Costa Rica
VAT implementation: First draft regulations released

What’s new?
On 29 January 2019, Costa Rica’s Ministry of Finance released the first version of draft regulations relating to the implementation of a Value Added Tax (VAT) regime that will replace the General Sales Tax (GST) on 1 July 2019.

The draft regulations include provisions on the tax collection model that would be applicable to cross-border supplies of digital services provided by nonresident businesses.

The introduction of VAT was included in the Public Finance Strengthening Project, published in Costa Rica’s official gazette.
on 5 December 2018 (see the article on tax@hand for a discussion of the other changes in the law).

Scope of VAT

The scope of VAT will be broader than the scope of GST, i.e. VAT will be levied on the sale and import of goods, and the supply of services in Costa Rica, including digital services supplied from abroad i.e. services that are provided over the internet or via other digital platforms, where the services are used in Costa Rica.

The introduction of VAT will represent a substantial change since very few services currently are subject to GST.

Collection of VAT on services from abroad

Services other than digital services

When a nonresident service provider supplies services to a business customer in Costa Rica (i.e. business-to-business or B2B supplies), the recipient will have to self-assess VAT via the reverse charge mechanism.

When a nonresident service provider supplies services (that are not considered “digital services”) to private customers in Costa Rica (i.e. business-to-consumer or B2C supplies), these services will fall outside the scope of Costa Rican VAT and the nonresident supplier should not be required to register for VAT purposes.

Specific regime for cross-border digital services

Services provided to business and private customers in Costa Rica over the internet or other digital platform fall within the scope of Costa Rican VAT. The draft regulations would establish a “financial intermediary” collection model, under which the credit/debit card issuers would be appointed as withholding agents for the purchase of cross-border digital services over the internet and be responsible for collecting and paying the VAT due on the services to the Costa Rica tax authorities.

It is expected that this VAT collection regime would apply to digital services supplied by nonresident suppliers to both business and private customers in Costa Rica.

VAT would be computed and collected by the financial institution on top of the service price charged by the supplier.

Notably, nonresident sellers would have the possibility to opt for local VAT registration if the value of B2B and B2C annual supplies to Costa Rican customers exceeds “30 base salaries” (Colones 13,386,000 or approximately USD 21,625).

It is our understanding that once a nonresident supplier opts to register for VAT, the supplier would be required to collect VAT on both B2B and B2C supplies of digital services.
However, an option made by nonresident digital services supplier to register for VAT in Costa Rica should not give rise to a permanent establishment in the country or associated corporate income tax requirements.

**VAT rates**

The standard VAT rate will be 13%, with three reduced rates of 4%, 2% and 1%. The 4% reduced rate will apply to the purchase of air tickets for flights into and out of Costa Rica, and to health care services. The 2% rate will apply to:

- Medicine and raw materials and equipment required to produce medicine;
- Personal insurance; and
- Purchase and sale of goods/services by higher education government agencies and departments.

The 1% rate will apply to:

- Supplies of food staples that are included on a list of items that are considered essential for a traditional household; and
- Supplies of veterinary and agricultural products.

The following goods and services will be exempt from VAT (non-exhaustive list):

- Leasing of residential real estate;
- Internet in residential services;
- Residential consumption of electricity and water;
- Purchase of goods and services from free trade zones;
- Sales of goods and services to individuals or companies outside Costa Rica; and
- Books (except for e-books, which would be subject to the standard VAT rate of 13%).

**VAT credits**

A taxpayer will be entitled to recover VAT paid on the acquisition of goods and services linked to taxable transactions. The taxpayer will be able to deduct VAT in its VAT returns, with any credit balance available to be carried forward for the next four years. If the taxpayer anticipates that it will not be able to absorb the VAT credits in three years, it may request a VAT refund.

**Next steps**

Certain aspects of the VAT regime still need to be clarified, such as supplies falling within the scope of VAT, which digital services would fall within the financial institution VAT collection regime, VAT invoicing obligations, etc. Additional details and subsequent versions of the (draft) implementing regulations are expected to be issued in the coming months, which should provide further information. Potentially affected taxpayers
should be aware that the regulations still are subject to amendments and, therefore, should monitor developments carefully.

How Deloitte can help?
Deloitte can help businesses prepare for these changes and to comply with the future VAT requirements in Costa Rica.

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