

Vat no. 20

1. INTRODUCTION

This leaflet is a guide to contractors. The services made in the construction industry are made over a long period of time, in some cases covering several tax periods, and thus creating difficulties in determining the tax point and the taxable value. This brief leaflet helps explain how VAT applies to the Industry. It should, however, be read in line with the VAT Act, VAT Guide, and VAT Liability Guide.

2. CONTRACT

The construction Industry largely comprises Building Contractors, Road Contractors, and Sub-contractors. Projects in the industry are governed by a contract which specifies all the terms including:

- a) Frequency of certificate of valuation and terms of payments;
- b) Advance payments;
- c) Payments towards the Certificate of Valuation; and
- d) Retention's

There are formally two types of contracts and these are:

- I) Fixed Price Contracts - The price of the contract is fixed but provisions for fluctuations and variations are made.
- II) Cost Plus Contract - Purchase price of materials and other expenses incurred by the contractor are reimbursed by the client including a percentage for profit.

3. DEFINITIONS

- I) Bill of Quantities - A report prepared by independent quantity surveyor specifying:
 - a) the contract price; and
 - b) list of materials to be used with quantity and price estimates.

The bill of quantities serve as a performance standard for evaluation of the quality of work performed.

- II) Preliminary and General Items - Cost of setting up and maintaining a project site e.g material storage facilities.
- III) Measured Work - This is the work done in respect of quantities and costs specified in the bill of quantities.

- IV) Variations and Extra Works - This is the work done on the project but was not originally included in the bill of quantities.
- V) Materials On/ Off Site - The cost incurred for all material for the project.
- VI) Retention - The client withholds certain amounts of money from the certificates as a precaution against failure to execute the project by the contractor. This amount is paid to the contractor upon issuing of the certificate.
- VII) Advance - Normally an advance payment is made to the contractor before the work commences. Advance payments should be treated as part of the taxable value at each stage when such payments are made.
- VIII) Fluctuations - Fluctuations take into account of changes in prices of materials and wage rates.
- IX) Amounts Previously Certified - This amount is the sum of all amounts certified in previous stages to date.

4. TAXABLE VALUE

Since the project may cover more than one tax period, at times extending over a number of years, certificates are issued in the interim according to the frequency stipulated in the contract. The certificates are based on the percentage of completed work and VAT is calculated on the certified value of the portion of work completed at each stage.

ILLUSTRATION

			<u>Amount (K)</u>
Preliminary and General Items	20,000		
Measured Works	100,000		
Variations and Extra Work	30,000		
Materials On/ Off Site	20,000		
Sub-total	170,000		
Add: Advances	50,000		
Fluctuations	<u>60,000</u>	<u>110,000</u>	<u>280,000</u>
Less: Retention @ 5%	14,000		
Amount previously certified (which are VAT inclusive)	<u>120,000</u>		<u>134,000</u>

Value of Completed Portion of Work (Taxable Value)	146,000
VAT @ 16%	<u>23,360</u>
Amount Due on the Completed Portion of Work	<u>169,360</u>

5. TAX POINT

The tax point is the time when goods or services are considered to be supplied for VAT purposes. In case of services, it is the earliest of the following:

- a) the time when payment for the supply is received;
- b) the time when a tax invoice is issued; or
- c) the time when services are actually rendered.

In practice, the sequence of events in the building industry is likely to be:

- a) interim certificates are issued and payment made on the amount involve (creating a tax point and a tax liability for the amounts involved).
- b) Any part payments, including interim or advance payments also create a tax point.
- c) Completion of the building services - the tax point in this case will be the date of issue of a compliance certificate, which then creates the tax point for any remaining payments due. The practice of issuing a tax invoice and /or accounting for output tax when the final contract payment is due or made is not allowed under VAT. The only exception would arise when a business is authorised to use payment basis.
- d) Issuing of a tax invoice for work /payments not covered by (a), (b), and (c) above also creates a tax point.

6. SPECIAL CASES

I) Construction of Domestic Building

The Exemption of "Sale or Lease of Domestic Buildings" does not cover the provision of construction services provided for building or renovation of domestic buildings. It is only the lease or sale of the domestic buildings that is exempt. If a developer builds a house on a plot for resale or a self occupier house, the supply is exempt. The crucial test is what exactly is supplied and in the case of a building contractor it is likely to be construction services which are taxable.

II) Zero-Rated Construction Services

Construction services supplied to the following persons or group of persons are

zero-rated subject to conditions provided in Group 2 of the second schedule of the VAT Liability Guide:

- I) the supply of services to a donor in Zambia for official purposes of that donor;
- II) services supplied under a technical aid programme or project which are:
 - a) paid for through donor funding; and
 - b) provided by the donor or by a contractor of the donor, under a written agreement with the Republic of Zambia.
- III) services supplied under a technical aid agreement or project providing for exemption from Zambian taxation which is either:
 - a) dated on or before 30th June, 1996; or
 - b) approved by the Minister of Finance.

7. WHAT INPUT TAX CAN I CLAIM?

VAT incurred on business purchases can be claimed by VAT registered suppliers if they are in possession of a valid tax invoice. Examples of purchases on which VAT can or cannot be reclaimed are:

RECLAIMABLE

(N.B. Only if for use in the business you are registered for)

Building materials
Sub-contractor costs
Diesel
Plant and equipment
Electricity charges
Legal and accounting fees
20% of Petrol expenses

NOT RECLAIMABLE

Purchase of saloon cars,
station wagons and twincabs
Telephone charges
Business entertainment

8. REMINDERS

- I) As a VAT registered supplier, you will be required to submit VAT returns and pay VAT to the Zambia Revenue Authority on or before 21st day of the month after each tax period. Payment must be made by either a company cheque or a bank certified cheque. Once a company cheque is dishoured by your bank you will be required to pay VAT by a bank certified cheque. Voluntary VAT registered suppliers are required to submit a return within 21 days after the end of their three monthly tax period.
- II) Late submission of returns attract an automatic penalty of K180,000, or 0.5% of the tax due: whichever is higher for each day that the return is late. Non payment

of VAT attracts an automatic penalty of 0.5% of the tax due for each day that VAT remains unpaid and the amount outstanding will attract interest.