Draft Law no. /

VALUE-ADDED TAX LAW

Explanatory Note

Transfers from the Petroleum Fund account for the majority of revenue in the General State Budget. In fact, the percentage of revenue originating from Petroleum Fund transfers has, since its creation, fluctuated between 60% and 90% of total revenue. Although in recent years, revenue from Petroleum Fund transfers has fallen below 60 per cent, this in itself does not represent a reduction in the State Budget's dependence on this type of revenue, as this is the result of changes in the budgeting of management balances and the increase in Social Security revenue, which although it counts towards total revenue, does not finance the central government expenditure.

In the first years after the creation of the Petroleum Fund, most of its revenue came from taxes on petroleum activities. However, with the decline in oilfield revenues, the fund now depends on its financial investments for most of its income. Continued withdrawals above the estimated sustainable yield are currently expected to deplete the Petroleum Fund by 2035. According to current forecasts, Timor-Leste is expected to face a fiscal cliff by 2035, with the General State Budget showing a deficit of 2.3 billion US dollars.

In this context, Law no. 8/2022 of 15 June, which approved the Major Planning Options for 2023, identified the need to diversify the sources of funding for the General State Budget by increasing tax revenue, broadening the tax base, adopting more modern taxes and reviewing tax rates in order to achieve a more progressive tax burden.

To this end, and as was also clear from point 14.2.7 of the aforementioned law, point 5.3.2 of the IX Constitutional Government's programme defined the introduction of value added tax (VAT) as one of its objectives.

With this proposed law, the 9th Government is therefore implementing the objective of introducing VAT in Timor-Leste.

I.

Given the context described above, the main purpose of creating this new tax is to obtain new sources of tax revenue.

However, the following concerns were particularly present in its design: i) ensuring a simple tax system that is easy to apply for taxpayers and the state; and ii) keeping the tax burden at levels that are compatible with the country's economic and social reality.

With regard to the concern to ensure a simple tax system that is easy for taxpayers and the state to apply, this bill has deliberately chosen to minimise the number of tax rates, exemptions, exceptions, and special regimes. In fact, the government's intention is that VAT should have a single tax rate, and that exemptions, exceptions and special regimes should only be those that are required for technical reasons. In this way, it will be possible to ensure the correct application of the operating mechanisms of the tax itself and of the refund system. It will also be possible to limit the initial scope of application of VAT to a universe of taxpayers that is manageable for the tax administration, particularly for inspection and collection purposes. Otherwise, there would be a serious risk that the introduction of VAT would generate situations of abuse or tax fraud that the tax authorities would find exceedingly difficult to detect.

With regard to the concern to keep the tax burden at levels compatible with the country's economic and social reality, this bill ensures this in two particular ways: on the one hand, by ensuring a very low tax rate, compared to international rates; on the other hand, by ensuring that the scope of the new tax is limited to very large taxpayers.

However, to the extent that the implementation of VAT is successful, additional layers of complexity and expanding the number of taxable persons covered could be considered later, as the system proves to be consolidated, and also taking into account the levels of formalisation of economic activity, the ability of consumers to pay, and the operational difficulties experienced by taxable persons and the tax administration.

In the meantime, and especially with regard to certain technical options that would bring additional complexity to VAT, simplicity has been favoured over perfect neutrality.

This proposal was based on the work of the Tax Reform Commission, which had been practically completed and professionally reviewed with rigour and technical precision, as well as the analyses and contributions of development partners, in particular the Asian Development Bank, the International Monetary Fund and the United Nations, especially with regard to the design of the tax itself.

Nevertheless, this bill should be read in conjunction with the proposed new Tax Law.

In fact, in the new Tax Law, there are aspects that are transversal to all taxation and all taxes that should also apply to VAT, such as certain legal and tax definitions (for example, the definition of "entity" or "permanent establishment"), the means of paying tax, the way in which declaratory obligations are

fulfilled, the rules for carrying out accounting, the rules for invoicing, the rules for converting amounts denominated in foreign currency, etc.

For these reasons, the new Tax Law will apply to VAT in everything that is not specifically provided for in this proposal. In this way, it is also clear that the powers of the tax administration are applicable to VAT, particularly with regard to its reciprocal relations with taxpayers, administrative mechanisms to combat tax evasion, and provisions common to the administration of all taxes. As also indicated in the Tax Law, the legal regime of the tax procedure relating to the collection and recovery of tax, provided for in UNTAET Regulation no. 18/2000, of 1 July, as amended, and UNTAET Directive no. 2/2001, of 31 March, as well as the provisions on infractions and penalties provided for therein, remain applicable until the entry into force of the law that defines them, insofar as they have not been derogated from by law.

As far as sales tax is concerned, it should also be noted that the new Tax Law already eliminates the legal provisions that used to make it equivalent to a value-added tax, but which were never actually implemented. In fact, since the sales tax in practice only applied to imports, and as such was equated to customs duties on imports, the new Tax Law opted to replace the sales tax with a corresponding increase in the rate of customs duties on imports. However, even with the incorporation of sales tax into customs duties on imports, the respective tax rate remains at low levels compared to other island nations with levels of development comparable to Timor-Leste.

Considering this aspect, the new VAT is, at this stage, effectively being introduced as a new source of tax revenue, mitigated by the neutrality of its operating mechanism. However, in the medium and long term, the prospect is that the successful implementation and extension of VAT will lead to a reduction in customs duties on imports.

Finally, it should also be noted that the new Tax Law also eliminates the tax on services, which only charges certain types of business activities, in an unjustified deviation from the principle of neutrality in the tax system, and is also a tax that is of little significance to the state in terms of revenue collection. In contrast, the new VAT is applied more homogeneously and equitably to all consumption of goods and services.

II.

From a technical point of view, some aspects of this bill deserve special mention, especially from the point of view of methodological options. Some of these options are presented below.

The reference to international law in Article 2 of this draft law aims to extend the territorial scope of VAT to the whole of TimorLeste's national territory, including its territorial sea, as well as its exclusive economic zone and continental shelf.

However, Article 5(2) excludes taxable transactions carried out in the context of *offshore* oil exploration from the scope of VAT. On the other hand, transfers of goods dispatched or transported to those oil platforms are treated as exports subject to tax at a rate of 0%, under the terms of Article 17, and the entry of goods from those platforms is treated as an import of goods, under the terms of Article 8(2).

This approach not only favours the administration of the tax, especially at customs level, but also allows Timor-Leste to honour its international commitments regarding the taxation of the former joint petroleum development area.

In Article 4, the state and public entities are not categorised as taxable persons for VAT. In fact, it was considered methodologically more efficient to avoid creating additional obligations for the state and public entities to obtain already public and general revenue. This approach has the additional advantage of not subjecting supplies of goods and services made by the state to VAT, particularly in the areas of health and education. On the other hand, considering the low tax rate presented in this bill, it is considered that even in situations where the state and public entities occasionally carry out an economic activity outside the scope of their respective powers of authority, not subjecting them to VAT does not give rise to significant distortions of competition with the private sector.

In Article 7, this bill has opted for a residual definition of the concept of the provision of services, categorising as such all onerous transactions that do not constitute the transfer or import of goods. The aim was to avoid creating gaps that could result from a closed definition.

However, making donations is not considered a taxable transaction for VAT purposes. In the case of monetary donations, the definition of transfers of tangible goods in Article 2 does not include money under the terms and for the purposes of Article 6. In the case of donations of non-monetary goods or services, the absence of consideration excludes them from the concept of transactions for consideration under the terms and for the purposes of Article 7.

In Article 8, the concept of importing goods for VAT purposes has been aligned with the taxable event that customs legislation provides for in relation to customs import duties and excise duty, i.e., the moment of release for free circulation. Thus, imports of goods under a suspensive customs regime (namely those destined for customs warehouses) are not subject to VAT until the moment they are released for free circulation, making it easier for the customs services to assess the tax, which as such will be carried out together with the other duties, taxes and charges due on imports, under the terms of article 24.

Under the terms of Article 23, VAT is generally paid to the state by taxable persons who conduct taxable transactions. In other words, the suppliers of the goods or services hand over the tax they have collected from the purchasers to the state under the terms of Article 28. However, Article above 23 also contains a *reverse charge* rule: for certain services which, under the terms of Article 10, are deemed to have been supplied in Timor-Leste and whose supplier is a non-resident without a permanent establishment in Timor-Leste, it is up to the purchaser of the service to reverse charge and hand over the tax directly to the state, provided that the purchaser is a taxable person not covered by the special exemption regime.

Article 16 of this draft law provides for a single general tax rate, set at [5%], applicable to the entire territory of the Democratic Republic of Timor-Leste. The application of special rates to what are commonly referred to as peripheral areas is not in line with recommended international practice. Furthermore, at least in the initial phase, it is expected that the tax rate will already be sufficiently low compared to international rates. As such, it was considered inadvisable to introduce special (reduced or

intermediate) tax rates for certain categories of goods or services, as this approach would make it more complex for taxpayers to fulfil their obligations and for the tax authorities to administer the tax.

The only exception to the application of the general rate is exports and similar transactions, which for technical reasons, and under the terms of Article 17, are subject to a rate of 0 per cent, as an alternative to an exemption. In this way, it is clear that exports give rise to the deduction of input VAT by the taxable person, i.e., that this is, in practice, a complete exemption aimed at favouring the competitiveness of Timorese exporters in the international context.

On the contrary, the number of so-called incomplete exemptions under Article 18 has been deliberately reduced to a minimum, also for technical reasons.

In particular, this concerns financial transactions for which there is no specific consideration (since otherwise it would be extremely complex to precisely define the respective taxable value), and transfers of rights in rem in immovable property (which according to the proposed new Tax Law are subject to a new tax on each real estate transaction).

The number of VAT exemptions provided for in Article 18 considered the fact that they entail - as described above with regard to special tax rates - an increased degree of complexity for both taxpayers and the tax administration.

In fact, exempting certain transactions from VAT implies giving different tax treatment to sales of certain goods and supplies of certain services.

On the other hand, taxpayers cannot deduct input VAT on sales of exempt goods or services. In other words, if you do not pay VAT on a particular transaction, you cannot deduct input VAT on that transaction either.

Thus, so-called mixed taxable persons (i.e., those who conduct both exempt and non-exempt transactions) are obliged to quantify the part of input VAT that can be deducted, applying certain methods of partial tax deduction (in this case, the percentage deduction method, or *pro rata*).

For the tax administration, this implies the ability to monitor the correct fulfilment of that obligation.
At this stage in the implementation of VAT in Timor-Leste, it is considered inadvisable to introduce such complexities which, as indicated above, could lead to situations of abuse or tax fraud that are exceedingly difficult to detect. For this reason, it is important to minimise the number of mixed taxable persons.

Added to this is the fact that VAT exemptions do not necessarily translate into an advantage for the end consumer. In fact, if a taxable person pays input VAT on exempt transactions, and cannot deduct that VAT on the output (because the transactions they carry out are exempt), then the tax ends up being included in the final price of the goods they sell, or in the price of the services they provide.

However, as we have already seen, social concerns and the need not to burden the purchase of so-called essential goods and services have been mitigated through alternative mechanisms that do not hinder

the implementation of VAT: i) on the one hand, a single, lower tax rate, as described above; ii) on the other hand, a general scope of application of the tax limited to larger taxable persons.

Specifically, only taxable persons with a turnover of more than [150,000.00] US dollars and fewer than fifteen employees will be obliged to pay VAT, as seen from articles 36 to 40. This particular exemption regime ensures that the tax burden is not too onerous and does not constitute a fiscal and bureaucratic burden for small businesses. On the other hand, the level of accounting sophistication required of taxpayers for VAT purposes is brought into line with the level of accounting sophistication required in the new Tax Law for income tax purposes. Thus, taxpayers subject to and not exempt from VAT will tend to be the same ones who, for income tax purposes, use the economic accrual method of accounting (instead of the cash accrual method).

Article 21 states that in cases where all the active and passive transactions conducted by the taxable person result in a VAT credit in his favour, he can deduct this credit from the VAT calculated in the following six months. Only at the end of this period can the taxable person request a refund if the credit situation persists. This approach makes it possible not to burden the tax administration with verifying and processing refund requests which, as a rule, will be of a transitory nature. This is only not the case for taxable persons with an export vocation, who, because they pay VAT on exports at the rate of 0%, can immediately request a refund of the tax borne in the tax transactions for the realisation of those exports.

In this proposal, it was deliberately decided not to include limitations on the right to deduct input VAT. In this way, the tax configuration is as simple as possible, favouring its practical implementation and contributing to the economy's formalisation.

As already provided for in the Tax Law, which, as we have seen, will be subsidiarily applicable to VAT, all the declaratory obligations stipulated in this law may be fulfilled electronically, favouring simplicity and efficiency in the administration of the tax (both for taxpayers and the tax administration), and the prevention of tax evasion. However, in addition to the provisions of the Tax Law, which already safeguard the specific provisions of this draft law, taxpayers subject to VAT and those not exempt from it are obliged, under the terms of article 27, to invoice their taxable transactions by electronic means, using computer programmes or equipment duly authorised by the tax authorities.

In this proposal, it was deliberately decided not to include transitional measures allowing the deduction of sales tax paid on the acquisition of the current assets of taxable persons. Although this option was possible, in order to ensure greater neutrality when VAT came into force, not only would it not be operationally possible for the state to verify the deductions in question individually, but this could imply a high volume of initial refunds that neither the state nor taxpayers legitimately counted on.

On the other hand, it would create a relationship of succession between sales tax and VAT that is intended to be guaranteed, but only with regard to legal and contractual rules in force (for example, under the Private Investment Act).

The Government therefore submits the following draft law to the National Parliament, pursuant to Article 97(1)(c) and Article 115(2)(a) of the Constitution of the Republic:

Law no. /
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special regimes. In fact, the government's intention is that VAT should have a single tax rate, and that exemptions, exceptions and special regimes should only be those that are required for technical reasons. In this way, it will be possible to ensure the correct application of the operating mechanisms of the tax itself and of the refund system. It will also be possible to limit the initial scope of application of VAT to a universe of taxpayers that is manageable for the tax administration, particularly for inspection and collection purposes. Otherwise, there would be a serious risk that the introduction of VAT would generate situations of abuse or tax fraud that the tax authorities would find exceedingly difficult to detect.

With regard to the concern to keep the tax burden at levels compatible with the country's economic and social reality, this bill ensures this in two particular ways: on the one hand, by ensuring a very low tax rate, compared to international rates; on the other hand, by ensuring that the scope of the new tax is limited to very large taxpayers.

However, to the extent that the implementation of VAT is successful, additional layers of complexity and expanding the number of taxable persons covered could be considered later, as the system proves to be consolidated, and also taking into account the levels of formalisation of economic activity, the ability of consumers to pay, and the operational difficulties experienced by taxable persons and the tax administration.

In the meantime, and especially with regard to certain technical options that would bring additional complexity to VAT, simplicity has been favoured over perfect neutrality.

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For these reasons, the new Tax Law will apply to VAT in everything that is not specifically provided for in this proposal. In this way, it is also clear that the powers of the tax administration are applicable to VAT, particularly with regard to its reciprocal relations with taxpayers, administrative mechanisms to combat tax evasion, and provisions common to the administration of all taxes. As also indicated in the Tax Law, the legal regime of the tax procedure relating to the collection and recovery of tax, provided for in UNTAET Regulation no. 18/2000, of 1 July, as amended, and UNTAET Directive no. 2/2001, of 31 March, as well as the provisions on infractions and penalties provided for therein, remain applicable until the entry into force of the law that defines them, insofar as they have not been derogated from by law.

As far as sales tax is concerned, it should also be noted that the new Tax Law already eliminates the legal provisions that used to make it equivalent to a value-added tax, but which were never actually implemented. In fact, since the sales tax in practice only applied to imports, and as such was equated to customs duties on imports, the new Tax Law opted to replace the sales tax with a corresponding increase in the rate of customs duties on imports. However, even with the incorporation of sales tax into customs duties on imports, the respective tax rate remains at low levels compared to other island nations with levels of development comparable to Timor-Leste.

Considering this aspect, the new VAT is, at this stage, effectively being introduced as a new source of tax revenue, mitigated by the neutrality of its operating mechanism. However, in the medium and long term, the prospect is that the successful implementation and extension of VAT will lead to a reduction in customs duties on imports.

Finally, it should also be noted that the new Tax Law also eliminates the tax on services, which only charges certain types of business activities, in an unjustified deviation from the principle of neutrality in the tax system, and is also a tax that is of little significance to the state in terms of revenue collection. In contrast, the new VAT is applied in a more homogeneous and equitable way to all consumption of goods and services.

This law therefore fulfils all these objectives, which converge to ensure the sustainability of public finances, while maintaining the simplicity of the tax system, the moderation of the tax burden and its economic neutrality.

Therefore, the National Parliament decrees, pursuant to Article 95(2)(p) of the Constitution of the Republic, to be valid as law, as follows:

Chapter I
Preliminary provisions

Article 1
Objective

This law creates value added tax.

Article 2
Territorial scope

Without prejudice to Article 4(1)(b), this Law shall apply to the territory of the Democratic Republic of Timor-Leste, including the special administrative regions, and to its territorial sea, exclusive economic zone, and continental shelf, in accordance with international law.

Article 3
Definitions and subsidiary law

1. For the purposes of this law, the following definitions shall apply:
   a) "tangible property" means any tangible thing, movable or immovable, including electricity, natural gas, heat, cold and the like, but excluding money;
   b) "consignment" means a contractual relationship as defined for the purposes of the Civil Code;
   c) "Enforceability of tax" means the right that the tax administration may enforce under the law, from a given moment, vis-à-vis the debtor, with regard to the delivery of the tax, even though such delivery may be deferred and subject to deductions;
   d) "taxable event" means the moment at which the legal conditions necessary for the tax to be chargeable are fulfilled;
   e) "Invoice" means the accounting document that certifies the realisation of taxable transactions, as well as other equivalent documents that contain the same elements as the invoice under the terms of [article 57(3)] of the Tax Law, namely receipts, debit notes, credit notes and customs documents;
   f) "tax" means the value added tax approved by this law;
   g) "importation of goods" means the release for free circulation in national territory of tangible goods from abroad, under the terms of Article 7;
   h) "deductible tax" means the tax that can be deducted, under the terms of Articles 20 to 23, from the amount of tax due for the taxable transactions conducted;
   i) "Tax chargeable" means the product of the value of the taxable transaction and the tax rate provided for in Article 14;
   j) "exempt transaction" means a taxable transaction in which tax is not assessed, and in which tax assessed on other taxable transactions necessary for the realisation of the exempt transaction is not deductible;
   k) "taxable transaction" means a transaction subject to tax pursuant to Article 5;
   l) "tax period" means a period corresponding to one month of the calendar year;
   m) "supply of services" means any operation referred to in Article 7;
   n) "taxable person" means any natural person or entity referred to in Article 4;
   o) "transfer of goods" means the transfers listed in Article 6;
   p) "transfer of goods free of charge" means a transfer not subject to any consideration, whether immediately due or payable, made in cash or in kind;
   q) "market value" means the total amount which the purchaser of goods or services would have to pay, under conditions of free competition, to an independent supplier with an equivalent market position, at the time and place where the transaction takes place or at the time and place closest to it, and at the same stage of marketing at which the supply of goods or services takes place;
   r) "turnover" means the value, excluding tax, of production, trade or service activities conducted by the taxable person.
2. In all matters not specifically provided for in this law, the provisions of the Tax Law shall apply in the alternative.

Chapter II
Incidence

Article 4
Taxable person

1. The following are considered taxable persons:
   a) Any natural person or entity who, being resident or having a permanent establishment in national territory, independently conducts business activities, under the terms defined in [article 54] of the Tax Law; e,
   b) Any natural person or entity who, being a non-resident and not having a permanent establishment in national territory, conducts any taxable transaction under the terms of article 5.

2. Without prejudice to the provisions of the previous paragraph, intermediaries who, acting in the name and on behalf of a non-resident taxable person without a permanent establishment in national territory, conduct any taxable transaction under the terms of Article 5, shall also be considered taxable persons.

3. Natural persons bound by an employment contract are not considered taxable persons in respect of work provided under that contract.

Article 5
Taxable transactions

1. Are subject to tax:
   a) Transfers of goods and the supply of services for consideration within national territory;
   b) Imports of goods.

2. The scope of the previous paragraph excludes the transfer of goods, supply of services and import of goods conducted in the exclusive economic zone and continental shelf, when the exclusive activity of the purchaser consists of the exploration and extraction of oil.

Article 6
Transfers of goods

1 In general, the transfer of property is considered to be the onerous transfer of tangible goods in a manner corresponding to the exercise of the right of ownership.

2. The following are also considered transfers of goods:
   a) The material delivery of goods in execution of a lease contract with a transfer of ownership clause, binding on both parties;

b) The material delivery of goods resulting from the execution of a purchase and sale contract, where the reservation of ownership is provided for until the total or partial payment of the price;
c) Failure to return goods sent on consignment within one year of delivery to the consignee;
d) The permanent use of the organisation's assets for the personal use of its members or employees or, in general, for purposes other than those of the organisation, as well as their free transfer, when there has been a total or partial deduction of tax in relation to these assets or their constituent elements.

3. The permanent reallocation of the organisation's assets in the event of the cessation of its activity, under the terms of Article 26(5), shall be deemed to be included in subparagraph d) of the previous paragraph.

Article 7
Provision of services

1. In general, the supply of services is considered any onerous transaction that does not constitute the transfer or import of goods.

2. Services are also considered to be provided:
   a) The provision of services free of charge by the organisation itself for the particular needs of its members or employees or, in general, for purposes unrelated to the organisation;
   b) The transfer of goods that is ancillary to the provision of services.

Article 8
Imports of goods

1. In general, the importation of goods is considered to be the introduction into free circulation, in national territory, of goods from abroad, under the terms defined in customs legislation.

2. The definitive transfer to Timor-Leste of goods from the exclusive economic zone and the continental shelf, including the Former Joint Petroleum Development Area, is also considered to be the importation of goods, when their entry into that zone has not been subject to taxation under the terms of Article 5(2).

Chapter III
Localisation of operations

Article 9
Transfers of goods

1 When the goods are neither dispatched nor transported, the location of the transaction shall be deemed to be where the goods are located at the time of delivery.

2 When goods are dispatched or transported by the supplier, the purchaser or a third party, the location of the transaction is deemed to be where the goods are located when dispatch or transport to the purchaser begins.

3 In the case of the supply of electricity, natural gas, heat, cold and the like through a distribution network, the location of the transaction is deemed to be where the purchaser actually uses and consumes the goods.

Article 10
Provision of services

1 Where the customer is not a taxable person, the location of the supply of services shall be deemed to be the place where the supplier has established his business or has a fixed establishment from which the services are supplied or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides.

2 Where the customer is a taxable person, the location of the supply of services shall be deemed to be the place where the customer has established his business or has a fixed establishment from which the services are acquired or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides.

3 Notwithstanding the provisions of the preceding paragraphs, they are always considered to have taken place in national territory:
a) Services rendered in connection with real estate located in national territory, including services to prepare or coordinate the execution of real estate work and services rendered by real estate experts and agents;
b) Work conducted on tangible movable property and appraisals relating to it, conducted wholly or mainly in Portugal;
c) c)The provision of artistic, scientific, sporting, recreational, educational, and similar services, including those of the organisers of these activities and the provision of services ancillary to them, which take place in national territory;
d) The supply of accommodation services, in hotels and similar establishments, and catering services, which take place in national territory;
e) e) The provision of transport services for goods and persons, when the transport begins in national territory;
f) f) Leasing of motor vehicles, boats, helicopters, aeroplanes, or any other means of transport, when these are placed at the disposal of the recipient in national territory.

4 Notwithstanding the provisions of the preceding paragraphs, where the supplier of services is a non-resident taxable person without a fixed establishment in national territory, the location of the supply of services listed below shall be deemed to be the place where the purchaser has established his business or has a fixed establishment from which the service is acquired or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides:

a. Telecommunications services;
b. Broadcasting and television services;
c. Electronically supplied services, in particular those referred to in Annex I;
d. Insurance and financial services.

Chapter IV
Taxable event and tax liability

Article 11
Taxable event and tax liability

1. Subject to the provisions of the following article, the tax is due and becomes payable:
   a) In transfers of goods, when the goods are placed at the disposal of the purchaser;
   b) In the case of the supply of services, at the time of their realisation;
   c) For imports, at the time of their release for free circulation in national territory, under the terms defined in customs legislation.

2. For the purposes of point, a) of the previous paragraph, the goods shall be deemed to have been placed at the purchaser's disposal:
   a) At the time transport begins, if the transfer of goods involves transport conducted by the supplier or by a third party;
   b) At the time the installation or assembly is completed, if the transfer of the goods implies an obligation to install or assemble on the part of the supplier.

3. In the case of the continuous supply of goods and services, resulting from contracts that give rise to successive payments, the goods are deemed to have been made available and the services are deemed to have been supplied at the end of the period to which each payment refers, and the tax is due and payable for the respective amount.

4. In the case of the supply of goods and services referred to in Article 6(2)(d) and Article 7(2), respectively, tax is due and payable at the time when the supply of goods or services referred to therein takes place.

5. In the case referred to in Article 6(2)(c), the tax is due and payable at the end of the period referred to therein.

Article 12
Chargeability of tax in the event of the issue or non-issue of an invoice

Without prejudice to the provisions of the previous paragraph, the tax is always due and payable:
   a) When an invoice is issued, even if this is before the taxable transactions have taken place;

b) On the deadline for issuing an invoice, it has not been issued on time, under the terms of [article 57(4)] of the Tax Law.

Chapter V
Taxable value

Article 13
Internal operations

1 Without prejudice to the provisions of the following paragraph, the taxable value of the supply of goods and services is the value of the consideration obtained or to be obtained from the purchaser, the recipient or a third party.

2 In the case of the following transfers of goods and supplies of services, the taxable amount is:
   a) For the operations referred to in Article 6(2)(c), the value shown on the invoice;
   b) For the operations referred to in Article 6(2)(d), the purchase price or, failing that, the cost price, reported at the time the operations were conducted;
   c) For the operations referred to in Article 7(2)(a), the normal value of the service.

3 In cases where the consideration is not defined, in whole or in part, in cash, the taxable amount will be the amount received or receivable in cash plus the market value of the goods or services given in exchange.

4 The taxable amount referred to in the previous paragraphs includes consumption taxes, duties, fees, and other charges, with the exception of value-added tax itself.

5 Discounts, rebates, or bonuses granted shall be excluded from the taxable amount referred to in the preceding paragraphs.

Article 14
Administrative changes to the taxable value in domestic transactions

The tax administration corrects or indirectly determines the taxable value in domestic transactions, under the terms of [article 32] of the Tax Law, when it finds a clear discrepancy between the declared taxable value and the economic value of the goods or services in question, or when, in general, it is not possible to directly and accurately verify and quantify the elements indispensable for the correct determination of those values.

Article 15
Imports

The taxable value of imported goods is their customs value, determined in accordance with customs legislation, plus customs import duties, excise duty and any other taxes or charges actually borne on importation, with the exception of value added tax itself.

Chapter VI
Fees

Article 16
General rate

The tax rate shall be [5] %, without prejudice to the provisions of the following article.

Article 17
Tax rate on exports and similar transactions

The tax rate is 0% on the following transactions:

a) Transfers of goods dispatched or transported abroad by the seller or by a third party on his behalf;
b) Transfers of goods dispatched or transported to the exclusive economic zone and continental shelf, including the Former Joint Petroleum Development Area, when the exclusive activity of the purchaser consists of the exploration and extraction of petroleum.

Chapter VII
Exemptions

Article 18
Exemptions for internal operations

They must be exempt from the tax:

a) Financial intermediation operations, namely those listed in Annex II, but with the exception of those in which a specific fee, commission or consideration is charged for the service;
b) The acquisition of rights in rem over immovable property;
c) Transfers of goods that are under a custom's suspensive procedure, for as long as they remain so, and without prejudice to the respective taxation at the time of release for free circulation;
d) Transactions exempt from taxation under the terms of an agreement binding the State of Timor-Leste internationally.

Article 19
Exemptions on imports

They must be exempt from tax:

a. Imports of goods exempt from customs import duties under the terms of the Tax Law;

b. Imports exempt from taxation under the terms of an agreement binding the State of Timor-Leste internationally.

Chapter VIII
Right to deduct

Article 20
Birth and scope of the right to deduct

1. The right to deduct arises when the deductible tax becomes chargeable, in accordance with the provisions of Articles 11 and 12.

2. The taxable person is entitled to deduct, under the terms of the following articles:
   a) Tax due or paid on the acquisition of goods and services from other taxable persons;
   b) The tax paid on the import of goods;
   c) Tax paid under Article 24(2) as the recipient of taxable transactions conducted in national territory by non-resident taxable persons without a permanent establishment in national territory.'

3. Notwithstanding the provisions of the previous paragraph, only the tax levied on goods or services acquired, imported, or used by the taxable person to conduct the following transactions may be deducted:
   a) Non-exempt taxable transactions;
   b) Transactions conducted abroad that would be taxable if they were conducted in Portugal.

4. Notwithstanding the provisions of no. 2, no tax may be deducted if it results from a simulated transaction or if the price on the invoice is simulated.

5. Notwithstanding the provisions of paragraph 2, the right to deduct shall be excluded when the tax authorities find that, through the transaction invoked to justify the right in question, the taxable person was participating in tax evasion or avoidance.

Article 21
Exercising the right to deduct

1) The amount of tax deductible will be subtracted from the amount of tax due for the taxable transactions conducted in each tax period.

2) Only tax mentioned on invoices drawn up in legal form and held by the tax-able person is eligible for deduction.

3) The deduction must be made in the tax return for the period in which the invoices referred to in the previous paragraph were received.

4) Whenever the tax deduction exceeds the amount due for taxable transactions in the corresponding period, the excess will be deducted in subsequent tax periods.

5) If, six months after the period in which the excess began, there is still a credit in favour of the taxable person, he may, if he does not wish to maintain, in whole or in part, the procedure established in the previous paragraph, request the corresponding refund.

6. Irrespective of the deadline referred to in the previous paragraph, the taxable person has the right to request immediate reimbursement when:
   a) If you cease your activity;
   b) The tax credit situation results from the realisation of transactions subject to tax at the rate of 0%, under the terms of article 17, when these constitute more than 50% of the total turnover conducted by the taxable person during the previous twelve months.

6. Refunds, when due, must be made by the tax authorities by the end of the third month following the submission of the respective request, after which overdue payment interest will be added to the amount to be refunded.

8. The interest on overdue payment referred to in the previous paragraph corresponds to the same monthly rate provided for non-payment of tax by taxpayers, and is calculated from the end of the deadline for reimbursement until the date of issue of the respective payment order.

Article 22
Partial deduction

1. When, in the course of carrying out the activity, transactions that confer the right to a deduction and transactions that do not confer this right are carried out together, under the terms of article 20, the tax borne on the acquisitions will only be deductible in the percentage corresponding to the annual amount of the transactions carried out that confer the right to a deduction.

2. The percentage deduction referred to in the previous paragraph results from a fraction comprising the following amounts:
   a) in the numerator, the annual turnover, excluding tax, of the activities giving rise to a deduction under Article 20;
   b) In the denominator, the annual turnover, excluding tax, of all the activities conducted by the taxable person.

3. The deduction percentage, provisionally calculated on the basis of the previous year's turnover, will be corrected in accordance with the figures for the year to which it relates, giving rise to the corresponding regularisation of the deductions made, which must be included in the declaration for the last period of the year to which it relates.

4. Taxable persons who start their business or substantially change it may deduct tax on the basis of an estimated provisional percentage, to be entered in the register referred to in Article 26, which must be corrected in accordance with the previous paragraph.

Chapter IX
Obligations of taxable persons

Article 23
Tax debtors

1. Tax is payable by taxable persons who conduct the supply of goods or services, without prejudice to the provisions of article 28.

2. Notwithstanding the provisions of the previous paragraph, the tax is payable by the purchaser when the following cumulative conditions are met:
   a) The supply of services is localised in national territory, in accordance with Article 10(2) to (4);
   b) The supplier of the services is a non-resident taxable person without a permanent establishment in national territory; and,
   c) The purchaser is a taxable person not covered by the special exemption scheme provided for in Article 36.

3. The tax due on the import of goods is due by the importer of the goods, as defined in customs legislation.

Article 24
Tax delivery

1. Taxable persons are obliged to submit to the tax authorities, at the same time as the declaration referred to in Article 30, the amount of tax assessed in accordance with the following paragraph.

2. The amount of tax to be paid is the total amount of tax payable minus the total amount of tax deductible.

3. Whenever the tax is assessed ex officio, under the terms of articles 41 and 42, the taxable person will be notified immediately to make payment by the end of the month following the date of notification.

4. Notwithstanding the provisions of the preceding paragraphs, the tax due on the importation of goods shall be paid, together with any other customs duties and taxes due, at the time of their release for free circulation, in accordance with customs legislation.

Article 25
Obligations of resident and equivalent taxable persons

1. The taxable persons referred to in Article 4(1)(a) are obliged to:
   a. Make the relevant register and keep it up to date, in accordance with the following article;
   b. Issue an invoice for each transfer of goods or provision of services, under the terms of articles 27 to 29;
   c. Submit a monthly declaration regarding the transactions conducted in the course of their activity during the previous month, indicating the tax due or the existing credit, and the elements that served as the basis for its calculation, under the terms of article 30;
   d. Have adequate accounts for the assessment and supervision of the tax, under the terms of articles 31 to 35.

2. The obligation to issue an invoice, as provided for in point b) of the previous paragraph, also applies when the taxable value of a transaction or the corresponding tax are altered for any reason, including inaccuracy.

3. The obligation to submit a periodic declaration, as provided for in paragraph 1(c), continues even if there are no taxable transactions in the corresponding period.

4. Transactions subject to tax at the rate of 0 per cent under Article 17 must be evidenced, as the case may be, by the appropriate customs documents or, where there is no intervention by the customs services, by declarations issued by the purchaser of the goods or user of the services, indicating the destination to be given to them

5. Taxable persons who carry out exclusively tax-exempt transactions, or who are covered by the special exemption scheme provided for in Article 36, are exempt from the obligations referred to in points b), c) and d) of paragraph 1, without prejudice to compliance with the invoicing and accounting obligations provided for in the Tax Law.

Article 26
Registration of the taxable person

1. Before conducting any taxable transactions, taxable persons must register as such with the tax authorities by means of the declaration of commencement of activity provided for in [article 58(1)] of the Tax Law.

2. Whenever there is a change in any of the elements listed in the register, taxable persons must notify the tax authorities of this fact by means of the declaration of changes in activity provided for in [Article 58(2)] of the Tax Law.

3. Taxable persons who, while included in the normal tax regime, come to fulfil the requirements set out in Article 36(1) and wish to apply the special exemption regime must, under the terms of Article

37, amend their registration by means of the declaration of changes in activity referred to in the previous paragraph.

4. Taxable persons who, under the terms of article 38, wish to waive the special exemption regime and opt for the normal application of tax to their taxable transactions, must expressly do so in the respective register, by means of the declaration of commencement of activity or the declaration of changes in activity referred to in paragraphs 1 and 2 of this article, as the case may be.

5. The closure of a taxable person's registration is affected by means of the declaration of cessation of activity provided for in [Article 58(3)] of the Tax Law.

6. The inaccuracy or falsity of the information declared in the register shall constitute grounds for non-acceptance of the registration, its amendment, or its cancellation.

7. The tax authorities will correct or delete the taxable person's registration of their own motion if the taxable person fails to do so within 10 days of being called upon to do so.

Article 27
Issuing invoices

1. The provisions of [article 57] of the Tax Law shall apply to taxable persons.

2. Taxable persons, with the exception of taxable persons covered by the special exemption scheme provided for in articles 36 to 40, issue their invoices using a computer invoicing programme or equipment duly authorised by the tax authorities.

3. Without prejudice to the provisions of [article 57(7)] of the Tax Law, and article 29 of this law, invoices which do not include the tax identification numbers of the taxable person and the purchaser do not give rise to the right to deduct.

Article 28
Repercussion of the tax

1 The amount of tax assessed must be added to the invoice value for the purposes of demanding it from the purchasers of the goods or services.

2 For the purposes of the previous paragraph, in transactions in which the issue of an invoice is waived, under the terms of the following article, the tax shall be included in the price, unless the supplier of the goods or the service provider is covered by the special exemption regime provided for in article 36.

Article 29
No invoicing

1. Exemption from the invoicing obligation provided for in [Article 57(8) of the Tax Law] applies to the following transactions:
   a) Transfers of goods made by travelling salesmen;
   b) Transmissions of goods made through automatic distribution devices;
   c) c)Services where it is customary to issue a receipt, ticket, ticket, or other printed document as proof of payment.

2. The tax authorities may, in cases where invoicing is waived under the terms of the previous paragraph, require the presentation of another document suitable for proving the operation conducted.

Article 30
Periodic declaration

Taxable persons are obliged to send the periodic declaration provided for in Article 25(1)(c) by the last day of the month following the month to which the transactions covered by it relate.

Article 31
Carrying out the accounts

1. The provisions of [article 56] of the Tax Law shall apply to taxable persons.
2. The accounts must be organised in such a way as to enable clear and unambiguous knowledge of the elements necessary for calculating the tax, as well as to allow its control, including all the data necessary for completing the periodic tax return.

3. For the purposes of the previous paragraph, they must be registered:
   a) Taxable transactions conducted by the taxable person under the terms of Article 5(1)(a);
   b) Taxable transactions conducted by the taxable person under the terms of Article 5(1)(b);
   c) Taxable transactions under the terms of Article 5(1)(a) made to the taxab le person.

4. The operations mentioned in point a) of the previous paragraph must be recorded in such a way as to show:
   a) The value of taxable transactions, net of tax;
   b) The value of taxable transactions exempted under Article 18;
   c) The value of taxable transactions subject to the 0% tax rate, under the terms of Article 17;
   d) The amount of tax assessed.

5. The operations mentioned in paragraphs 3 (b) and 3(c) must be recorded in such a way as to show:
   a. The value of transactions for which tax is deductible under Article 20, net of tax;

b. The amount of tax deductible.

Article 32
Recording active operations

The taxable transactions referred to in paragraph 3 a) of the previous article must be registered after the corresponding invoices have been issued, and no later than the deadline for submitting the returns referred to in article 30.

Article 33
Recording passive operations

The taxable transactions referred to in Article 31(3)(b) and (c) must be registered once the corresponding invoices have been received, and no later than the deadline for submitting the returns referred to in Article 30.

Article 34
Tax registration included in the price

In cases where invoicing or registration is processed using tax-inclusive values, under the terms of the previous articles, the corresponding tax base will be obtained by dividing those values by the sum of 1 and the general tax rate provided for in article 16, and rounding the result down or up to the nearest unit.

Article 35
Tax rectifications

1. The provisions of articles 27 to 29 must be observed whenever, after the invoice has been issued, the taxable value of a transaction or the respective tax is corrected for any reason.

2. If, after making the registration referred to in article 32, the transaction is cancelled or its taxable value reduced, the supplier of the goods or service provider may deduct the corresponding tax until the end of the tax period following that in which the circumstances that led to the cancellation of the assessment or the reduction of its taxable value occurred.

3. In the case of inaccurate invoices that have already given rise to the registration referred to in article 32, rectification is compulsory when there is underpaid tax, and may be carried out without any penalty until the end of the tax period following that to which the invoice to be rectified relates, and is optional when there is overpaid tax, but may only be carried out within one year.

4. The purchaser of the goods or the recipient of the service who is a taxable person shall, if he has already registered under Article 33 a transaction in respect of which his supplier has cancelled or reduced the taxable amount under paragraph 2, correct the deduction made by the end of the tax period following receipt of the corrective document.

5. Correction of clerical or calculation errors in the register referred to in articles 31 to 34 and in the declarations referred to in article 30 is compulsory when there is under-delivered tax, and may be carried out without any penalty until the end of the following period, and is optional when there is over-delivered tax, but may only be carried out within one year.

Chapter X
Special exemption scheme

Article 36
Scope of application

1. Taxpayers with a gross annual turnover of less than [150,000.00] US dollars and fewer than fifteen employees are exempt from the tax.

2. The assumptions referred to in the previous paragraph are verified at the end of the previous tax year or, in the case of the first tax year in which the activity is conducted, by means of the estimate contained in the tax registration made by the taxable person under the terms of Article 26(1).

3. Taxable persons who are exempt from tax under the terms of paragraph 1 are excluded from the right of deduction provided for in articles 20 to 23.

Article 37
Transition from the normal regime to the special exemption regime

1 If taxable persons included in the normal tax application regime who now fulfil the requirements set out in paragraph 1 of the previous article wish to apply the special exemption regime, they must change their registration under the terms of paragraph 3 of article 26.

2. The amendment to the register referred to in the previous paragraph must be sent to the tax authorities during the month of January of the year following that in which the conditions referred to therein occurred.

3. Taxpayers who were previously covered by the normal regime but make use of the option provided for in paragraph 1 must regularise the tax deducted and relating to remaining inventories at the end of the year, in accordance with article 35, and these regularisations must be included in the return for the last tax period.

Article 38
Waiver of the special exemption regime

1. Taxable persons who may benefit from an exemption from tax under the terms of Article 36(1) may waive this exemption and opt for the normal application of tax to their taxable transactions.

2. The right of option shall be exercised in the taxable person's tax file, in accordance with Article 26(4).

3. The tax administration may refuse to exercise the right of option within 30 days of submitting the amendment to the register if the taxable person's tax situation has not been regularised or if there is evidence of a previous failure to comply with declaratory obligations or obligations relating to the execution, organisation and filing of accounts.

4. Having exercised the right of option under the terms of the previous paragraphs, the taxable person is obliged to remain in the system they opted for a period of at least five years, without prejudice to the provisions of Article 40.

5. At the end of the period referred to in the previous paragraph, a taxable person who, having previously exercised the right of option, wishes to return to the special exemption regime, must submit an amendment to the register, in accordance with Article 26(2), which will take effect on 1 January of the following year.

6. In cases of change from the special exemption regime to the normal taxation regime, the tax authorities may authorise the taxable person to deduct, in the first tax period, the tax contained in the inventories remaining at the end of the previous year.

Article 39
Reporting and invoicing obligations

1. Taxpayers exempt under Article 36(1) are exempt from the obligations set out in this law, with the exception of the following:
   a) The realisation of the respective register, and its closure, in accordance with article 26;
   b) The issuing of invoices, under the terms of articles 27 to 29;
   c) Keeping the accounts and filing and preserving the accounting records and respective supporting documents, under the terms of articles 31 to 35.

2. Taxpayers who are exempt under the terms of Article 36(1) must include the words "VAT - Special exemption scheme" on the invoices they issue.

Article 40
Exit from the special exemption regime

1. When the conditions for the application of the scheme referred to in Article 36(1) cease to apply, the taxable person is obliged to change the respective registration, under the terms of Article 26(2).

2. Whenever the tax administration has indications that an exempt taxable person has exceeded the turnover limit or the number of employees under the special exemption scheme in a given year, it will notify them to amend their registration.

3. Tax will be due on taxable transactions conducted by taxable persons from the month following the month in which the conditions for leaving the special exemption regime are verified.

Chapter XI
Non-compliance with tax obligations

Article 41
Failure to submit a periodic declaration

1. If a taxable person fails to submit the periodic declaration to which he is obliged, under the terms of article 30, within the respective legal deadline, the tax authorities must assess the tax of their own motion.

2. The assessment will be made on the basis of the declarations of previous periods or on the basis of other elements available to the tax authorities, namely those relating to income tax.

3. The tax assessed in accordance with paragraph 1 shall be paid within the time limit indicated in Article 24(3).

Article 42
Omissions or inaccuracies

1. The tax authorities will rectify the taxable person's periodic tax return when they consider that it contains a lower tax or a higher deduction than is due, and will also pay the difference.

2. The rectification provided for in the previous paragraph may result directly from the content of the declaration, from the comparison with declarations relating to previous periods or from the comparison with other elements available to the tax authorities, namely those relating to income tax.

3. The rectification provided for in no. 1 may also be conducted as part of an internal or external tax inspection, which includes inspection visits to the taxable person's premises, an examination of the taxable person's records or a check of the establishment's physical inventories.

4. The tax assessed in accordance with paragraph 1 shall be paid within the time limit indicated in Article 24(3).

Article 43
Failure to submit or pay the tax within the legal deadline

Failure to deliver or pay the tax within the legal deadline may result in the suspension of the taxable person's status by the tax authorities until that delivery or payment is made, without prejudice to the assessment of interest and penalties.

Article 44
Joint and several liability of third parties

1. The taxable person acquiring the goods or services is jointly and severally liable with the supplier for payment of the tax when the invoice, the issue of which is compulsory under the terms of Article 27, has not been drawn up or contains inaccurate information as to the name or address of the parties involved, the nature or quantity of the goods or services supplied, the price or the amount of tax due.

2. The taxable person acquiring or receiving the goods who proves that he has paid all or part of the tax due to his supplier, who has been duly identified, is released from the joint and several liability provided for in the previous paragraph for the amount corresponding to the payment made, except in the case of bad faith.

Chapter XII
Final provisions

Article 45
1. Tax succession

1. The legal and contractual provisions in force regarding sales tax and service tax shall be understood to apply to the value added tax approved by this law.

2. Without prejudice to the provisions of the previous paragraph, sales tax, and service tax, even if assessed after the entry into force of this law, are not, under any circumstances, deductible from value added tax.

Article 46
Entry into force

This law comes into force on ……. 2025.

Approved on....

The President of the National Parliament,

Promulgated in.....

To be published on....

The President of the Republic,

Annex I
(referred to in Article 10(4)(c))

Indicative list of services provided electronically

1. Supply of computer sites, web page hosting, remote maintenance of programmes and equipment.
2. Supply and updating of computer programmes.
3. granting, for consideration, the right to put goods or services up for sale on an Internet site operating as an online marketplace.
4. Providing images, texts, and information, and making databases available.
5. Provision of music, films, and games, including games of chance and gambling, and of political, cultural, artistic, sporting, scientific or leisure broadcasts or events.
6. Provision of distance learning services.

Annex II
(referred to in Article 18(a))

Indicative list of exempt financial intermediation operations

1 Credit granting and the management of credit guarantees.
2. currency exchange and other operations relating to currency, with the exception of the transmission of coins and collector's notes.
3. operations relating to financial deposits and account management.
4 The transfer of financial securities.
5 Management of common investment funds.

Approved by the Council of Ministers in 2024.

The Prime Minister,

_____
Kay Rala Xanana Gusmão

The Minister of Finance,

_____
Santina Viegas Cardoso