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Nepal Rastra Bank issues circular for approval of capitalization of expenses incurred in a foreign country as a foreign investment in the foreign investment projects.

Nepal Rastra Bank, the Central Bank of Nepal ("**NRB**") has issued a circular on May 21, 2017 (2074/02/07) relating to capitalization of expenses incurred for the feasibility study, geographical exploration, survey or design of the project in a respective foreign country of a foreign investor for the projects under foreign investment (the "**Circular**"). Prior to the Circular, there was no legal mechanism to recognize expenses made by a foreign investor prior to establishment of a company in Nepal. With issuance of the Circular, the expenses incurred by a foreign investor can be capitalized subject to conditions as specified in the Circular. The Circular has limited capitalization of expenses in connection with feasibility study, geographical exploration, survey or design of the Project by providing certain conditions. These conditions are i) requirement for obtaining of government approval, ii) expenses to be incurred in jurisdiction of foreign investor iii) compliance with the policy, iv) obtaining of Board approval, and v) ensuring non abuse of the foreign currency.

1. Conditions for incurring expenses

1.1 Eligibility Criteria

- (a) . The Circular provides following project as eligible projects for capitalization of aforementioned expenses: (a) the projects listed as the national pride projects by the Government of Nepal (the "**GON**"), or (b) the projects to be carried out in Nepal subject to approval of Investment Board of Nepal (the "**IBN**") (collectively referred as the "**Projects**").
- (b) There is no specific guideline relating to prerequisites required for a project to be listed as the national pride project by GON. The GON on the basis of recommendation from National Planning Commission lists out the national pride projects. GON is in the process of framing the guidelines setting out the criteria to be listed as national pride projects. There are currently 21 projects which are designated as national pride projects (http://www.npc.gov.np/images/category/national_pride_2072_6_19_.pdf).
- (c) The projects under the mandate of IBN are specified under Section 9 of the Investment Board Act 2011. Some of the projects specified in Section 9 of the Investment Board Act includes, among others, investments in the following projects-(A) infrastructure projects such as fast track road, tunnel as prescribed by the GON, construction of international or regional airports or modernization and management of the existing airports, large bridges as prescribed by the GON, etc. (B) hydropower projects with installed capacity of 500 MW or more, (C) medical college and the hospitals or nursing homes with full modern facilities having more than 300 beds, (D)

construction of the special economic zone, export promotion or processing zone, special industrial zone or information technology park, (E) any infrastructure projects or service industry with fixed assets of Rs. 10,000,000,000 or project costs of more than Rs. 10,000,000,000, (F) any manufacturing industry with fixed assets of Rs. 10,000,000,000 or project costs of more than Rs. 10,000,000,000 (for foreign investment only), and (G) any other industry of similar nature as a priority sector industry as prescribed by the GON.

1.2 Scope

Expenses incurred for only feasibility study, geographical exploration, survey or designs in relation to the Projects can be capitalized pursuant to the Circular.

1.3 Foreign Investment Approval

Such expenses should be incurred by the foreign investor only after obtaining requisite approval for its investment in Nepal. This foreign investment approval should generally be obtained under Foreign Investment Technology Transfer Act 1992/Investment Board Act 2011 and Foreign Exchange Regulation Act 1962.

2. Conditions for capitalizing expenses

2.1 Requirement of audit

The audit should be conducted by a local auditor and internationally recognized auditor and approved or recognized by auditor general of concerned state/ country of the foreign investor.

2.2 Requirement of corporate decision

A corporate decision will be required for capitalization of expenses. In case of joint venture company with local partner, corporate decision of a local partner is required. However, in case of projects fully owned by foreign investor, the decision of Top Level Management (definition not provided in the Circular) of the foreign investor is required to capitalize the expenses.

3. Timing of Capitalization

The capitalization for the expenses and recording of such expenses as “foreign investment” can only be made after the commencement of the operation of the Project.

4. Additional conditions

4.1 Framing of Policy by the Concerned Authority

The policy setting out the standards and limitation on expenses incurred by the foreign investor is required to be framed by the concerned authority granting approval for the foreign investment. For example, Investment Board of Nepal is required to frame such policy in relation to the



projects falling under its mandate. It appears that such policy has also not been published by the concerned authority as of this date.

4.2 Recommendation from the Concerned Authority

The concerned authority granting approval for foreign investment is required to issue a recommendation letter to NRB stating that the expenses made in foreign country is reasonable and there has not been abuse of the foreign currency.

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