

## Foreign Exchange Payments for Goods and Services

### Introduction

The Government of Nepal (“GON”) in its Monetary Policy for the Fiscal Year 2077-2078 (2020-2021 A.D.) made a commitment that arrangements shall be made for granting exchange control facility to Nepali individuals and entities in order to effectuate online purchase of goods and services from abroad. This initiation was made in light of the increasing number of foreign exchange payments being made by Nepali individuals and entities through informal channels, especially for online advertisements on various social media. Payments made through such informal channels were perceived to increasingly give rise to instances of money laundering, loss of revenue to GON, and misuse of foreign exchange. Nepal Rastra Bank (“NRB”), the central bank of Nepal, issued a Notice in this regard on January 31, 2020.

In light of the commitment made in the Monetary Policy, NRB recently released a Consultation Paper to invite recommendations from stakeholders regarding the draft of a Circular/Directive to be formulated for this purpose.

### Current Provisions Relating to Foreign Exchange Payments for Goods and Services

Currently, exchange control regulations provide limited avenues to Nepali individuals and entities to make foreign exchange payments for purchasing services from abroad.

Section 2(c)(7) of Circular No. 15/2076 of Unified Foreign Exchange Management Circular 2076 (“UFXMC”) provides that Nepali individuals who maintain a bank account in convertible foreign currency with Nepali commercial banks and has obtained credit or debit cards using the accounts, may purchase services from abroad up to US\$2,000 (to be understood annually) using convertible foreign currency from the accounts.

Similarly, Section 9 of Circular No. 07/2076 of UFXMC provides that commercial banks may provide exchange control facility to its customers for up to US\$3,000 (to be understood annually) for purchase of services from abroad; and may further

provide exchange control facility for up to US\$10,000 on the recommendation of the concerned regulatory agency of the customer, for the purchase of services from abroad.

Purchase of goods from abroad must necessarily take place through other modes of banking channels, i.e., Letter of Credit or Trust Receipts or other similar transactions. Hence, Nepali individuals who are not engaged in import and trading business are generally not eligible to purchase goods from abroad directly and must therefore approach domestic retailers.

### Proposed Provisions for Providing Exchange Control Facility

NRB in the Consultation Paper has proposed the following provisions:

- Commercial banks may issue prepaid cards denominated in US Dollars to its customers by granting exchange control facility against Nepali Rupees (“NPR”) linked to their accounts. KYC formalities and Permanent Account Number (“PAN”) registrations shall be mandatory while issuing the prepaid cards.
- Commercial banks shall be allowed to deposit up to US\$500 or equivalent foreign exchange in the prepaid cards of their customers. Commercial banks are required to collect and deposit advance tax applicable for purchase of services from abroad while depositing funds in the prepaid cards.
- If a customer does not use the full limit of US\$500 in a year, commercial banks shall be allowed to top up the portion of used amount into the cards, however, not exceeding the annual limit.
- Customers may use the limit of US\$500 or equivalent foreign currency in a year without limit on the number of transactions.
- Customers may use the prepaid cards to purchase non-prohibited services from abroad, online.

- Commercial banks shall be allowed to provide additional exchange control facility into the prepaid cards on the basis of necessity and justification to those customers who are able to demonstrate through documentary evidence that she/he was able to earn an income in foreign exchange at least double the amount of foreign exchange spent using the prepaid cards.
- Commercial banks must obtain a self-declaration from each customer seeking to obtain a prepaid card stating that she/he is not obtaining such facility from any other commercial bank. A customer, who uses prepaid cards facility from more than one bank shall be subject to prosecution under Foreign Exchange (Regulation) Act 2019 (1962 AD).
- Commercial banks shall not deposit foreign exchange in the name of another customer or in the prepaid cards belonging to others while granting the exchange control facility to a customer.
- Commercial banks must submit reports to NRB on a monthly basis describing details of prepaid cards issued by them as well as details of amounts spent by the customers from the prepaid cards issued.

### Preliminary Observations and Comments

The proposed Circular/Directive aims to allow Nepali individuals and entities to avail limited exchange control facility to purchase goods and services online directly from foreign vendors. As of now, Nepali entities either require a bank account in convertible currency or need to open a Letter of Credit or a Trust Receipt to avail exchange control facilities through formal and highly regulated banking channels. By allowing prepaid cards in foreign exchange, purchase of goods and services online from foreign vendors will undoubtedly become easier and foreign markets would be more accessible. The proposed exchange control facility will also reduce the

practice of using informal channels for payment of foreign exchange abroad. Apparently, online marketplaces and social media companies will be mostly benefited from this arrangement once enforced as law.

The threshold limit of US\$500 per year to those individuals and entities who do not have an account in convertible foreign currency may seem to be appropriate from an exchange control perspective, however, this may not seem practical to those individuals and entities who already maintain accounts in convertible foreign currency. It may be more practical as well as appropriate to allow account holders to link this facility to their credit/debit cards which are linked to their convertible foreign currency accounts and permit them to use the fund to the extent covered by their convertible foreign currency accounts in order to avoid obtaining additional exchange control approvals. Similarly, foreign exchange issued to Nepali citizens for international travel should also be combined in the debit cards and allow them to use the fund to the extent covered by their convertible foreign currency accounts in order to have a single and efficient foreign exchange payment method. This will not in any way burden national foreign exchange reserves.

The provision of deduction of advance tax prior to depositing foreign exchange into the prepaid cards requires more clarification. Since most online services require payments net of taxes, it would be appropriate to clarify that advance taxes shall be deducted from the customers' NPR account.

Further, advance tax is payable on import of services only and not on goods. Purchase of goods online will require a buyer to either clear the customs herself/himself or pay the seller in advance for the same. Provisions relating to deduction of advance tax neither clarify on how commercial banks will deposit advance tax on purchase of services nor provide a practical mechanism where advance tax is not applicable on purchase of goods from abroad.

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