their final clearance as imports or exports; and

- *transit, re-exports and re-imports:* goods may be re-exported or re-imported for reasons that include transshipment, advertisements (promotion) and repairs.

Importers using the customs "entry" or "declaration" discussed below pay VAT immediately on goods "cleared" for domestic use or exports. However, customs laws suspend the VAT on transit and bonded warehouse transactions, pending their "final" importation or export. As noted in Section A, the special VAT rules relating to these transactions and imported services are discussed in Chapter 11.

Importance of customs entry, declaration or SAD

Customs offices base the "declaration" or "entry" for VAT and other customs duties on the same valuation, inspection, classification, and post-release rules, controls and audits. Many countries now use a standard *Single Administrative Document (SAD)*—that is, entry or declaration, to satisfy a number of objectives.

- A declaration is a multi-purpose composite document used by importers and exporters to calculate VAT, tariffs and other customs taxes, duties or levies. In this regard, *VAT laws make the customs entry a de facto VAT invoice and return.*

- Taxpayers must retain the foreign invoice but a customs entry is more relevant for establishing import and export values in support ITC claims.

- The entry is more authentic because customs offices routinely adjust the classification and value of goods on foreign invoices—due to errors, tax evasion and tax avoidance.

- Foreign suppliers may not be registered domestically for VAT and, technically, they cannot issue a VAT invoice (which is a legal requirement under many VAT laws).

In summary, an entry is important because foreign suppliers cannot register and charge VAT—except in customs unions and the special cases discussed in Chapter 11. Moreover, they view supplies as zero-rated exports from a home-country or origin perspective.

D. VAT on imports and exports of goods

This section covers the basis for calculating VAT on imports and exports, eligibility to pay VAT on foreign trade transactions, and examples of actual VAT calculation.

Basis for calculating VAT

Customs offices calculate the VAT due on imports and exports of goods by taking three principal classifications of values and taxes into account.

- *Cost of imports and exports:* The value for VAT in foreign trade is the total sum of *cost, insurance and freight (CIF)*. Tax offices accept the value agreed between the importer and supplier under World Trade Organization (WTO) rules, provided they reflect arms-length prices (Chapter 5). The WTO rules and domestic customs and VAT laws allow customs offices to adjust these values in the event of errors, tax evasion or avoidance (e.g., over- and under-invoicing).

- *Foreign currency conversion:* The CIF value may be stated in foreign currency and taxpayers need to convert it at an exchange rate into domestic currency equivalent for VAT and customs duty purposes. Some countries apply the spot or daily exchange rate while others apply rates that are determined at longer intervals (e.g., weekly).

- *Tariffs, excises and other levies:* As a general rule, taxpayers add the customs duty or tariff, excise duty, other taxes and incidental expenses such as commissions, and packaging to the CIF value to calculate VAT on imports and exports (note that CIF implies that insurance and transportation costs are also added).

Table 2 illustrates the discussions on customs valuation and classification up to this point.

Table 2: Calculation of import/export (CIF) value

Classification	Details	Value ($)
Cost (importer or customs value)	Foreign currency values	10000
Insurance		1000
Freight		500
CIF value		11500
CIF value (local currency)	$1=1.2	13800
Customs duties	15 percent	2070
CIF + duty	Local currency	15870

These calculations can become complex as a result of several factors that include the following—

- some countries base the VAT on international trade on the ***free-on-board (FOB)*** value, which exclude freight (transportation) and insurance (see discussion below);

- the customs and excise duties added to CIF varies by tax policy (e.g., the VAT on *excisable products* may be based on the *duty-inclusive* or *duty-exclusive* value);

- the excise and customs duties are subject *drawback (refund)* in many countries but the procedures may not be as automatic as ITCs;

Table 3 illustrates these points and shows an increase in the value for calculating the import VAT (with the addition of import duty and import excise to the base).

Table 3: Calculation of import/export value on ***excisable*** goods

Classification	Details	Value ($)
Cost (importer or customs value)	Foreign currency values	10000
Insurance		1000
Freight		500
CIF value		11500
CIF value (local currency)	$1=1.2	13800
Customs duties	15 percent	2070
CIF + duty	Local currency	15870
Excise duty	20 percent	3174
CIF + duty and excises		19044
Value for calculating import VAT (zero for exports); as shown later, upon export, customs and excise duty may be subject to ***drawback***		

Eligibility criteria

Customs agencies require all importers and exporters of goods to comply with the customs law and regulations—*whether or not they are registered for domestic VAT, with the domestic VAT registration becoming relevant in filing a domestic VAT return.*

- All importers and exporters must make a *VAT declaration* and pay the VAT due at importation, whether or not they are registered for domestic VAT (the main exception being *imports of personal goods* in international travel and migration).

- Import VAT does not depend on whether the importer gave or received *consideration* in an international trade transaction. In other words, the importer paying VAT need not be the person who trades in the goods *in the ordinary course or furtherance* of domestic *enterprise* or commercial activity.

- All importers and exporters account for VAT but it is only those registered who can claim ITC (and offset input VAT against zero-rated exports) on their domestic VAT returns (Section E).

In short, consumers as well as registered and unregistered businesses are all subject to the customs law when it comes to applying VAT to foreign or international trade.

Examples of VAT calculation

The ensuing paragraphs discuss VAT payments, credit and refunds for imports and exports. The illustrations are based on Table 3 and, unless stated otherwise, they exclude excise duty.

VAT on taxable imports: As shown in Table 4, importers complete the customs by applying the standard, zero or other rate to the domestic currency equivalent of the CIF value plus customs duties and other taxes.

Table 4: Import VAT based on CIF value

Classification	**Details**	**Value ($)**	**Taxes**
Cost (importer or customs value)	Foreign currency values	10000	
Insurance		1000	
Freight		500	
CIF value		11500	
CIF value (local currency)	$1=1.2	13800	
Customs duty	15 percent	2070	2070
CIF + duty	Local currency	15870	
Import VAT	10 percent	1587	1587
CIF + duty + VAT	Local currency	17457	3657

As shown in Table 5, some countries apply the import duty rate to the free-on-board (FOB) value (plus taxes). Since this is equivalent to the value before insurance and freight, it is clear that the FOB basis reduces the import VAT in comparison with the CIF value basis.

Table 5: Import VAT based on FOB value

Classification	Details	Value ($)	Taxes
Cost (importer or customs value)	Foreign currency values	10000	
Customs duty	15 percent	1500	1500
FOB + duty	Local currency	11500	
Import VAT	10 percent	1150	1150
FOB + duty + VAT	Local currency	12650	2650
Rates (import duty/VAT)		15%	10%

Given that the WTO rules favor CIF by requiring the addition of transportation, incidental expenses and insurance to FOB, unless specified, the remaining examples adopt that basis.

VAT on exports: The destination rule zero-rates exports of goods to remove the burden of domestic VAT on foreign buyers and, therefore, compared to exemptions, *registered exporters* can claim ITC under the relevant VAT rules (Table 6).

Table 6: Zero-rated exports

Classification	**Details**	**Value ($)**	**Taxes**
Cost (customs/importer value)	Foreign currency	10000	
Insurance		1000	
Freight		500	
CIF value		11500	
CIF value (local currency)	$1=1.2	13800	
Export/export VAT	0 percent	0	0
CIF + VAT		13800	

As discussed in Section B, on a strict interpretation, exports that are exempt, not zero-rated, would not be part of an ITC, zero-rated and refund regime (Chapter 6). This may give rise to special application of zero-rating, together with customs and excise duty drawbacks—

- *export of exempt goods*: unless provided, this means the ITC would be blocked or apportioned and lead to export price increases (thus contravening the case for excluding all domestic taxes from exports); and

- *customs drawback schemes:* this relief is provided when imports are used to produce goods for export—in essence, the taxpayer is given a refund by applying to a customs office with the requisite documents.

The customs duty of $2070 in Table 7 below could be refunded under drawback regimes. Secondly, some VAT laws insert provisions to ensure that all exports would be zero-rated, even when goods are VAT-exempt as domestic supplies and ITC would have been blocked.

Exempt and zero-rated imports: In principle, VAT laws extend the exemption or zero-rating of supplies on social or economic grounds to imports. As shown in Chapters 6 and 7 as well as Table 7 below, as an upstream transaction, the exemption or zero-rating at importation has the effect on the import price.

Table 7: Exempt/zero-rated imports (VAT only)

Classification	Details	Value ($)	Exemption	Zero-rating
Cost (importer or customs value)	Foreign currency values	10000	10000	10000
Insurance		1000	1000	1000
Freight		500	500	500
CIF value		11500	11500	11500
CIF value (local currency)	$1=1.2	13800	13800	13800
Customs/import duty	15 percent	2070	2070	2070
CIF + duty	Local currency	15870	15870	15870
Import VAT			Exempt	0
CIF + duty + VAT	Local currency	15870	15870	15870

However, differences arise when the goods are sold locally as (a) final exempt or zero-rated supplies; or (b) inputs for making taxable or exempt supplies.

- If sold in its original state as an exempt product, the registered person may not claim Input VAT on incidental expenses as ITC. On the other hand, this is possible when the product is also zero-rated domestically.

- If the product is used to make domestic taxable supplies, the VAT waived or not paid at importation would be captured in downstream transaction (see Chapter 6).

The example above also assumes that the supply attracts customs duty but not VAT. As shown in Table 8, however, the supply may be exempt form both VAT and tariffs.

Table 8: Exempt/zero-rated imports (VAT and import duty)

Classification	Details	Value ($)	Exemption	Zero-rating
Cost (importer or customs value)	Foreign currency	10000	10000	10000
Insurance		1000	1000	1000
Freight		500	500	500
CIF value		11500	11500	11500
CIF value (local currency)	$1=1.2	13800	13800	13800
Customs duty	Nil	0	0	0
CIF + duty	Local currency	13800	13800	13800
Import VAT	Nil		Exempt	0
CIF + duty + VAT	Local currency	13800	13800	13800

Time of payment

In principle, the VAT on imports is due immediately upon clearing the goods at a customs office. In practice, import VAT is deferred under certain circumstances.

- *Immediate payment:* In principle, the import VAT is administered as a tariff and, therefore, payable immediately before the goods can be released or cleared. Any deferment of the import VAT, besides those discussed below, is deemed to be a financial arrangement. For example, some countries allow the VAT and tariff on certain significant imports (e.g., capital goods and raw materials) to be paid in installments. The payment may be made in customs offices or through bank transfers, including electronic payments (Chapter 15).

- *Deferred payment schemes*: Some countries allowing taxpayers to clear the goods and make payment on deferred or installment basis (e.g., 21 days after clearance or after the month in which the goods were cleared). These arrangements may necessitate guarantees or security deposits (Chapter 15).

- *Deferral of import VAT:* As noted in Chapter 11, the VAT on goods to be placed in a customs or bonded warehouse is deferred until the goods are removed for domestic consumption, use or application. Similarly, the VAT on transshipments and re-exports may be waived until they are declared for home consumption or use.

In general, the VAT on the bulk of imported goods is payable immediately. This contrasts with the filing of domestic VAT returns where the payment is for supplies made during the previous month. At this stage, we discuss the relationship between domestic and foreign VATs before returning to VAT on imported services in Section F.

E. VAT on foreign trade and domestic VAT returns

As noted in previous sections, all importers and exporters of goods must comply with the customs rules and pay any VAT due, regardless of domestic VAT registration. For domestic VAT purposes, the status of registration becomes critical for the treatment of the VAT paid or self-assessed on both imports and exports of goods and services.

Customs entry and domestic VAT processes

As discussed earlier in Section C, a registered person must retain the customs entry approved by customs offices for releasing or clearing goods. To reiterate a few points made earlier—

- the entry shows the value, classification, rate and amount of VAT for taxable (including zero-rating), exempt (and relief) or mixed supplies of goods;
- entries provide evidence of import VAT since foreign suppliers may not be obliged under the domestic VAT laws to register—hence, it is the SAD, not the foreign invoice, which shows the import VAT and zero-rated exports;
- in essence, an entry is a *de facto* invoice for claiming ITC and proving that supplies have been exported for zero-rating purposes (as noted, some VAT laws classify the SAD or entry as an invoice for VAT purposes).

The *domestic VAT returns*, with international trade components, are discussed briefly below (Tables 11 and 12) and in Chapter 16. Table 9 shows Component II (lines 100 to 160), which shows the zero-rated exports.

Table 9: Extracts of domestic VAT Return (Output)

Component II: Computation of Output VAT			
Line	Description	Amount	Comments
100	Standard-rated supplies (sales)	+	Exclude VAT charged
110	**Zero-rated supplies (sales)**	**+**	**Exclude VAT charged**
120	Exempt supplies (sales)	+	No VAT charged
130	Total supplies (sales)	+	Lines 100+110+120
140	Output VAT payable on standard-rated supplies	+	Line 100 x rate
150	Adjustments	+/-	Debit/credit notes
160	Total Output VAT for period	+	Lines 140 +/- 150

Table 10 shows the inclusion of imports in Component III *(line 200 and 230)* relating to purchases, expenses and input tax credit (ITC).

Table 10: Extract of domestic VAT Return (Inputs)

Component III: Computation of Input Tax Credit (ITC)			
Line	Description	Amount	Comments
200	**Value of taxable imports—excluding VAT**	**+**	**Exclude VAT paid**
210	Value of taxable domestic supplies—exclude VAT	+	Exclude VAT paid
220	Total value of inputs or supplies	+	Line 200+210+220+230
230	**Import VAT paid/payable**	**+**	**Customs entry**
240	Domestic VAT paid/payable	+	Line 210 x rate
250	Adjustments: debit and credit notes	+/-	Debit/credit notes
250	Adjustments: irrecoverable input VAT	+/-	Relates to exempt sales
260	Total input VAT paid/payable for period	+	Lines (250+260)+/-270

Where the original transaction (or invoice) value is not acceptable, customs offices adjust the foreign invoice submitted by importers and exporters for the supply of goods by applying the provisions of the WTO Valuation Agreement. Hence, for these and other business reasons, the adjustments may include changes made to import and export items.

Import and export values on domestic VAT returns

VAT laws require registered persons to disclose certain import and export values for the month or accounting period in which a registered person files a domestic VAT return.

Common disclosures: The common disclosures for import-dependent countries include—

- *value of imports:* this is the CIF value calculated in the tables in this chapter, plus the relevant import duties, excises and levies that affect the computation of import VAT;

- *value of exports:* the value of exports, also as calculated in tables, that is subject to zero-rating in the accounting period;

- *import VAT paid:* the total amount of VAT paid on imports (or exports);

- *input tax credit (ITC):* the full or partial amount of the total import VAT that can be offset against the Output VAT in the accounting period; and

- *period of disclosure:* these import and export values are disclosed in the month in which the entry is approved by customs—they are not on preceding value basis, as normally happens with domestic VAT values (Chapter 16).

The Import VAT offset against Output VAT must conform to the normal ITC rules by being related to only taxable supplies. Hence, where import VAT relates to taxable (including zero-rated) and exempt supplies, the ITC claim must be apportioned accordingly (Chapter 6).

Non-registered businesses: It is necessary to discuss non-registered entities in the context of imports and exports. Even consumers are eligible to pay VAT on taxable imports.

- Non-registered businesses do not file domestic VAT returns even if they pay Import VAT (it may be embedded in their purchases).

- They are not eligible to make ITC claims, including the right to offset Import VAT against zero-rated exports (which is automatic under VAT/customs laws for even non-registered businesses).

As noted in Chapter 13, VAT laws allow small business entities with sales below the turnover threshold to register voluntarily. Note that exports are included in the value for determining the annual turnover or registration threshold.

Domestic VAT declarations

The discussions to this point clearly suggest several combinations of domestic and foreign transactions involving taxable (including zero-rated) and exempt output (sales) and inputs (purchases and expenses). Table 11 shows five combinations of these transactions (with apportionments based on sales or turnover values).

Table 11: Examples of domestic and international trade transactions

Category	Nature of transactions
Simple examples	
A	Domestic sales (taxable) from imported and domestic supplies (both taxable).
B	Domestic sales (taxable) and exports (zero-rated) from imports and domestic supplies (both taxable).
Complex examples	
C	Domestic sales (taxable/exempt) from imports (taxable/exempt) and domestic (taxable) supplies.
D	Domestic (taxable/exempt) sales and exports (zero-rated) from imports and domestic purchases (taxable/exempt).
E	Same as D but in different proportions.

Tables 12 is an illustrates the five simple and complex transactions shown in e 11 above.

Table 12: Combinations of domestic and foreign trade transactions

Examples of transactions					
Transactions	**Simple**		**Complex**		
Firms	**A**	**B**	**C**	**D**	**E**
Sales:					
Domestic taxable	2000	500	1000	800	400
Exports		1500		700	1200
Domestic exempt			1000	500	400
Total	2000	2000	2000	2000	2000
Inputs:					
Import taxable	1000	1000	600	500	500
Import exempt			400	300	300
Domestic taxable	400	400	400	200	200
Domestic exempt				400	400
Total	1400	1400	1400	1400	1400
VAT rate	10 percent				
Calculations of VAT payment and credit (refund)					
Firms	**A**	**B**	**C**	**D**	**E**
Transactions	**Simple**		**Complex**		
Output VAT					
Domestic taxable	200	50	100	80	40
Exports		0		0	0
Domestic exempt			na	na	na
Total	200	50	100	80	40
Input VAT					
Import taxable	100	100	60	50	50
Import exempt			na	na	na
Domestic taxable	40	40	40	20	20
Domestic exempt			na	na	na
Total	140	140	50	53	56
Net VAT	60	(90)	50	28	(16)
Rate	10%				
Apportionment (sales)			50%	75%	80%

na = no [rate] applicable

F. VAT on imports and exports of services

The VAT on imports and exports of services is more difficult to administer than foreign supplies of goods. This is particularly the case for imported services.

General features: In general, a summary of the key issues relating to the imports and exports of services include the following:

- *personal involvement:* the import and export of services usually have elements of personal involvement because of their specialty nature (e.g., accountants, lawyers, sportsmen and entertainers);

- *destination principle:* in principle, service transactions are based on the destination principle discussed in Section B, with one notable exception for imported services, as it relates to place of supply rules (Chapter 2);

- *place of supply:* given their personal nature, services are deemed to be rendered (and, hence, subject to VAT) in the location or business where they are *received*—which, in particular, makes foreigners accountable for VAT locally;

- *enforcement:* while they are accountable, it is difficult to enforce the domestic VAT laws against foreign suppliers—hence the local recipient (not the foreign supplier) is accountable for VAT on imported services under the *reverse charge* rule; and

- *reverse charge rule:* registered local recipients are required to self-assess the Output VAT on imported service and, *in reverse,* claim it on the VAT return as an *input tax credit (ITC)*—provided they relate to taxable supplies.

The ensuing paragraphs discuss more of these rules, including so-called reverse charge rules that are unique to imported services.

Place of supply: The approach to taxing imports and exports of services depend on their definition.

- The place of supply of services is deemed to be where they are *received*, not necessarily where the supplier is resident or registered.

- In general, therefore, services provided to foreigners—and those they may provide—locally are subject to VAT.

The key compliance issue is that foreigners are often non-resident and it is difficult to enforce the law against them—hence, the need for special rules for imported services.

Imported services: Since it is difficult to hold foreigners accountable for VAT, the importer is held accountable for both Output VAT and, *simultaneously or in reverse*, Input VAT. The implied reverse transaction—in “reverse charge” rules—is equivalent to a contra entry in financial accounting. Example 1 illustrates the point.

Example 1: Imported services

Messrs. DanTosu & Sisters engage the services of a foreign expert from Repkret Enterprises for 120,000 to install proprietary machinery for the production of Product X. The taxable sales and expenses for the period were 500,500 and 370,230 respectively.

Table 13: DanTosu's imported service records

Transaction	Value	Output VAT	Input VAT	Net
Sales (Output):				
Sales	500,500	50,050		
Consulting fees	***12,500***	***1,250***		
Purchases (Input):				
Purchases	370,320		37,032	
Consulting fees	***12,500***		***1,250***	
Totals		51,300	38,282	13,018
Rate	10%			

In the suggested answer above, the local firm self-assesses and makes a contra entry (bolded) for the VAT which the foreign expert should have charged. However, immediately *in reverse* or simultaneously, DanTosu takes an ITC for the amount charged. VAT offices accept the domestic recipient's invoice to support the imported service transactions.

Exported services: Under the above rules, if the recipient of the service is overseas (or the service relates to property located overseas), the supply is deemed to be an exported and must be zero-rated. Example 2 and Table 14 illustrates this transaction.

Example 2: Reverse charge rule

Kway (Merton) Inc makes domestic supplies of taxable services for 150,000 in the period. The cost of taxable inputs for the services was 130,000. In addition, the firm sends an expert to Airegin (a foreign country) to provide services to EFT [Canterbury Woods] Ltd: taxable supply 25,000 which cost Kway [Merton] 18,000. The VAT rate is 10 percent.

Table 14: Reverse charges

Transactions	Cost/ Price	Input VAT	Output VAT	Net VAT	Comments
Purchases (input):					
General services	125000	12500			Non-imported services
Expenses--exports	18000	1800			ITC [reverse charge]
Sales (output):					
Domestic	150000		15000		Includes EFT [CWES] charge
Exported services	25000		0		Reverse charge
VAT payable		14300	15000	700	Output VAT less Input VAT
Rate	10%	Export :	zero-rated		

In general, taxpayers have a better incentive to declare the export of services because they are zero-rated. The collection of VAT on imported services is more difficult enforce.

G. Property and supplies related to property

The VAT on fixed property depends on the domestic or foreign location of the property at the time of sale or acquisition. The location also determines the taxation of goods and services related to the property.

VAT on disposal of property

As noted in Chapter 2, property is fixed or immobile in comparison with goods. The domestic and foreign trade rules relating to property are relatively straightforward.

- *Property located in domestic market:* VAT is due on the sale of property located in a country—unless it is a special class such as residential property.

- *Property located abroad:* Property located in overseas is outside the jurisdiction of domestic VAT law. Therefore, their sale by domestic owners will not be subject to VAT. Note particularly that it is immovable and, therefore, no export arises.

The complex issues often involve other goods and services (e.g., legal or accounting fees) related with, or connected to, property located overseas (even when it is not for sale).

Supplies connected to fixed property or goods

In principle, supplies connected to domestic fixed property is subject to VAT while those relating to property located outside are zero-rated. The crucial test is that the supplies must be separate and not merely complementary to a transaction involving the fixed property.

- *Connection to the primary supply:* The first rule is to establish that the secondary supplies are “connected’ to the primary property or good. In other words, the supply should be complementary or composite—not multiple or separate—to be on the same basis as the primary supply (see Chapter 2 and 8).

- *Connection to the country:* The second important rule is that the primary commodity should be connected to a foreign country to be zero-rated by a registered person. This is easy to ascertain for fixed property.

In essence, the VAT on a supply connected to goods or property depends on its composite or multiple nature. The location of the supplier (i.e., resident or non-resident) is irrelevant in these cases. The following two implications are worth noting:

- the supply of a service to a foreign client in relation to property located outside the country can be zero-rated by a domestic registered firm (or the payment is made by resident agent of the foreign firm); and

- similarly, the domestic firm can zero-rate the supply if the property is owned by a resident person who makes the payment domestically.

Examples of supplies that could be zero-rated because they are related to property or goods located overseas include architectural, insurance, legal, security and repair services for a property located outside the country.