

EXEMPTION FROM VAT

Source of exemption

- Art 8 of the VATP no. 285/ 2002 and art 20 to 34 of VATR no. 79/ 2002 lists the exempted good and services from VAT
- Delegation of power to exempt is given to now minister of finance and economy cooperation, then MOFED pursuant to art 8 sub 4 of the VATP. Accordingly it declares some exemptions.
- Agreements

Reasons for exemption

- To minimize regressive nature of VAT
e.g exemption of education and foods
- Difficulty nature of the good or service
e.g financial service
- To decrease inflation e.g palm oil
- Encouragement: e.g printing and sale of books
- Keeping society value: e.g religious activity

1. Dwelling house (art 8 sub 2 [a] VATP as amended and art 19 VATR)

- Since it is difficult to identify dwelling as consumption or saving.
- Shelter is a necessity for life
- Sale of dwelling house used at least for two years or lease for dwelling is exempted.
- It does not include rent in motel, hotel, hostel and other similar business
- Is real state housing subject of this exemption?
- In practice real state are not subject of exemption.

2. Financial service (art 8 sub 2 [b] VATP and art 20 VATR)

- b/c it is difficult to create conventional transaction
- It is connected with money which is a medium for exchange
- Even the proclamation puts the exemption in open air, the regulation restricts to what extent financial service be exempted. This is articulated by listing the exempted and non exempted services in inclusive way.

Exempted financial services include:

- Granting, negotiating, or dealing with loans, credit, credit guarantees, or any security for money, including management of loans, credit, or credit guarantees by the grantor; or
- Transactions concerning money including interest
- Provision of credit under a hire purchase agreement
- Transfer of ownership, of an insurance policy

Non-exempted financial service includes:

- Legal, accounting and record package services, actuarial, notary, and tax agency services
- Safe custody for cash, documents or other items;
- Data processing and payroll services;
- Debt collection or factoring services;
- Management services, such as management of a superannuating fund;
- Trustee, financial advisory, and estate planning services,
- Leases, licenses, and similar arrangements relating to property other than a financial instrument.

3. Religious or related services(art 8 sub 2 [e] VATP and art 23 VATR)

- Pure religious doctrinal services
- Sale and print of religious books
- Donation if there is no consideration
- Are renting of house or some other income deriving activities of business also not subject of VAT?

4. Medical service and medicine (art 8 sub 2 [f] VATP and art 24 VATR)

- There is a need of qualified person or the service is given in qualified institution.
- Being required the above the following are the subject of exemption:
 - Medicine and drug
 - Laboratory and other diagnostic services
 - Meals and other accommodations
 - Room service for medical service
- Are traditional licensed reactionaries qualified persons?

5. Educational service (art 8 sub 2 [g] VATP and art 25 VATR)

- It must be taken in qualified institutions from pre-primary to universities.
- Course instruction, materials related to education process including meals when available, transportation
- Religious students are also considered here as students.
- House rent or other rents are not exempted as related service of education
- Are short trains like Burberry part of education service?

6. Other exempted supplies in VATP and VATR

- The Supply or import of national or foreign currency
- The import of gold to be transferred to the National Bank of Ethiopia
- The supplies of electricity, kerosene and water (except for those supplies of water bottled by a factory)
- Supplies by the post office authorized under the Ethiopian postal proclamation, other than services rendered for a fee or commission

Continued list of exemption

- The provision of transport
- Permits and license fees
- The supply of goods or services by a workshop employing disabled individuals if more than 60 percent of the employees are disabled
- Supply of books
- Humanitarian service related imported or purchased supplies
- Goods imported in schedule 2 of the tariff

7. Exemptions by letters (may be directive)

- Supply of food grain e.g. Teff, Wheat, Maize, Sorghum and other cereal. (Circular Ref. No. __3/16/28/635 Dated 09/07/2000 E.C.)
- Materials for making mosquito net such as fiber (thread), label, plastic for packing and polypropylene bag (Circular Ref. No __3/16/28892 dated 08/07/2001 E.C.)
- Purchase of the production of pickle, wet blue, and crests by leather factories. (Circular Ref. No __./16/26/28/860 dated 10/02/2001)

Continued list of exemption

- Import of mosquito net and import of cloth, immersed in chemical, for sewing mosquito net (Circular Ref. No __3/16/28/785 __ 10/02/2001)
- Import of wheat by the government (Circular Ref.No.__3/16/28/914 Dated 11/02/2000 E.C.)
- Import of palm oil (Circular Ref. No .__3/16/28/9644 dated 25/07/1994 E.C.)
- Supply of bread and milk (Circular Ref.No. .__3/16/28/889 dated 09/05/1995 E.C.)
- Medicine, Medical supplies, and medical kits (Circular Ref. No .__3/16/28/889 dated 09/05/1995 E.C)

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- Supply and import of agricultural raw materials such as fertilizer, seeds of superior quality, insecticides (Circular Ref. No re3/16/28/930 Dated 28/06/1995).
- Payment of pension fund (Circular Ref. No .__3/18/28/961 Dated 01/09/1995).
- The sale of air-tickets to customers by travel agents (Circular ref. No. __3/16/28/13 Dated 01/25/1996).
- Enjera (Circular Ref. No. __3/16/28/171 Dated 11/10/1997)
- Publication of books (Circular Ref. No. __3/16/28/185 Dated 05/09/1997)
- Animal skin or hides sold to shoe factories by a leather factory after the tanning process is done. (Circular Ref. No. __3/16/28/227 Dated 08/11/2000)
- The supply or import of fuel gas (Circular Ref. No. .__3/16/28/227 Dated 25/12/2007)

VAT registration

- In Ethiopia we have Two types of VAT registration:
 - Obligatory registration (art 16 of VATP)
 - Voluntary registration (art 17 of VATP)

Obligatory (Mandatory) registration

- Art 16 (1) strictly puts that a taxpayer who has the value of the taxable activities of 12 months is more than 500,000 Birr or is expected to be more than 500,000 at the beginning of the 12 months has the obligation to register of VAT.
- This sub article deals with:
 - The lower amount is 500000 which can be changed by MOFED
 - The valuation is only on taxable activity, it does not include nontaxable or exempted supply

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- Actual reaching on the lower amount
- An expectation to reach the amount evidence is needed
- Time consideration: 12 months
- Are zero-rated supplies part of the lower valuation amount?

Sector based obligation of registration

- VAT registration Directive no. 25/2001 art 4 (3) {c} introduced sector based obligation of registering VAT.
- Sector based obligation does not consider the lower amount
- There are two arguments whether this directive has legality or not.

Sectors obliged

- Gold
- Electronic business such as television, tape
- Plastic and plastic result factors
- Importers
- Shoe factory
- Contractor grade 1 to 9
- Computer and its spare part sale
- Skin result producer factors and sale of the goods

Issue of related parties

- To check whether a tax payer attains the obligation to be VAT registered the authority can aggregate the sum taxable activity of related persons and register them separate.
- The broad definition of related persons makes difficult to apply it.
- It is to avoid escaping from VAT.

Voluntary VAT registration

Art 17 of the VATP puts a taxpayer who supplies at least 75% to other VAT registered taxpayer can be registered in voluntary.

Tax authority has the power to reject the application of voluntary taxpayer not to register (art 18 sub 8 of VATP):

- The taxpayer has no fixed place
- Cannot keep records properly

Procedure of registration

- Application by taxpayer immediately on the obligation comes
- The authority can also issues certificate in its own motion
- The tax authority shall check the reality and issues certificate for the taxpayer
- The authority can permit separate registration for branched on their application
- Onwards taxpayers are obliged to use their VAT number in each leaf

VAT cancellation

- At the time of death or close of business or
- After three years the transaction of taxpayer become lower than 500,000 birr with in twelve months
- the taxpayer can apply for cancellation and cancellation time will be the time of application unless the taxpayer run the business.

Place, Time and Valuation of Supplies

1. Place

Goods starts: principle

- Where the transfer of good is occurred

Goods: exception

- At the place where transport starts
- At the recipient place if the good is energy thermal. But if the recipient is out of Ethiopia, the starting place

Place of service

General principle:

- The place of registered person

Exceptions:

- Immovable property related where the property is situated
- Actual carrying out place: e.g transport, art, technician services

2. Time of supply

- At the time of invoice is done
- In absence of invoice the time when payment is made
- In continuous service delivery and prepayment was done the time when the payment shall payable
- The time of custom declaration is done for imported goods.

3. Valuation of supply

- The return the receiving person pays plus any duty, tax that can be paid but does not include VAT.
- Market price plus any duty, tax that can be paid but does not include VAT.
- Custom value and other payable taxes but not VAT and withheld income tax.

CALCULATION OF PAYABLE TAX

Calculating methods

- Every tax payer in the supply chain undertake the act of controlling and collecting the tax, remitting the amount of the tax corresponding to the margin obtained on each transaction, or the difference between the VAT paid out to suppliers as **an input tax** and the VAT collected from customers **as output tax**.
- To reach at actual taxable VAT in each chain we have two methods.

1. Invoice credit method

- The invoice credit method demands each business collects VAT at the fixed rate on each sale and gives the buyer an invoice certifying the portion of tax thus charged. Then the buyer can reduce the taxes paid to the supplier who supplied input against the tax collected from customers if his transaction is subject to VAT.
- The issue of VAT inclusive and exclusive

Advantage of invoice credit method

- There is crucial evidence: the document
- Audit is simple
- Simple to have any account period
- This is why most countries follow it.

Applying the VAT Rate: VAT inclusive and VAT Exclusive

- VAT may be calculated inclusive or exclusive of the price of the good. In the case of invoice credit method, VAT is typically calculated exclusive of the price. This involves a simple application of the VAT Rate to the basic price of the good.
- The VAT inclusive method tries to extract the VAT embedded in the price/value of the good. This method is used to calculate VAT where

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- The VAT was not applied in the first place or where VAT cannot be imposed due to the peculiar nature of the transaction.
- This method is also used where the tax system uses the subtraction method without the invoice credit system. The VAT inclusive method ensures that the amount of VAT collected through the exclusive method is equal to the VAT collected through the inclusive method.

2. Subtraction method

Tax is imposed directly on value added calculated from the account of the firm by subtracting VAT calculated on allowable transactions from VAT on taxable sales. Registered tax payer subtracts the value of total non-labor inputs from their gross sales transaction to get the value added by them and then this is multiplied by the tax rate to figure out the tax on added value.

Disadvantage of subtraction method

- It is one year method
- It is difficult to audit
- No crucial evidence

3 allowed VAT input In Ethiopian context (art 21 of VATP art 11 VATR)

- VAT paid or payable by registered person on imports
- VAT paid or payable at purchase of domestic goods or services
- In case of mixed purchase or importation to the extent of VAT paid or payable
- No VAT input is allowed to:
 - Passenger vehicle
 - Entertainment expense

Reverse taxation (art 23 of VATP art 12 VATR)

- Withholding VAT from taxable service rendered by non-resident person by the recipient person.
- The following persons are expected to withhold it:
 - VAT registered person
 - Legal person

Accounting period and Refund

- The time when tax (VAT) shall be declared and paid is within one month from transaction performed, **a month**.
- The declaration shall be made in a form prepared by tax authority, mostly by the Ethiopian revenue and custom authority (ERCA)

Refund of VAT

- When the tax payer's transaction is 25% and above at zero-rated. Transferring for two months
- Input tax is greater than output tax. Transferring for five months.
- ways of refunding:
 - Crediting for any tax
 - Refunding money if it is more than 50 birr.

Obligation of taxpayer

- Registering to VAT when reached the minimum threshold.
- Giving an invoice for each sale
- Declaring and paying VAT each month. Even if there is no payable VAT there shall be a Nil declaration .
- Preparing records of book
- Keeping records for ten years

Methods of Assessment

- VAT withholding system: introduced in VATP amendment art 2 sub 4
- Governmental offices attain this obligation.
- Self declaration s