

# **CHAPTER – I**

## **INTRODUCTION**

### **1.1 General Background of the Study**

In the present day, a government has to spend a lot of money to fulfill their responsibility towards its people. The responsibility may be for development, health, education etc. The nation will be able to achieve social welfare if it has sufficient financial resources at its disposal. Government expenditure is increasing because of the demand of time, increase price and national income, increase in social progress and population etc. To meet the growing funds from internal as well as external sources.

External sources consists of foreign subsidy, foreign loan etc which is used for economic development, reconstruction, cover crises and productive use. That's why in this crises Nepal needing these kinds of sources to go up. But these kinds of sources are uncertain and inconvenient because they have to return after a certain due date. Continuous use of external sources of fund to raise necessary public fund is not good because it reduce the liquidity position of the government, increase one dependency upon other countries and increase the inflation (Lekhi, 2000). Thus it is better to mobilized internal or domestic sources for development activities.

In this modern age, a government entails a lot of revenues in order to influence the macro economic performance of the economy of fiscal policy to carry out the function of the government such as infrastructure reconstruction and redistribute resources among individuals or classes in the population. In this context, a tax is a significant and inseparable source of state revenue of the government. According to its nature it is most reliable certain, flexible and convenient to obtain the required amount. Therefore, the government of any country up holds the main priority in tax revenue. (K C, 2006)

Tax revenue and non-tax revenue comes under the internal sources. Non-tax revenue is conditional which includes grants, fees, fine and penalties, special assessment and gift etc. In Nepal around 20% of the revenue comes from these sources because these sources are inconvenient, uncertain and levied according to necessary of government. The other internal sources of the government revenue are the taxation. Custom duty, excise duty, value added, corporate and personal income tax are the example of the source of tax revenue. Nepal gets around 80% of the revenue from these sources. These sources are contributing in national capital formation, equal distribution of national income, and also occupy the most important place in government treasury. Because of the importance of the source in revenue mobilization of a country, some person likes to pay tax can be grouped into two categories which are,

Direct tax: Income tax, house tax, property tax, interest tax etc. These tax burdens cannot be shifted to other.

Indirect tax: Value added tax, export duty, excise duty, custom duty and entertainment tax are the example of indirect tax. Indirect tax is shift able partly or wholly to other.

Value added tax is a major component of indirect tax for resources mobilization to general public revenue. It is the tax imposed on value added by business firms on goods and services at the successive stages of production and distribution. Value addition on a commodity or service is simply the excess of sales value over business purchases by a business entity. During the successive stages of production and distribution processes, business enterprises add value to their purchase by processing or handling them by their own machinery, building or other capital goods. VAT was considered as one form of sales tax. It is the multiple sales tax which has grown as a heterogeneous or turnover tax and retail level sales tax. Thus, VAT is the multistage sales tax, which is lived

on the value added of business enterprises at different stages of production and form of old sales tax.

“Taxation, in the modern world has been taken as the best effective tool for raising the ratio of saving of the national income” (Pant, 1970). Taxes as major fiscal policy instrument and important government policy tools have an important role in increasing the capital formulation and achieving the high rate of economic growth without inflation. Increasing taxes may be directed to increase savings through the postponement of consumption. “Taxation may play a dual role in this regard one; taxation may be used to make the maximum volume of resource available to the public sector. Secondly, it may be used to promote useful investment in the private sector and to prevent the resource from being dissipated over speculative and unproductive investment as well as over lavish and luxurious consumption.” (Tripathy, 1985)

The concept of resource mobilization by increased taxation is not recently developed, it was widespread in early postwar in developing countries that increased taxation would result in the increased saving needed to finance the investment that is turn needed to produce the desired rate of economic growth. Such calculations called required rate of taxation were at one time almost mandatory in developing countries and are still by no means uncommon.

Under development, countries are served by indirect tax as their taxes have been designed so properly. Due to such poorly designed and their low revenue yield, they are unable to increase their productivity through capital formation. The low level of revenue mobilization creates the fiscal crisis under the revenue-expenditure gap. The use of resource without creating inflation finance. The tax reform efforts of under developing country during the last and present decades have established some new trends and directions. In this context, to solve the resource gap and as an instrument of resource mobilization

from private sector to public sector and to make the tax system more rational; there is a development a worldwide phenomenon of new tax system, i.e. Value Added Tax has been taken as broadly based low – rate taxes on domestic consumption and self- monitoring feature as well as having ability to raise revenue. It is also most improved forms of sales tax and revenue enhancement with neutrality and efficiency.

“The Value Added Tax is a tax imposed upon the value that the activity of a business firm adds to the goods and the services. It purchases from other firms that is upon the excess of sales during a period over the amounts paid for goods and the services acquired from other business firms during that period.”

VAT is new concept on collecting revenue, which is recently innovated in the field of the taxation. Each stage of the goods and services are levied to tax on its Added value. It covers the value- added to each commodity by a firm during all stages of the production and the distribution and the VAT is forwarded completely to the ultimate consumers.

## **1.2 Statement of Problem**

In the global age every country should meet the challenges through the economic development. Nepal also facing such problems of its political and social. Before the movement -2, Nepal had facing Maoist problem, but now it is going to over because Maoist is leading the government of Nepal. The government need huge amount for growing public expenditure and economic development of country. The budget of fiscal year 2056/66 also shows that huge amount of money is needed for implementation of the budget. It can only possible when the available resource could be sufficient as public requirement. Govt. expenditure rate is exceeding over the growth rate of revenue almost every year from the beginning of planned development of Nepal.

The revenue mobilization has not been satisfactory in relation to the increasing trend of government expenditure, which shows that there is a gap between government revenue and expenditure. In FY 2061/62, expenditure to GDP ratio was 17.4% and 17.2% in FY 2062/63, which is less than 0.2% with comparative to the FY 2061/62. Similarly, in FY 2061/62 revenue to GDP ratio was 11.9% and 11.2% in FY 2062/63, which is less than 0.7% with comparative to the FY 2061/62. It shows that the expenditure and revenue ratio with GDP has decreased, from the FY 2061/62 to FY 2062/63. But the decreased in revenue is higher than the decreased in expenditure ratio. (Economic Survey, 2063/64)

To meet the excessive expenditure it requires more revenue. Due to the deficit internal sources, foreign loan and domestic borrowing will be increased. The foreign loan has a bad effect on national economy. Increased in foreign loan will increased the interest of loan will have to be repaid from the amount of regular expenditure.

So the government has to focus on revenue collected from Vat system. It will be a best system to reduce the gap between expenditure and revenue in coming FY.

### **1.3 Objective of the Study**

The main objectives of the present study are as follows;

- a) To find out the contribution of VAT from NTC to total tax revenue, total vat revenue an total national revenue of Nepal
- b) To examine the effectiveness of VAT revenue collection from NTC
- c) To examine the major problem of VAT system
- d) To recommend possible measure for further improvement

#### **1.4 Significance of the Study**

In developing country like Nepal, the importance of VAT cannot be minimized. It can fulfill its financial needs by increasing its revenue through VAT. But there are many problem associated with the VAT related with its management, administration as well as policies.

For mobilization of internal sources, Nepal government has already adopted VAT administration and policy. Nepal has adopted VAT since 16 November 1997 with the following objectives; (a) expanding the tax net (b) export promotion (c) reducing economic inefficiency (d) acceleration the development by abolishing/ reducing cascading/ pyramiding effect (e) evolving a clean and transparent tax system in place of sales taxation.

This study will provide a clear idea and knowledge to those who are interested to know more about VAT and who are confused about VAT system. It also provides information about VAT revenue collection from NTC to the interested persons.

#### **1.5 Scope of the Study**

The study has been covered the following major areas;

- a) Role of VAT revenue from NTC to national revenue
- b) Revenue collection from VAT of NTC
- c) Comparative study of total VAT revenue with vat from NTC.
- d) Existing contribution of VAT from NTC

#### **1.6 Research Methodology**

The data and information used in this study “Contribution of VAT from NTC to national revenue” is both primary and secondary. The primary data are from the analysis of respondent, field visit and face-to-face interviews with selected persons included in this purpose sample.

The major sources of secondary data are economic survey and budget speech of various years, ministry of finance Govt. of Nepal, books related to vat, report and record of department of Inland Revenue (VAT) ministry of finance, govt. of Nepal, National Newspapers, Journals, Souvenir and News Magazines, various annual report, record of Nepal Telecom.

For the purpose analysis the collected data are classified, tabulated and analyzed in descriptive and analytical way. Generally, simple statistical tools have been used which are as follows,

- a) Simple Percentage
- b) Simple Average
- c) Correlation
- d) Graphs Chart and Diagram

### **1.7 Limitation of the Study**

The present study is not free from the limitation. The limitations of the study are as follows;

- a) The study is based on the availability of reliable data and literature
- b) This study covers period from fiscal year 1995/96 to fiscal year 2005/06
- c) Data used in this study are secondary as well as primary but primary data has been collected from the Kathmandu valley only due to the lack of time and other difficulties

### **1.8 Scheme of the Study**

This study has organized in sixth chapter. The first chapter is introduction chapter, which includes general background, statement of problem, objective of study, significance of study, scope of study and limitation of study.

Second chapter is about conceptual framework, public enterprises & Nepal Telecom and review of literature through different relevant books, journals and up published dissertation.

The third chapter is research methodology, which includes research design, nature and source of data, data processing and analysis procedure.

The fourth chapter is the main body of research, which includes vat revenue from NTC, has been analyzed and data collection and survey result is presented.

Finally, summary, conclusion and recommendations are presented in the final chapter.

## **CHAPTER - II**

### **REVIEW OF LITERATURE**

#### **2.1 Conceptual framework**

##### **2.1.1 Concept of tax**

The main goal of government in any developing country is the improvement in life standard of its people through development activities. To plan and implement different development activities, government needs huge amount of different resources. Government can mobilize additional financial resources internally or externally. However internal sources for resource mobilization are better and safer means for sustained economic development. Taxation is regarded as the most important instrument for internal resource mobilization of the country. The government collects the revenue from different sources such as tax remittance from public enterprises, fees, fines, grants and financing from loan.

However, across all these sources of collecting the public revenue, taxation is the main source and it occupies the most important place in the government treasury. Because of importance of this source in revenue mobilization of country, some person likes to say tax as the sinews of the state.

What is tax? Different persons have defined taxation in different way. In this respect, it would better to take the definition given by seligam. In this words taxation is the “compulsory contribution from a person to the government to defray expenses incurred in the common interest of all without references to special benefit conferred” (Kandel, 2003: 2 ). The definition given by Bastable is considered most appropriate, “A tax is a compulsory contribution of wealth of a person or body of persons for the service of public power” (K C, 2006, P.2). A tax is a contribution from citizen for the support of the state. (Adam Smith)

A tax is a compulsory contribution from a person whether it is law made or natural one to the government to defray the expenses incurred in the common interest of all without special reference to special benefit conferred. It is a personal obligation to pay tax and there is no direct relationship among tax, benefit and individual. Tax is collected from haves and utilized for the interests of those have not. Government imposes taxes on the basis of legislation. The main objective of taxation is to divert control of economic resources from the state for its own use or transfer to other (R. Godde-1984, Government Finance in Developing Countries). Tax is a compulsory contribution to the public authorities to meet the general expenses of the government, which has been incurred for the public welfare and without reference to special benefits. Tax is a compulsory legal contribution to the government by a person who has liability to pay tax from his/her income. The government expends the collected tax amount for general welfare and betterment of nation as well as for the interest of general public. Thus taxes are general contribution of wealth levied upon person, natural or corporate to defray expenses incurred to conferring common benefits upon residents of the state. Presently, almost all the countries have their respective taxation system in their economy. It has become an indispensable source of revenue for the government.

### **2.1.2 Taxing Principles and Objectives in Developing Economy**

The major sources of government revenue in any country are taxes. Taxes come from the economic activities like employment, industry, trade, profession and investment etc. So the tax system should play the role of facilitator to the economic activities of the nation. The effects of tax on ability of a person pay tax and on industry and trade should be considered while formulating tax policies.

Senior classical economist Adam Smith has suggested some taxing principles.

a) Principle of Equity

Equity principle of taxation focuses on ability to pay. Person having income should be taxed higher income group should be with lower tax rate. Thus policy establishes equitable to liability in the same income group.

b) Principle of Certainty

Tax system should be certain in terms of rate, payment and procedures for payment of tax.

c) Principle of Convenience

General taxpayers may not possess sufficient knowledge on taxation. Tax system should be so simple that general taxpayers would feel no difficulties. Time, place and process of tax payment should be convenience to tax payers.

d) Principle of Economy

The collected tax amount should account higher than the expenses incurred for the collection of such revenue. Besides these, other principles for good taxation system are productivity, elasticity, diversity, simplicity, neutrality and coordination etc.

### **Taxing Objectives**

a) Growth Objective

Economic development is measured in terms of growth in real per capita income. In order to achieve in per capita income the rate of investment in public and private sector should be accelerated by means of taxation.

b) Equity Objective

Equity in taxation refers to taxation on the income on the basis of ability to pay. There are two aspects of equity, horizontal equity and vertical equity. The

problem of equity cannot be neglected in developing countries. A tax system, which assumes equity objective, has to be progressive.

#### c) Stabilization Objective

Since the process of planning is necessarily inflationary, prevention of inflationary pressures on process assumes particular importance in developing countries. The indirect taxation inquiry committee to Indian found the contribution of direct and indirect taxes a positive role in controlling inflation. Universal direct tax curbs aggregate demand without affecting consumer sovereignty. Indirect taxes can affect the demand for different products differently. They can curtail the demand for those goods, which are short in supply.

### **2.1.3 Classification of Taxes**

There is variation in classification of taxes between economist and tax accounts. The major classification of tax may be direct taxes, indirect taxes, progressive taxes, proportional taxes, regressive taxes, degenerative taxes, multiple taxes, single taxes etc. however taxes are broadly classified into two groups: Direct tax and Indirect tax.

#### **Direct Tax**

Direct tax is a personal tax and both impact and incidence of tax is borne by the taxpayer. There is no possibility of forward and backward shifting. So, full burden of tax is borne by the same taxpayer. According to Dr. Dalton, “A direct tax is really paid by the person to whom it is legally imposed”. In the world, most of developing countries generate 3/4<sup>th</sup> of their internal revenue from direct taxes and out of which income tax is the major component. In Nepal, contribution of direct taxes to the total tax revenue accounts about 21%. Examples of direct taxes are income tax, gift tax, interest tax, property tax, vehicle tax, house and land tax etc. direct tax is equitable, certain, elastic and

economic also. Direct tax creates public awareness by inspiring to assess the utilization of revenue paid by them whether in productive sector or not. In other font, direct tax has some demerits as well. As the impact and incidence of direct tax is to be borne by same person may fill economic burden, inspiring the possibility of tax evasion. As the taxpayers feel the burden of tax imposed by government directly there may be tax-evading attempts. There may be lack of mass participation and it may discourage saving and investment in the economy.

### **Indirect Tax**

Indirect tax is the tax collected from other persons by transferring the tax liability, by the taxpayer. The taxpayer transfers the burden of tax to other in the society partially or fully. It is imposed on one person but the incidence of the tax is borne by another person through backward and forward shifting processes. In the case of indirect tax, the person paying the tax and the person bearing the burden of tax is different. Value added tax, hotel tax, entertainment tax, excise duty; export and import duties etc. are the examples of indirect tax. Nepal is heavily relying on indirect tax revenue, which seems to be approximately 79% of total tax revenue (Amatya, Pokhrel & Dahal, 2004).

#### **2.1.4 Introduction of VAT**

Value added tax is newly developed modern and scientific tax system which is recently introduced in the field of taxation. It is hybrid taxation from the retail level of sales tax. So VAT is an advance form of sales tax. It has spread all over the world within a short span of time. It has gained huge popularity in short period of time in a history of taxation.

In the field of taxation, VAT has been considered as an attractive alternative to indirect tax system. It has been emerging as a main element of the worldwide tax reforms.

Value added tax is a tax imposed on “Value added” by a business firm on goods and services at the successive stage of production and distribution. “Value added” on a commodity or services is simply the excess of sales value over purchases by business entity. The VAT is collected from sellers on the basis of their value added at each of the stage of business process, thus the same value is never taxed twice and never produces cumulative effect.

VAT for a firm is nothing but its gross receipts from sales minus all expenditure on goods and services purchased from other firms. In the production and distribution process, a firm buys materials from other firms. These materials may include principal raw materials, auxiliary raw materials, chemical, electricity and goods such as machinery, equipment, building, furniture, and vehicles. The firms adds value to these purchased materials by processing or handling them with help of its own factors of production such as labor, land, capital etc. This increase in the value of output over inputs is the value added by a firm. In this sense, value added by a firm is the sum total of incomes paid out by the firm to factors employed. This means that value added by a firm is equivalent to its payment of wages, salaries, rent and interest plus its profit and this value added is the base of VAT.

VAT is new concept of collecting revenue. Each step of goods and services are levied to tax on its added value. It covers the value added to each commodity by a firm during all stages of production and distribution and the VAT is shifted forward completely to the ultimate users.

We can able to get a clear concept of VAT through an example, consider the case of sugar production. A farmer produces sugarcane and sells it to miller. The miller adds value in the process of changing sugarcane into sugar. Value added of the miller constitutes all the expenditure including profit. And, miller sells his product i.e. sugar to a dealer, which in turn sells it to the retailer with

an increased value. Ultimately, sugar is sold to the consumers with some additional value. Thus, at each stage of production and distribution, value is added as sum total of all such added value exactly equals to the final sales value of the sugar.

The following table shows simple process of calculating VAT

**Table 2.1**  
**Operation of VAT**

<b>Production &amp; distribution stages</b>	<b>Purchase price</b>	<b>Selling price</b>	<b>Value added</b>	<b>Output tax(tax collected on sales)</b>	<b>Input tax(tax paid on purchase)</b>	<b>VAT payable to govt. each stage</b>
Farmer		500	500	65		65
Miller	500	600	100	78	65	78-65=13
Dealer	600	700	100	91	78	91-78=13
Retailer	700	800	100	104	91	104-91=13
<b>Total</b>						<b>104</b>

*Source: Arbitrarily Estimated Figure*

From the table, by using a VAT rate of 13%, the farmer pays of Rs. 65 as VAT to government. The miller collects a VAT of Rs. 78 on his sales but has as input tax credit Rs. 65 and thus remits Rs. 13 to the government. Likewise, the dealer collects VAT of Rs. 91 but deducts his input tax Rs. 78 and remits the balance of Rs. 13 to the government account. On the same way, retailer collects Rs. 104 as VAT and remits Rs. 13 to the government after deducting his input tax of Rs. 91. and finally; the government gets total revenue of Rs.104 (65+13+13+13) from all stages.

### **2.1.5 Origin and Development**

The world is steeping in developing way. The world now has developed various techniques, innovation, likewise a VAT in the field of taxation. VAT, a latest and emerging tax, is one of the successful experiments in the tax system.

It isn't a one job. It has long historical journey to be developed from the crude concept.

While going to the origin point of the VAT, Dr. Wilhelm Von Sieman recommended Vat for Germany in 1919 to replace the 'Umsatzsteller' (multistage sales tax) in order to avoid the undesirable effects, particularly cascading and vertical integration of the latter tax (MST) for the first time. The German government seriously considered introducing VAT but due to the fear of administrative complication, which involve with this tax, it decided to lower the rate of Umsatzsteuer instead, in order to minimize negative effects of this tax. Therefore in 1921, Prof. Thomas S. Adams suggested the tax for the United State of America to replace the existing corporate income tax. Further, same tax was developed in 1949 by a tax mission to Japan led by Professor Carl S. Shoup for the purpose of reconstructing the Japanese economy by a avoiding the existing defects of the turnover taxes. Although, these proposal and recommendation were not come into place. VAT was not introduced by any country until 1953. The development of VAT remained limited only in theory up to the early years of 1950s.

France put forward a VAT in 1954 that covered the industrial sector alone and the tax was limited up to the wholesale level. The tax was limited to the boundaries of France until 1959.

Ivory Coast introduced VAT in 1960, became first follower of France after a gap of six years. Senegal also implemented VAT since 1961. VAT in these both African countries, was limited to import and manufacturing stage only.

Since the 1960s, VAT becomes a popular subject matter of taxation in many countries. Denmark and Brazil also adopted it in same year of 1967. In the year of 1968, France redesigned the existing VAT system and extended it to the

retail level. Germany also adopted VAT in the same year. Since 1969, VAT was in operation in Netherlands and Sweden; Luxembourg adopted VAT in 1970, Belgium in 1971, and Ireland in 1973. Of the other member of the European Economic Community, Portugal and Spain introduced VAT in 1986 while this tax was adopted by Greece in 1987. Thus this trend shows that VAT became most popular in the Europe.

Vietnam was the first country in Asia to introduce VAT in 1973. South Korea introduced VAT in 1977, China in 1984, Indonesia in 1985, Taiwan in 1986, Philippines in 1988, Japan in 1989, Thailand in 1992 and Singapore in 1994.

In SAARC region, Pakistan introduced VAT in 1990 as a first member country of SAARC countries. India introduced VAT in a different way under the name of modified value added tax (MOD VAT) in 1996. Bangladesh adopted VAT in 1991. Nepal has adopted VAT since November 1997. However the first intention of Nepal to move towards VAT could be found in Eight Plan (1992-1997) but the government finally expressed its commitment to introduce VAT from April 1997.

In this way, many rich and poor countries, developed and developing countries, small and big countries, socialist and capitalist countries have adopted VAT. In present situation more than 125 countries adopted VAT system and also have growing attraction of other developed and developing countries.

### **2.1.6 Types of VAT**

The type of VAT has been several bases. The most important of them is the classification of VAT on the base of its treatment to capital goods. The VAT has typically been classified into three variants according to the way the capital goods are treated. They are:

### **2.1.6.1 The Consumption Type**

Under the consumption type VAT, all capital goods purchased from other firms in the same year are allowed to deduct from sales values. While depreciation is not deducted from the tax base in the subsequent years. Since investment is relieved from taxation under this variant, the base of tax is consumption. As exports are relieved from tax while imports are taxed, the base of this tax becomes identical to the base of retail sales tax on consumer goods and services.

Thus, consumption type = Gross National Product – Gross Investment = Total Consumption Expenditure

### **2.1.6.2 The Income Type**

Under this variant, capital goods purchased from other firms are not deducted from the tax base, however, the depreciation in the subsequent years are allowed to deduct from the tax base. The tax falls both on consumption and net investment and the conceptual tax base of this variant is the national income. Thus, tax base under this variant includes consumption and not investment, which is equivalent to the net national product (NNP). Therefore, tax base is given as:

$$\begin{aligned}\text{Income type} &= \text{Gross National Product} - \text{Depreciation} \\ &= \text{National Investment} + \text{Consumption (In +C)} \\ &= \text{Net National Product (NNP)}\end{aligned}$$

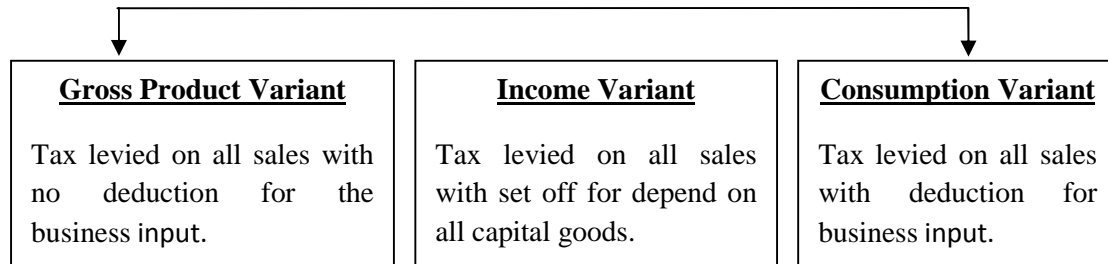
### **2.1.6.3 The Gross National Product Type**

The base for this type of VAT includes capital goods along with the value added on the other raw materials, semi-manufacturing goods etc. purchased from other firms. Hence under this variant, capital goods purchased from other are not allowed to deduct from sales while calculating the tax base. Thus, the

base of VAT consists of consumption and gross investment, which is equivalent to the Gross National Product (GNP).

$$\begin{aligned} \text{Base of VAT} &= \text{GNP} = C + I_g \\ &= \text{Consumption} + \text{Gross Investment} \end{aligned}$$

### **Different Variants of VAT**



Among three types of VAT, the consumption variant has been widely used in several countries in Europe and elsewhere in the recent years. Nepal has also adopted this type of VAT. The reasons for the popularity of this type are that this variant does not affect decisions regarding investment and growth since it relieves investment from any tax burden. Since the tax does not discriminate against capital-intensive techniques in favour of labor-intensive techniques, there is no need for a firm to switch over from capital to labor intensive production. On the other hand, since the gross national product variant creates a “a substantial distinctive for saving, investment and capital intensive production” it is not likely to be a member of tax family of any country. Further more, the consumption variant is more attractive than the income variant from the consideration of foreign trade, because the consumption variant incompatible with the destination, principle of tax action which has been used by many countries. On the other hand, the income variant is consistent with the original principle of taxation. This is why the consumption variant was selected by many countries and why in this study also by VAT, we basically mean the consumption variant.

VAT can be classified on the basis of the vertical coverage through production and distribution stages. Under this classification extent of vertical coverage forward from manufacturing has more practical importance, which has three sub-divisions with different bases. Firstly, the value-added principle may be used within the manufacturing sector only, with tax applying to each manufacturer on his value-added but not by wholesalers or retailers, except to a limited degree. Secondly, the tax may be extended through the last wholesale transaction usually called a pre-retail VAT. Lastly, VAT may be extended through the retail level from the earlier stages of production. This type of VAT is known as comprehensive or full-fledged VAT. Under the same classification next type is based on the extent of vertical coverage backward from manufacturer. Under this type, VAT may be extended to all producers of basic raw materials including farmers. However, this type creates administrative difficulties due to the large number of small establishments and scattered units.

### **2.1.7 Methods of computing VAT**

Value added tax could be collected by using different methods of computation. However, the choice of the appropriate method depends basically on the types of VAT employed and the principle under which VAT is adopted. The VAT can be computed by employing any of the three methods.

#### **2.1.7.1 Additional Method**

For the calculation of VAT payable in this method, the tax base is obtained by adding the income produced by the business firm. In other words, the tax base is computed by adding the payments made by the firm to the factors of production employed in turning out the product such as wages, interest, rent, royalties and profits. This method is appropriate for the income type of VAT that includes in this base its rewards to all factors.

$$\begin{aligned}\text{VAT} &= f (\text{wages} + \text{rent} + \text{interest} + \text{profit}) \\ &= f (W + R + I + P)\end{aligned}$$

If the firm constructs its own capital goods rather than purchasing it, this additional method captures the value added by a firm. The capital method is readily applicable to the income type but clumsy for the consumption type of value added tax. Virtually no country uses the additional method although Argentina and Israel have applied it to selected economic activities, such as banking and finance, where value of outputs is difficult to measure.

#### **2.1.7.2 Subtraction Method**

Under this method, value added is determined as net turnover which is obtained by subtracting the cost of materials from sales proceeds and the procedure was used in the Michigan VAT. This method is driven by subtracting purchase from sales. Thus, value added is obtained by subtracting purchases of produced goods from the figure of sales during the period. This method is appropriate for the consumption variant of VAT. Calculation of tax payable under subtraction method is given in functional form by

$$\begin{aligned}\text{VAT} &= f [\text{outputs (sales value)-inputs (purchase value)}] \\ &= f (S_v - P_v)\end{aligned}$$

This method of calculating VAT is suitable for the consumption variant of VAT. This method is not well suited for discrimination among types of consumer goods but it needs any adjustment to operate correctly for inputs under the origin principle.

#### **2.1.7.3 Tax Credit Method**

This method is also known as invoice and uses an indirect subtraction technique to compute the tax liability. Value added, as such, is never calculated at all, in this method, but the effect is exactly the same as if the figure was calculated and the tax rate applied. Since, the firm deducts the amount of tax paid on its purchases during the period from the figure calculated by applying

the tax rate to its figure of taxable sales for the period. Under this method, tax payers are allowed to subtract the taxes already paid by their suppliers a passed on to them from the gross tax liability, which is, levies on the total value of their sales. Thus, in contract to the subtraction method, which deducts purchases from sales and levied taxes on the difference, tax on purchases is subtracted from the tax on sales under the tax credit method. Hence, net tax liability is given by:

$$\begin{aligned}\text{VAT} &= f(\text{Output} - \text{Inputs}) \\ &= \text{Tax Paid on Sales} - \text{Tax Paid on Purchases}\end{aligned}$$

Among the three methods of computing VAT, the tax credit method is widely favoured in the countries of the European Economy Community and elsewhere. The invoice method is used generally in the European countries and constitutes an advantage of the value added approach, especially in countries where tax compliance is otherwise poor. The tax credit method is so superior to the other methods in terms of the application and enforcement, as well as adoptability to various rate modifications that is now universally employed. The tax credit method can be especially useful if is desired to reduce the rate of the value added tax at some stages in the production and distribution process, say the raw materials or farm products stage, for administration reasons, without reducing the total tax paid on total value added. However, this tax credit method fails to give credit for tax paid prior to the exempt that is given to either of pre-import domestic stage except first stage, because the tax credit chain is broken. The tax credit method encounters still more difficulties under an origin principle value added tax that imposes different stages simply for administrative reasons. Beyond these positive and negative aspects of tax credit method, it has a power to make the overall rate depend on the rate imposed at the last stage of production or distribution, whatever may be the rate of various earlier stages. A simple example of the calculation of value added tax liability under three different methods is given in the table below.

**Table 2.2****Calculation of VAT Liabilities Under Three Different Methods****(Figures in Rs.)**

	<b>Stages of production and distribution</b>			
	<b>Manufacturer</b>	<b>Wholesaler</b>	<b>Retailer</b>	<b>Total</b>
<b>A. Additional Method</b>				
a. Wages	1000	550	750	<b>2300</b>
b. Rent	300	150	150	<b>600</b>
c. Interest	150	100	50	<b>300</b>
d. Profit	350	200	250	<b>800</b>
e. Value added(a+b+c+d)	1800	1000	1200	<b>4000</b>
f. VAT liability	234	130	156	<b>520</b>
<b>B. Subtraction Method</b>				
a. Sales	8600	9600	10800	<b>29000</b>
b. Purchase	6800	8600	9600	<b>25000</b>
c. Value added(a-b)	1800	1000	1200	<b>4000</b>
d. VAT liability	234	130	156	<b>520</b>
<b>C. Tax Credit Method:</b>				
a. Sales	8600	9600	10800	<b>29000</b>
b. Tax on sales	1118	1248	1404	<b>3770</b>
c. Purchases	6800	8600	9600	<b>25000</b>
d. Tax on purchases	884	1118	1248	<b>3250</b>
e. Net VAT liability (b-d)	234	130	156	<b>520</b>

*Source: Arbitrarily Estimate Figures*

*Note: All sales and purchases are exclusive of tax (assumed)*

Above table shows that VAT liability calculated by using any of the three methods is same i.e. Rs.520. However, same VAT liability is possible only when same rate is applied on all stages of sales. If different rates are applied on

different stages. VAT liability differs being higher in first two methods and lower in the later. If we assume that the figures of the value added by the economy is Rs. 4000 in a particular tax period, a 13% VAT gives the corresponding figures of Rs. 520 tax. However, in tax credit method, the calculation of value added is not required but VAT liability under the method is the same. This means that the VAT is ultimately and indirectly levied on the basis of value added. Tax credit method is further explained below.

**Table 2.3**  
**Calculation of VAT Liability Using Tax Credit Method**  
**(VAT at the rate of 13%)**

**(Figures in Rs.)**

	Stages of production and distribution			
	Farmer	Manufacturer	Wholesaler	Retailer
Types of Product	Sugarcane	Sugar	Sugar	Sugar
Purchase value (a)	0	200	400	450
VAT Paid on purchase (b)	0	26	52	58.5
Sales Value (c)	200	400	450	500
Gross VAT liability on sales (d)	26	52	58.5	65
Net VAT liability (d-b)	26-0=26	52-26=26	58.5-52=6.5	65-58.5=6.5
Actual sales price (c+d)	226	452	508.5	565

*Source: Arbitrarily Estimated Figures*

*Note: Both the sales and purchase value exclude tax liability.*

Here, in above table, for the sake of simplicity, the purchase value of the farmer is assumed zero. As shown in the table, each seller calculate the gross tax by applying the given tax rate to his sales value and the net VAT liability by subtracting the among of VAT liability paid by seller at different stages equals to the gross VAT liability on sales with the same VAT rate, so far as tax credit chain is not broken unlikely the remaining two methods, in the tax credit

method, there will be no change in total VAT liability by the rate differentiation in earlier stages, unless tax rate on last stages is changed.

### **2.1.8 Principles of VAT**

While considering the international trade, the principles of VAT have great significance. Whenever international trade between two countries is considered, cross boarder adjustment is necessary; in that case it is very useful to know these principles. There are two principles for levying VAT. They are origin principle and destination principle. Choice between these two principles largely depends on the goals and the policies of nation, accession of international trade computing methods and types of VAT.

In case of international trade, two serious alternatives appear while implementing VAT in any country. They are taxing all domestically produced goods including exported ones and exempting all imports or taxing all the imports and making exception for all exported goods and services to the foreign countries.

#### **2.1.8.1 Origin Principle**

Under origin principle, goods and services produced in a country are subject to tax at the place where they are produced or rendered, wherever they are consumed, and the goods and services imported from the abroad are beyond the tax base. Hence this principle is in the favour of imports and against exports where there is open broader and cross-country trade. Thus, this principle affects balance of payment of the country negatively specially for those who have a poor performance in the world economy. The principle could be followed, with appropriate changes, in the exchange rate, but countries are reluctant to attempt this approach.

As the country can enforce jurisdiction over firms located within its jurisdiction, the principle is much simple and there would be no rebates on sale for delivery within the common market countries, rather each country would give credit for tax imposed in the country of origin. Under such situation, the origin principle has gaining more importance in EEC countries to achieve the ultimate objectives. Three methods-subtraction, addition and tax credit, are all equally well adopted to use of single rate origin principle value-added tax with respect to exports. Imports, in contrast, are bound to present a difficult problem for the original principle if the tax credit method is used.

#### **2.1.8.2 Destination Principle**

Under this principle, all goods and services are taxed at the place where they are produced or rendered but the place where they are consumed. It includes all the imports in the tax net while exports are free from tax. As, the principle taxes imports and exempts exports, it will have favourable effects on the country's balance of payment. According to this principle, tax would be collected at importation and the firm would receive credit for this tax and a refund when the products are exported. This means tax levied on the importation of the basic raw materials, semi-manufactured goods etc. Which are imported for the production in the domestic market will be refunded when the product is exported. Indeed, by principle no tax is collected upon importation at all, other than by the ultimate user. The broad result is that the relative ability of one country to another will be unaffected by a destination arrangements which treats imported and home prepared goods. Thus, neutrality, one of the essential features of the good taxation, is provided by the destination principle by means of no discrimination between imported and domestic products.

## **2.2 Public Enterprises and Nepal Telecom**

### **2.2.1 Public Enterprises**

Public enterprises have assumed significant role in almost every countries of the world. Yet, there has so far been no standard definition of its own. The term public enterprises have been defined differently by different agencies and government to suit there own respective situations. UN has defined PE as ‘those organization, namely government enterprises and public corporation, which are entirely or mainly owned or controlled by public authorities consisting of establishments which by virtue of their kind of activities technology and mode of operation are classified as industries’. The second workshop on performance of public enterprises held in sept.1975 defined PEs as all productive entities organizations which are owned or controlled by public authorities and where outputs are marketed. (Shrestha, 1990)

Public Enterprises (PE) are those enterprises set up by the government, it has to be efficient and at the same time accountable to the government and public. Or in general, we can define public enterprises are those corporate bodies, which are partially or fully controlled and owned by public authorities including marketing of output. Generally, it is recognized as the useful and viable arrangements for the social and economic development of the country. They are virtually indispensable in the developing economics whose development process as a result of historical inequality and exploitation has suffered in the past serious setback and, therefore, needs to be accelerated at a faster rate.

A more practical definition of public enterprise is given by Friedman a well known jurist. He terms public enterprise as, “an institution operating a service of an economic or social character on behalf of the government but as an independent legal entity, largely autonomous in its management, though responsible to the public through government and parliament and subject to some direction by the government, equipped on the other hand with

independent and separate fund of its own and the legal and commercial attributes of a commercial enterpriser”. The definition has emphasis on the fact that PEs are engaged in an activity of commercial nature but on behalf of the government. Public enterprises are constituted as legal persons to whom a fictitious attribution of personality is given by the law. (Mathur, 1993)

PEs being owned by the public is subjected to control by different agencies of the government, which may have different sectoral goals of their own. Public enterprises are essentially economic entities. PEs were established in order to prepare infrastructure service to produce the required goods in the country and to help in controlling the price situation to create opportunities for employment to increase government revenue and to assist in the country’s economic development.

PEs are established in order to prepare infrastructure services to produce the required goods in the country and to help in controlling the price situation, to create opportunities for employment, to increase government revenue and contribute significantly in the national development as well as to assist in the country’s economic development. (Eighth plan)

### **2.2.2 Evolution of Public Enterprise**

Today, the evolution of Public Enterprises (PE), in the world has taken place in such a way that one can hardly find any government remaining aloof from the industrial enterprises, though the degree of involvement may vary. In fact that the very characteristic of the present century has been the acceptance of the role of the state involvement in the economy, no matter how loud the whole world cry for the total role played by the private sector.

Even PEs does exist in a country like USA, where the strongholds of private enterprises exist. The US makes the least use of the PEs. The US has disbanded

most of the PEs that expanded considerably mainly to meet the financial and procurement purposes. For the purpose of dealing with emergency requirements of the 2<sup>nd</sup> world war and the Great Depression of the 1930, it has founded Tennessee Valley Authority (TVA) in 1933, a unique PE setting an example to initiated by many countries to undertake integrated development of great river valleys, irrigation, flood control, navigation, soil conservation and the generation of hydroelectric power. The former British Minister for Overseas Development once marked “we now need to extend the concept of intervention and planning from the national to the international level; from the nation to the world; from the country to the planet. We must now determine that we shall solve out shared and common problems only by a firm rejection of any illusion that there is a free world market economy. The need of the PE was far greater fell especially during the post world war period and the great depression of the thirties, though the need of it went on emphasizing with the adoption of development planning since 1950s.

Each private sector as well as public has its own merits and demerits depending upon the ideology, resource available, regulation, consciousness, control, monitoring and supervision mechanism etc. Former Prime Minister of India Mrs. Indira Gandhi once remarked “people steeped in poverty are naturally impatient for an ending of disparities and for the opportunity of better life. Many projects have to be taken in hand. Development cannot be left to the mercy of market forces. For it is feasible for the private individual or group to finance the vast investments involved. State intervention is therefore necessary. And we must fulfill our pledge to give social and economic justice to our people.” Whereas Former President of Korea, Park Chung, he insisted “Private ownership of production should be unconditionally encouraged except in instance where it is necessary to control to stimulate national development and protect the interests of the people.”

It is believed that Japan was the first to use PE systematically for promotional purposes. Soviet Union (now it is separated in different countries) also used it properly for building up its socialist economy in those days. India is no exception to it. Public sector did exist in pre-independence era too. But its real development process could take shape only after 1974 with the industrial policy 1998 resolution, which called for “the state play a progressively active role in the development of industries.” In fact, it was the socialist orientation of the government, which led to the development of PEs in India. In Bangladesh, its history dates back to early 1950s. The creation of the PEs in Sri Lanka owes to the 2<sup>nd</sup> World War during which period, it was hard hit by supply position of essential commodities that the government to forcefully set up the PEs. The history of PEs in Thailand is associated with the upsurge of Thai nationalism till the 1930s. Mechanized spinning and weaving mills established in 1934, which was the first enterprise in Thailand.

To conclude, one thing is sure and it is that most developing countries need to make fairly extensive use of PEs as catalytic agent in the process of moving towards development oriented economy at a certain stage in the development process public utility and social sector.

### **2.2.3 Role of Public Enterprises in Nepalese Economy**

Public enterprises have become both necessary and useful as vehicles for development in developing nations. They are being loaded upon as effective instrument of program implementation of accomplishing the desired national development goals. PEs constitutes a large and rapidly growing sector of the economy in the majority of countries in the world today, including Nepal. The economy of Nepal is basically a mixed economy, where the public and private sector freely operate in the business environment except in the case of defense, which is not open to private sectors. There is coexistence of both the public and private sectors in Nepal for the overall development of the country.

Today PE encompasses vast and varied range of activities like banking, insurance, cement, sugar, petroleum products. They can play a crucial role in achieving a reasonably self reliant and self generating economy. Nepal is one of the under developed country which is still in its crawling stage of industrial development. So in Nepal PEs is not matter of choice, rather they are a matter of necessity. In various sector of economy, where private sector has not come forward or has only in limited extent, the public sector has to come into existence. The area in which they operate, range from basic infrastructure, industrial estates, banking, trading and commercial sectors to a big and small PEs to create industrial base in the country to provide better goods/ services to the people, to generate employment opportunities, to mobilize the domestic resources in to best productive used and to fulfill the government plans and objectives, PEs have helped to increase the standard of living, regional balance of developing and they have contributed through import substitution, export promotion and strengthening the revenue generation of Govt. of Nepal and save foreign currency by reducing import as well as to provide the consumable goods and services at a fair price.

Nepal tried to develop public sector institutions after the advent of democracy in 1951. The first enterprise to be turned in public sector was Nepal Bank Limited established in 1938 AD with government and private shareholding. Nepal has adopted national plan for the development of industrialization. Private investment is encouraged and foreign investment is welcome in national planning commission. In this process, the government has conducted the procedure of privatizing some public enterprise, such as Bhrikuti Paper Mill, Hari Siddhi Brick Factory, Banshbari Leather and shoe Factory are the first phase of privatization. The process of privatizing is continuing.

For the development of public enterprises as well as National Planning in Nepal, National Planning Commission was started since 2013 B.S.

Development and growth of public enterprises which are related on every plans. Since then the number of PEs has increased substantially in the various field of national economy. The PEs is categorized as follows:

- Industrial Sector: Nepal Orind Magnesite, Udayapur Cement Factory, Herbs Production and Processing Company, Hetauda Cement Industry Ltd., Janakpur Cigarette Factory, Dairy Development Corporation and Nepal Drugs Ltd.
- Business Sector: Agriculture Input Company, National Seeds Company, National Trading Ltd., Timber Corporation, Nepal Food Corporation and Nepal Oil Corporation Ltd.
- Service Sector: Nepal Civil Aviation Authority of Nepal, Nepal Airlines Corporation, Nepal Warehouse Co. Ltd., Nepal Engineering Consultancy, National Productivity and Economic Development Center Ltd., National Construction Company Ltd., Industrial District Management Ltd.
- Social Sector: Janak Education Material Center Ltd., Nepal Television
- Public Utility Sector: NEA, Nepal Telecom, Nepal Drinking Water Corporation
- Financial Sector: Rastriya Banijya Bank, Agriculture Development Bank, Nepal Industrial Development Bank, Deposit Insurance and Credit Guarantee Corporation Pvt. Ltd., Nepal Stock Exchange

#### **2.2.4 Privatization of Public Enterprises and Liquidation**

The government of Nepal has recognized privatization of PEs as an integral component of her economic liberalization and open market economic policy. This programme in Nepal has mainly concentrated on fulfilling the goals of increasing productivity of industries and academics through the administrative liabilities of the government, and increasing extensive participation of private sector in economic development of the country. In this process the programmed of privatization is being executed with priority for last one and half decades,

appealing the participation of private sector in the management and ownership of public enterprises. Commercially, economically, and financially feasible PEs have been handed over to the private sector. Similarly the PEs whose social and economic justification are found to have been no more viable in present time to correspond to the initial goals of their establishment, have been liquidated.

The name of 30 PEs either divested/ privatized or liquidated by now is stated below;

**Table 2.4**  
**Details of Privatized and Liquidated Public Enterprises**

S.N.	PEs Name	Privatized and Dissolution Year	Privatization Mode
1	Bhrikuti Paper Factory Ltd.	1992	Assets and Business Sale
2	Harisiddhi Brick and Tile Factory Ltd.	1992	„
3	Bansbari Leather and Shoe Factory Ltd.	1992	„
4	Nepal Film Industry Ltd.	1993	Equity Sale
5	Balaju Textile Industry	1993	„
6	Raw Hide Collection and Processing Co. Ltd.	1993	„
7	Nepal Bitumen and Barrel Industry Ltd.	1994	„
8	Nepal Lube Oil Ltd.	1994	„
9	Nepal Jute Development Co. Ltd.	1993	Liquidation
10	Tobacco Development Co.	1994	„
11	Nepal Foundry Factory Ltd.	1996	Equity Sale
12	Raghupati Jute Mill Ltd.	1996	„
13	Biratnagar Jute Mills Co. Ltd.	2002	Management Contract
14	Nepal Bank Ltd.	1997	Equity Sale
15	Nepal Tea Development Corporation	2000	„
16	Agriculture Project Service Center Ltd.	2001	Liquidation
17	Cottage Handicraft Sale Emporium Ltd.	2002	„
18	Nepal Coal Ltd.	2002	„
19	Hetauda Textile Industry Ltd.	2002	„
20	Nepal Transport Corporation	2002	Dissolved
21	Butwal Power Company	2003	Equity Sale
22	Birgunj Sugar Factory Ltd.	2003	Liquidation
23	Agriculture Tools Factory Ltd.	2003	„
24	Bhaktapur Brick factory	2004	Assets and Business Sale
25	Lumbini Sugar Factory	2006	„
26	Nepal Rosin and Turpentine Ltd.	2006	„
27	Himal Cement Industry Ltd.	2002	Liquidation
28	Nepal Drilling company	2006	„
29	Agriculture Chun Industry Ltd.	2006	„
30	Nepal Telecom Company Ltd.	2008	Equity Sale

Source: *Economic Survey 2064/65*

**Table 2.5**  
**Liability paid by Government of Nepal of the divested/ privatized and liquidated PEs**

S.N.	PEs Name	Liability	For
1	Himal Cement Company	37,00,00	Loan & employee's facility
2	Bhaktpur Bricks factory	20,62,31	„
3	Birgunj Sugar Factory	70,67,24	„
4	Agri. Tools factory	5,29,76	„
5	Nepal Rozin & Turpentine	18,08,12	„
6	Lumbini Sugar Factory	50,89,67	„
7	Agri. Chun Industry Ltd.	81,595	„
8	Nepal Coal Ltd.	83,91	Loan Investment
9	Nepal Transportation Corporation	36,16,85	„
10	Hetauda Textile Industry	53,60,35	„
11	Cottage Handicraft Emporium	81,033	„
12	Nepal Tea Development	11,86,71	„
13	Biratnagar Jute Mills	45,14,09	„

*Source: Economic Survey 2064/65*

### **2.2.5 Performance of PEs in Nepal**

Analysis of the overall economic situation of the entire 36 public enterprises owned entirely or partially by the government of Nepal shows that 22 PEs have earned profit where as 14 PEs are in loss in FY 2063/64. Among the profit earning PEs also the economic situation, capacity utilization and employee's productivity of most of them is not found to have been satisfactory.

There is a need to adjust the role of public enterprises in the economic development of the country in a manner to suit a liberal, open competitive economic system and therefore, in such context the aggregative achievement of the PEs goals/ target is not found to be satisfactory one. The main reasons for unsatisfactory standard of PEs are inability to operate commercially, excessive employees, obsolete plants and machineries, inability to operate in a competitive environment and gradual minimization of the objectives and justifications for which the PEs are established.

By the end of FY 2063/64, equity investment of the government of Nepal in all 36 PEs amounted Rs. 75802.7 millions and due loan investment has amounted to Rs. 65141.6 millions up to the end of the fiscal year 2063/64. And during the same period Rs. 1485.5 millions received as dividend. (Economic Survey, 2064/65)

As regards to the financial performance of PEs, in FY 2063/64, out of 36 PEs, 14 PEs have got operating loss whereas 22 PEs has generated net profit. Comparing with the FY 2062/63, most of the PEs has got improvement in their result. In the FY 2063/64, aggregate net profit of the PEs is Rs. 7960 millions whereas the PEs had got net profit Rs. 2540 millions in the FY 2062/63. The reason behind the increase in net profit is specially Nepal Telecom and Agriculture Development bank shas contributed Rs. 5980 millions and Rs. 150 millions respectively. Similarly, decrease in loss of Nepal Oil Corporation from Rs. 3670 millions to Rs. 1920 millions is also a key factor to increase in aggregate net profit of PEs.

We are going to analyze the financial performance of all PEs in sector wise as follows:

- a) Industrial Sector: - There are 7 PEs which are related to industrial sector. In FY 2062/63, aggregate net loss of all PEs of industrial sector amounted Rs. 278.8 millions but in FY 2063/64, aggregate net loss decreased to Rs. 178.1 millions. In FY 2063/64, Udaypur Cement Factory and Janakpur Cigarette factory has got losses amounted Rs. 134.2 millions and Rs. 50 millions respectively. Similarly, Milk Development corporation has got net profit in the FY 2063/64, amounted Rs. 11 millions whereas it had got amounted Rs. 25.5 millions losses in the FY 2062/63.
- b) Trading Sector: - There are 6 PEs are related with trading sector. In the FY 2063/64, aggregate net losses is amounted Rs.1930 millions of

trading sector PEs whereas in the FY 2062/63, the aggregate net loss was amounted Rs. 3820 millions. It shows that net aggregate loss has decreased due to decrease in 50% net loss of Nepal Oil Corporation.

- c) Service Sector: - There are 7 PEs related with service sector. The net profit of service sector in the FY 2063/64, is amounted Rs. 568.4 millions whereas in the FY 2062/63, it was amounted Rs.315.9 millions. It is indicated that 80.5% profit is increased in FY 2063/64 with compare to FY 2062/63.
- d) Social Sector: - In service sector, there are related 5 PEs. While analyzing the service sector, we can found that net loss of the sector in the FY 2062/63 was amounted Rs. 66.5 millions, but in the FY 2063/64, the net loss has increased to Rs. 124.2 million. There is 90% increased in net loss of the sector in the FY 2063/64.
- e) Public Utility Sector: - In public utility sector, there are related 3 PEs. From the analysis of the sector, it is concluded that net profit of the sector in the FY 2062/63 was amounted Rs. 3680 millions and Rs. 5570 millions in the FY 2063/64. With compare to FY 2062/63, the net profit is increased 90% in the FY 2063/64. The reason for increasing in net profit is the performance of Nepal Telecom and Nepal Electricity Authority. The both PEs are generating net profit in increasing trend.
- f) Financial Sector: - In financial sector, there are related 8 PEs. The aggregate net profit in the FY was amounted Rs. 2720 millions and amounted Rs. 4060 millions in the FY 2063/64. There are 49.3% increases in net profit due to increase in profit of Agriculture Development Bank. All the PEs of financial sector is operated in profit.

Net capital investment/ profit ratio in FY 2062/63 was 0.90% but in FY 2063/64, the net capital investment/ profit ratio is increased to 5.46%. At last we hope that the net capital investment/ profit ratio will increase in coming fiscal year.



**Table 2.6**  
**Performance of Public Enterprises**

**(Rs. In Million)**

Types of Enterprise	Gross Profit														
	2050/51	2051/52	2052/53	2053/54	2054/55	2055/56	2056/57	2057/58	2058/59	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Manufacturing	-113.9	-737.4	-537.4	-819.1	-679.2	-484.6	-409.0	-357.4	-353.5	-400.4	-117.1	-157.5	-340.2	-180.1	-129.0
Trading	-291.0	14.3	-673.0	-1563.9	-1383.3	265.2	689.4	86.5	-522.8	-2080.9	-1958.8	-2641.0	-4187.1	-1901.7	-7336.4
Services	375.7	-18.5	321.3	-27.5	-15.3	-90.3	26.9	-959.6	-272.7	200.8	-259.3	740.4	-57.0	499.5	59.4
Social	18.7	7.1	-12.2	22.4	-23.8	-26.2	-24.7	-21.1	-18.1	4.4	-141.2	43.3	47.9	-48.0	-15.2
Public Utilities & other	323.9	1990.2	1921.2	2027.5	2504.9	2555.7	3410.1	2166.6	2090.2	2662.1	5733.1	2344.2	3979.1	6887.8	5733.3
Financial	760.3	709.9	357.8	836.5	914.3	683.5	-1288.3	-2268.2	-6398.4	-2000.4	-5780.8	1800.9	2246.0	3644.9	5035.3
<b>Total</b>	<b>1073.7</b>	<b>1965.6</b>	<b>1377.6</b>	<b>475.9</b>	<b>1317.6</b>	<b>2903.3</b>	<b>2404.4</b>	<b>-1353.2</b>	<b>-5475.3</b>	<b>-1614.4</b>	<b>-2524.1</b>	<b>2130.3</b>	<b>1688.7</b>	<b>8902.4</b>	<b>3347.4</b>

Types of Enterprise	Capital Employed														
	2050/51	2051/52	2052/53	2053/54	2054/55	2055/56	2056/57	2057/58	2058/59	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Manufacturing	3856.8	7921.5	7591.6	7634.0	3753.5	6287.6	4858.6	4078.1	4035.6	3164	3448.9	3951.4	5458.8	-387.0	2332.4
Trading	297.9	-232.0	1207.6	1509.6	1227.5	1107.4	952.4	1770.7	2482.4	4106.9	3137.1	531.0	-3718.4	-3532.9	-3574.1
Services	8388.9	2539.8	2511.7	1417.9	1114.0	497.5	702.8	290.4	-522.7	-1364.7	9949.9	10792.1	10361.5	11121.4	-
Social	339.9	596.8	672.4	849.7	870.0	947.2	984.2	1066.2	1206.1	1742.5	1957.2	1973.4	1761.9	1851.7	1821.8
Public Utilities & other	39616.0	35035.7	34868.3	54370.0	62175.2	66545.5	72971.2	79027.8	84915.4	88210.9	94450.9	97473.7	105152.3	104524.0	11153.5
Financial	11385.5	13383.0	15159.3	19976.7	12130.6	8300.4	2951.4	-3322.7	57971.4	1372.8	-16040	61952.2	69448.1	49417.4	49242.2
<b>Total</b>	<b>63885.0</b>	<b>59244.8</b>	<b>62010.9</b>	<b>85757.9</b>	<b>81270.8</b>	<b>83685.6</b>	<b>83420.6</b>	<b>82910.5</b>	<b>150088.2</b>	<b>97232.0</b>	<b>96904.0</b>	<b>176674.2</b>	<b>188464.2</b>	<b>162994.6</b>	<b>161358</b>

Types of Enterprise	Gross Profit as % of Capital Employed														
	2050/51	2051/52	2052/53	2053/54	2054/55	2055/56	2056/57	2057/58	2058/59	2059/60	2060/61	2061/62	2062/63	2063/64	2064/65
Manufacturing	-2.95	-9.31	-7.28	-10.73	-18.10	-7.71	-8.42	-8.76	-8.76	-12.66	-3.40	-3.99	-6.23	-	-
Trading	-97.7	-	-55.73	-103.60	-112.69	23.95	72.39	4.89	-21.06	-50.67	-62.44	-497.39	112.61	-	-
Services	4.48	-0.73	12.79	-1.94	-1.37	-18.15	3.83	-330.44	52.17	-14.71	-2.61	6.86	-0.55	4.49	-
Social	5.5	1.19	1.82	2.64	-2.74	-2.77	-2.51	-1.98	-1.50	0.25	-7.22	2.19	2.72	-2.59	-0.83
Public Utilities & other	0.82	5.68	55.51	3.73	4.03	3.84	4.67	2.74	2.46	3.02	6.07	2.40	3.78	6.59	5.14
Financial	6.68	5.30	2.36	4.19	7.54	8.23	-43.65	68.26	-11.04	-145.72	-	2.91	3.23	7.38	10.23
Total	1.68	3.32	2.22	0.55	1.62	3.47	2.88	-1.63	-3.65	-1.66	-2.61	1.21	0.90	5.46	2.07

*Source: Ministry of Finance (Economy Survey 2064/65)*

### **2.2.6 An Introduction of NTC**

Telecommunication was introduced in Nepal towards the beginning of the twentieth century during the Rana periods. In the essential stage, a few magnet set was installed at the buildings of the top brass Rana in the year 1913. The people they were not allowed to use such a limited telephone services.

In 1969 for the systematic manner telecommunication board was established and its resources based considerably strengthened in terms of its ability to handled modern telecommunication technology for the establishment of new telecommunication facility in Nepal.

Later, in 1975 telecommunication board was converted into Nepal Telecommunication Corporation (NTC). After a stunning series of development, NTC was finally established on July 15, 1975 under the communication department. Telecommunication department was established by the combination of the existing Aakashbani Head Office and Telephone Head Office in 2016.

Before the drawn of democracy in 2007 B.S. trunk telephone service was provided to some of the important places of the country to establish contact among them. Telephone lines were joined from Kathmandu to Raxual, Dhankuta and Palpa to provide this facility. Besides this a 25 lines automatic telephone system was operated in capital and trunk call service provided to six districts.

Before implementation of 1<sup>st</sup> five year plan, Nepal had wire less relation only in 28 centers in various parts of the country. About 18 of these stations were equipped with modern equipment. The wire less service was made workable by means of petrol generators in different district except Kathmandu and Biratnagar. A material and machinery requisite for wireless services had been

made available during the period of 2<sup>nd</sup> world war, a satisfactory service could not be achieved on account of the difficulty of transporting the petrol in the remote district.

In the year 2031 BS, microwave transmission links were established for internal trunk. Beside this, the use of high technology and reliability, satellite earth station was established in 2039 B.S. at Balambu, Kathmandu. After successful establishment of satellite, telecommunication service of worked was linked with Nepal by the help of seven circuits joined.

The corporation is an inevitably accountable autonomous and organized institution. The first general manager of NTC was Uday Bahadur Nakarmi. The prime part of the corporation in NTC management committee, which was established in 2032 Ashar 1<sup>st</sup>. In Nepal, NTC is the only company to provide the telephone service and only corporation to earn profit while in the country the rest of the scenario is just the other way around. Apart from the other services provided by the company: 93% of total income which was Rs. 6097 millions in FY 2001/02, Rs. 7132 millions in FY 2002/03, Rs. 8235 in FY 2003/04, Rs. 8550 millions in FY 2004/05, Rs. 10285 millions in FY 2005/06 is achieved from telephone only. In this 93% of total income, 17% in STD, 32% in ISD, 18% in Mobile, 26% in Local and 0.5% in CDMA.

The main purpose of the establishment of NTC in Nepal was to strengthen the administrative efficiency of the government. It was later to serve the needs of development of various sectors as expansion of foreign trade, tourism development and international integration.

The other objectives adopted by the corporation are as follows:

- 1) To provide high quality, reliable and economic services

- 2) To exchange information for the preparation of fundamentals for development of nation
- 3) To establish telecommunication links among the countries around the world
- 4) To participate the publics in telecommunication so as to uplift their living standard
- 5) To provide prompt services to the places of demand
- 6) To introduce new technologies and cope up with time and tradition.

To meet the demand of day-to-day increment of telephone services, NTC has installed more and more exchanges around the country and expanded its network. Now 3162 VDCs are supplied with telephone networking by C-DOT exchange, martus terminal, UHF/VHF, IICA microwave station and HF exchange. Presently, out of total 75 Districts, 71 Districts are being served with CDMA System and 55 Districts with GSM Mobile.

### **2.2.7 Role of Nepal Telecom**

Telecommunication is one of the most quickest, cheapest and scientific means of communication in the modern world without the facility of telecommunication government could not run the economic governmental and development activities. Other means of communication such as postal services, transportation etc. is slower, expensive and less convenient but telecommunication is reliable means of communication. It brings co-ordination among different government entities, which ultimately promote administrative efficiency can be expected to enhance the productivity of government decision and a better utilization of society & resources as well as mobilization of labors force for the achievement of national goals.

Telecommunication links to overseas countries, which helps in the development of tourist industries, main sources of foreign exchange earning.

Not only it contributes in national economy, but also helps to bring national unity among the national and international people creating a brotherhood relationship among the people. Telecommunication has also contributed a lot for development of social condition of the country because it is a means of the social condition of the accumulation, exchange and transion of knowledge between peoples.

In the developing country like Nepal, without contribution of telecommunication in development of the country cannot explain. In Nepal, there is not any sector where telecommunication has not played role. The effects of telecommunication on the rural areas and their contribution to rural development are potentially extremely important, yet rather different to measure. NTC has played an important role in agriculture sector also by providing information on prices and market situations. Therefore, telecommunication has played a wonderful role in developing and developed countries to develop and to attain national objectives.

### **Transformation from Corporation to Company (Nepal Telecom): An Introductory Profile**

The Nepal Telecommunication Corporation was dissolved and converted to Nepal Doorsanchar Company Limited ( Nepal Telecom) from 1st Baisakh 2061 (13th April 2004). The new company was registered with the company Registrar Office on 2060-10-11 under company act 2053, and the notice to this effect was published in Nepal Gazette dated 26th Chaitra 2060.

The mission statement: Nepal Telecom as a progressive, public spirited and consumer responsive entity is committed to provide nationwide reliable telecommunication services to serve as an impetus to the social, political and economic development of the country.

The vision: Nepal Telecom's vision is to remain as a dominant player in the telecommunication sector of the country while extending reliable and affordable telecommunication services to all regions including the remotest area of the nation and at the same time retaining its present sound financial health event in the coming competitive environment.

Nepal Telecom ltd. has provided telephone service through the country with 240 telephone exchanges from these exchanges 540268 lines have been distributed and are in use. Similarly, Nepal Telecom has distributed 598204 overall CDMA lines, 2044760 GSM (Prepaid+ Post-paid) mobile telephones, 9744 ADSL lines, and 4420 email customer (PSTN) lines. STD and ISD services have been provided in 14 zones and 75 districts. (Economy Services 2006/07)

### **2.2.8 Human Resource Management System of Nepal Telecom**

Human resource management system has been introduced in Nepal Telecom to give the “360-degree view” of the information related to company’s human resources. This HRM system developed in-house in power builder using its native database called Sybase. Currently, HRM system is running under Nepal Telecom’s WAN network at HRD, central office. The system mainly stores the information of the company staff’s personnel, family, service, academic, training, grade and salary information. Its queries and reports are providing tremendous help in decision making especially in the area of recruitment, promotion, transfers, and trainings. Moreover it assists to calculate retirement date, pension/gratuity amount of the staffs at a click of button. On the process of further development, the system will add-in the entire facilities(like service/non service telephone, service mobile, vehicle, quarter, loan provident fund, insurance details, scholarship etc) owned by all categories of employees, their leave, rewards/punishment, evaluation form, company’s organization structure and darbandi details. On accomplishment of all this, only then HRM

system will be complete and ready to deploy in the regional level to work online throughout the Nepal Telecom.

**Table 2.7**  
**Comparative Growth of Nepal Telecom**

<b>Human Resource</b>	<b>2001/02</b>	<b>2002/03</b>	<b>2003/04</b>	<b>2004/05</b>	<b>2005/06</b>
Approved post	6001	6000	5759	6095	6984
Manpower per 1000 line of PSTN	14.3	12.83	12.59	11.76	11.18
Manpower per 1000 line (including mobile)	-	-	8.38	5.05	3.61
Working man power	4687	4772	5709	5717	5699
<b>Technical</b>	<b>2001/02</b>	<b>2002/03</b>	<b>2003/04</b>	<b>2004/05</b>	<b>2005/06</b>
Complaints per 100 line	7.34	7.69	7.2	6.86	8.02
Installed telephone exchanges	151	171	204	225	231
Districts having exchanges	66	67	71	72	72
Installed telephone lines	389400	445537	550257	602252	656070
Distributed telephone lines	327673	371816	453475	485997	509873
Waiters	317293	319514	314406	316546	-
International circuits in operation	1100	1306	2606	3140	3423
Mobile subscribers	21881	50367	227316	622737	909483
CDMA subscribers	-	-	-	23579	161155
MARTS subscribers	2958	3001	2659	2322	2014
Telephone penetration(PSTN)	1.40%	1.80%	1.79%	1.88%	1.93%
Telephone penetration(overall)	-	-	2.69%	4.4%	7.77%
<b>Financial</b>	<b>2001/02</b>	<b>2002/03</b>	<b>2003/04</b>	<b>2004/05</b>	<b>2005/06</b>
Operative revenue (in millions Rs.)	6,160	7,208	8,312	8,584	10,414
Total Assets (in millions Rs.)	25,281	29,893	33,221	35,572	39,351
Returns on investment	14%	16%	15%	18%	19%
Increase in net profit	6%	34.8%	(5%)	24%	24%
Revenue contribution – national	63%	62%	68%	66%	67%

Revenue contribution - international	37%	38%	32%	34%	33%
--------------------------------------	-----	-----	-----	-----	-----

*Sources: - Annual Report, 2007 Nepal Telecom*

### **2.2.9 Nepal Telecom - Milestones**

- 1913- Establishment of first telephone lines in Kathmandu
- 1914- Establishment of open wire trunk from Kathmandu to Raxual (India)
- 1935- Installation of 25 lines automatic exchange in Royal Palace
- 1936- Installation of open wire trunk line from Kathmandu to Dhankuta
- 1950- Establishment of Telegram services
- 1950- Introduction to High frequency Radio System (AM)
- 1950- Establishment of CB telephone exchange (100 lines) in Kathmandu
- 1951- Installation of Open wire trunk from Kathmandu to Palpa
- 1955- Distribution of telephone line to general public
- 1957- Registered as an ITU state member on 5<sup>th</sup> December 1957
- 1962- First Public Telephone Exchange in Kathmandu (300 lines CB)
- 1964- Beginning of International Telecommunication Services using HF Radio to India and Pakistan
- 1965- First Automatic exchange in Nepal (1000 lines in Kathmandu)
- 1974- Microwave transmission links establishment for internal trunk
- 1982- Establishment of standard “B” Types Earth Station for international circuits
- 1982- Establishment of SPC telex exchange
- 1983- Establishment of Digital Telephone Exchange
- 1984- Commencement of STD service
- 1984- Reliable Rural Telecom Service (JICA)
- 1987- Commencement of ISD service
- 1995- Installation of Optical Fibre Network
- 1996- Conversion of all Transmission link to Digital transmission link

1996- Automation of the entire Telephone Network  
1996- Independent Int. Gateway Exchange established  
1996- Introduction of VSAT services  
1997- Digital Link with D.O.T. India through Optical Fibre in Birgunj-Raxual  
1999- GSM NTC Mobile service  
2000- Implementation of SDH Microwave Radio  
2000- Internet Service  
2001- Payphone Service  
2002- East West Highway Optical Fiber Project  
2003- GSM Namaste Pre-paid Service  
2004- Transformation to NEPAL TELECOM (Nepal Doorsanchar Company Limited) from NTC Corporation  
2004- Pre-paid Calling Card (PCC) Service (Intelligent Network Services)  
2005- Advanced Free Phone (AFS) Service (Intelligent Network Services)  
2005- Soft launch of CDMA  
2005- Access Network Services  
2005- Outsourcing of Enquiry Services (1997)  
2006- PSTN Credit Limit Service – PCL Service (Intelligent Network Services)  
2006- Home Country Direct service – Nepal Direct (Intelligent Network services)  
2006- MCC (198) Complain Registration via IVR in Kathmandu Valley  
2006- CDMA Limited Mobility Service in Kathmandu Valley  
2007- CDMA Full Mobility Service  
2007- CDMA Full Mobility Service  
2007- Cheap calls @NRS 8.00/min to USA & Canada using PCC Service  
2007- 188 IVR Service

## **2.3 Reviews of Literature**

### **2.3.1 Reviews from Books**

Carl S. Shoup in his famous book “Public Finance” considers value added tax as the latest and probably the final stage in a historical development of general sales tax, which is imposed on the ‘value added’ by the business firms. VAT is the differences between sales proceeds and the cost of materials etc. purchased from other firms which is the tax base of a VAT. A firm adds value added by processing or handling these purchased items with its labour force and its own machinery, buildings of other capital goods.

Margaret Nicholson (1989) explains value added tax is a tax on the supply of goods and services which is eventually borne the final customers, but it is collected at each stages of the production and distribution chain. Value added tax which is generally abbreviated to VAT. VAT is an indirect tax charged as a percentage of the selling price on the certain services and commodities. The percentage rate is set by the government and is changed from time to time by the budget. Registration of VAT is compulsory for the persons and firms whose turnover is in excess of the threshold limit.

Encyclopedia Management (2002), a value added tax is a tax assessed at each steps of the production and distribution process, levied on the difference between purchase cost of an assets and the price at which it can sell. Tax is added to a product price each time it changes hands until delivery to the customer takes place, when the final tax is paid.

David N. Hyman in the book “The Economics of Government Activity” opines that the VAT is simply multi-stage sales tax which exempts the purchase of capital goods and services from the tax base. By exempting capital outlays at the time of purchase consumption type of VAT provides a kind of investment tax credit incentive.

Silwal (2002) in his book “Value added tax: A Nepalese experience” has expressed his practical experience about VAT. The book covers all aspects of

VAT. In writer's world "VAT is an all stage no cascading tax system. It extends to all levels of production and distribution similarly it covers all stages of goods and services. Any discrimination in taxing goods or services of exempting any of them renders VAT ineffective."

The book mostly concentration on Nepalese tax system. The book clearly analyze why the government of Nepal introduce VAT. Recent government announced retail level sales tax (RST) at the rate of ten percent covering a whole range of goods and services. There was not procedural law to administer it. When RST introduce in Nepal literacy level was meager and billing and record keeping was, fanciful. In this situation, required revenue con not take place, when is turn into the development expenditure. So that a modern, efficient and neutral tax like VAT was, therefore preferred to get rid of past anomalies.

The writer expresses a version by borrowing government declaration that "the government of Nepal does not have the option of doing nothing. Major changes must be made in order to make tax administration fair, efficient and effective. The hostility, harassment and non-cooperation that currently exist between the tax office and the business commodity must end if Nepal is to have a modern tax system. The business wants the system to change and willing to pay a reasonable tax but they want the system transparent and fair.

Silwal suggests that factors affecting VAT design take also into consideration. A poorly designed VAT accompanied by weak administration would just drain the treasury. So almost care is necessary while designing a VAT. According to him, the following fact were considered while designing a VAT in Nepal (i) tax base issue (ii) rate structure issue (iii) exemption issues and (iv) threshold issues.

Finally, Mr. Silwal has reached a conclusion that the introducing of VAT provides an opportunity to sweep a way to cobwebs and revamp a substantial part of the tax administration. In every country where it has been properly implemented the VAT has prove itself as a revenue productive tax. However, benefit from VAT depends upon its coverage.

M.L. Sharma (1994) VAT is levied on the basis of value added to the value of a product of each stage of its sale in the process of production and distribution. In the other words, it is assessed at each stage only on the increase in the value of a commodity since the last transaction.

Khadka (1989) an expert of Nepalese tax system, in his book entitled “VAT is the most recent innovation in the field of taxation. It is levied in the value added of goods and services. The tax is broad based as it covers the value added to each commodity by a firm during all stages of production and distribution.

This book has covered all aspects of VAT including the nature of VAT, reasons for the growing popularity of VAT, department of VAT etc. Apart this the report examines the structure and operation of VAT in the Asian Pacific Countries which also explore the possibility of introducing VAT in Nepal. Probably he is a person of observer of VAT in abroad and he firstly proposed VAT for Nepal with micro-studies of Nepalese economy and system.

Dr. Khadka (1991) in his book “Nepalese taxation a path for reform” has reviewed the development of Nepalese tax system. He analyzed its existing problem and studied feasibility and possibility of tax reform. He lights on the domestic and international economic scenarios. Then, he states that in Nepal, tax reform has become necessary and possible due to both internal and external factors. Further, economic reforms, including tax reforms, have been taking

place vary rapidly in South Asian Countries including India, Pakistan, and Bangladesh and they exert pressure in other countries including Nepal. In the context of Nepal, he states “the foregoing clearly indicates that the Nepalese tax system does not satisfy the criteria of a good tax system. Moreover, poor enforcement has only served to distort the Nepalese tax system does not satisfy the criteria of a good tax system. It is therefore, necessary to reorganize the structure and operation of the Nepalese taxes and strengthen the tax administration.

Khadka (2000) in his latest book “The Nepalese tax system” point out the need to introduce VAT in Nepal. In his book, there are several reasons to introduce VAT in Nepal. One of the important reasons was to develop a stable source of revenue by broadening the tax base. Moreover, Nepal will help to become less dependent on international trade taxes for its revenue in the future. Since it will not be in a position to level important duties on the trade that takes place within the South Asian for Regional Co-operation (SAARC) regions after the implementation of the South Asian Free Trade Arrangement (SAFTA).

The famous pair of modern economists Musgrave and Musgrave (1976) in their book “Public Finance in theory and practice”, suggests that in among three types of VAT, i.e. GNP income and consumption types, the latest types of for practical consideration for both efficiency and equity criterion and tax based on consumption similar to the retailer sales tax especially for the poor countries. The invoice method for calculation is more preferable and advantage of the value added approach.

Describing the problem of VAT states that “A sales tax may be imposed in their single or multiple stage form. If later is implemented in the value added sense, it is equivalent from the economics, point of view to a corresponding single stage tax, at each stage the value of product is increased the prices rise accordingly, which is the value added tax base”.

Among the two types of alternative i.e. VAT and retail sales tax (RST). Posing the same tax base, which one of is more preferable? These strong differences in their opinion are analyzes as:

- ) Number of tax payers is less under the RST than under VAT.
- ) The exclusion of capital goods is more effective in VAT system than under RST.
- ) VAT constitutes self enforcement in invoice system for calculation of tax liability than under RST.

Richard (1986) in his book “Government finance in developing countries” describes VAT as the most important tax innovation of the second half to the twentieth century and it is classified as a form of sales tax on consumption. The tax applies to the value added at production and distribution that is to sales proceeds less purchase of materials inputs and certain services.

### **2.3.2 Reviews from Research Papers, Articles and Journals**

Lent (1973) in the study of “Value Added Tax in developing countries” state that following the adoption of value - added taxes by Western European Countries, many developing countries have been giving in increased attention to this form of tax as a means of rationalizing their sales taxes and improving their revenue.

The study was purposed to examine the applicability VAT in developing countries. “After the empirical study of VAT structure of seven countries i.e. Brazil, Equador, Ivory Coast, the Malagasy Republic, Morocco, Senegal and Uruguay in 1973 and draw the principle features of VAT in developing countries. Applying comparative analytical methodology and covering the issue such as revenue importance of VAT problems of administration, compression of the VAT with other forms of sales tax, only with comprehensive of the VAT with other forms of sales tax, only with a

comprehensive and uniform coverage it is possible to achieve a truly neutral sales tax i.e. VAT.

Shout (1973) the government of India in 1978 appointed L.K. Jha as the chair person of the committee to examine the adoption of VAT at retail level such committee was called Jha committee. After the study, Jha committee presented the report in which the VAT was rejected by staying no need to adopt comprehensive VAT because of administrative constitutional problem and review consideration. But Jha committee concludes VAT can deliver better satisfactory solution of excise duty. It means VAT should be applicable at manufacturing level.

SC Won Change and M.C. Lourdes B. Recent (1988), A study held in 1988 by them on “The VAT experience in Republic of Korea” state that the adoption of VAT was response to the complex problem arising from the indirect tax structure. One of the reasons for adopting the VAT was to simplify the indirect tax structure in Korea. This was also expected to contribute to reduce of the price of commodities in the domestic and export markets. Similarly, on the advantages of VAT expecting to eliminate cascading effect of taxation, efficiency in resource, allocation to increase revenue for the government. VAT was introduced in Korea in 1977.

The study picture out the VAT is very precisely and detail after its implementation and visualizes the condition of the Korean economy before and after its adoption using with descriptive and analytical methodology covering various studies and proposals made by various researcher economists and practical men for VAT reform in Korea. The study draws the pre-VAT scenario saying that “prior to adoption of VAT”. The system of indirect taxes in Korea was complicated and distortion with several taxes and rates. The study covers the issue reasons for adopting VAT, guidelines for adopting VAT, the VAT

structure, the preparation for VAT reform, implementation, administration and problems, measure to improve it and conclusions giving various data and illustrations. Korea has introduced the consumption type of VAT covering all stage of production and distribution changed on supply of goods and services including import with 10% of normal rate, applying tax credit method for calculation, zero rating on import and basic necessities with some exemptions in very small firms and supplemented the VAT by excise duty on luxurious and giving special tax payer's facilities to small business.

Khadka, documentation VAT monitor feb.(1993). He has as research fellow at Philips university, Merbery Germany in his study on "a review of the Nepalese sales tax" state that it is therefore, necessary to introduce a full hedged VAT in other to streaming the sales tax system in Nepal. Briefly, discussing the sales tax system of Nepal its history and need to introduce VAT in Nepal, the study points out the weakness of Nepalese sales tax system i.e. inefficient, tax evasion on sales, inequitable and complex. So he includes a chapter "move towards VAT" and safe that "the import/manufacturing level sales tax gained some features of a value –added tax in Nepal in 1985, when an advance sales tax system in the place of suspension system was introduced.

Thapa(1994) "Value added tax in Nepalese context" he made an effort on value added tax into Nepalese context, he applied the theoretical methodology and deal with government theoretically to expenditure, low revenue effort high dependency of foreign loan, need of more economic growth of the country and because of low revenue potentially from direct tax there is a prompt need to improve the sales tax of Nepal. But there is less chance to mobilize more revenue through existing from of sales tax. In this context, there is no any other alternative except introducing VAT in Nepal.

Khadka (1995), He published an article on “Probability of VAT in Nepal” reached a conclusion that VAT. Theoretically is the best alternative to remove limitations of recent sales tax system of Nepal. He further adds, the merits of VAT do not appear voluntarily. For this implementation aspect of VAT must be efficient. The implementation aspect of the tax depends on the capacity of the tax administration, co-partnership of tax payers, accounting system of the business sector for and political condition etc. So it needs full preparation before introducing VAT in Nepal.

Khada (1996), A report on the government tax system and he has developed his experience and knowledge achieved in the study tour in Germany into the small booklet name as “A report on the Germany tax system study tours” in order to distribute its lessons and usefulness. This week covers all useful discussion held in Germany with policy maker and tax administrators as well as tax payers on the various related topics. Beside the study observers the tax administration training center, tax rates, the existed tax system and the distribution of the collected revenue. In relation with the government of Germany includes VAT. In this category the collected revenue from the various tax systems are distributed among the different levels of the government. VAT is imposed on the value added at all stages of production import and distribution. The revenue received from the VAT by the state government is distributed on the basis of population furthermore when data becomes available, a sound policy can be formulated and a tax system be made on the basis of the result introduction of VAT in Germany. When introduction of VAT, the number of tax payers will increase significantly and will be difficult to do all the work manually such as checking where the interest is paid or not. It is essential to introduce a computer system, which is suitable to the country even though the standardized system developed in countries.

Khadka (1996), “A VAT for Nepal” in his paper on the purposed structure, operation and administration set up of VAT for Nepal and necessary steps to be taken for its early introduction. In its purposed structure, the coverage of VAT should be made as broad as possible covering all business transactions. Exemption should be granted unless there is a specific reason to do so, such as administration and equity. Zero rating should be limited to export and tax rate should be single to avoid complication and inefficiencies in collection.

The purposed operation of VAT requires that the tax payers above threshold limit should be register, vender should issue an invoice for each sale, keep a clear account of his purpose and sale separate account for zero-rated, exempted and positive rates goods and VAT liability should be calculated of its taxable sale, tax credit method should be used as a method of computation of the tax and tax payment and refund period should be of one month. The present sales tax and excise department should be restructured drastically to administer of VAT. Officer level posts should be increased considerably and extensive training should be provided including the operation of computer system. A VAT implementation team including experts and persons for every field should be set up. A detailed preparation should be considered as a pre realist for introduction of VAT. A comprehensive VAT education programs most be launched to the educated tax payer.

Shoup, Carl S. (1998) “The value added tax and developing countries. In an article in the value added tax and developing countries” a VAT is a tax on the value that a business firm adds to things its buys from other firms, in producing its own products. A VAT is comprehensive if it covers all economic activities from the earlier stage of farming or mining right through to the retail. The speed with which the VAT has spread around the world is unmatched by that of any other tax in the modern time, VAT reduces vertical integration because of its nature, which is taxed on the value added but not on turnover. VAT offers

more revenue and coverage than other form of sales taxes. If exempts exports well considering the problem of deducting the capital goods, consumption type of VAT is superior to other forms. In calculation, tax credit method is the universal one. In the VAT system, the taxpayers' responsibility spread much better exempts producer's goods. VAT is more revenue productive, self-enforcing and if goods and basis necessities are to be zero-rated regressive may be reduce. Similarly, on the other hand, its complexity is difficult both in the case of compliance and administration or collection, in factionary in nature, more problems in developing countries and it regressively is also pointed out.

Thapa: (The fifth article), he is the director of foreign currency exchange department of Nepal Rastra Bank. The article points towards the weakness inherent in the value added tax system in Nepal. He is criticized in the time of the introduction of VAT in Nepal. He strongly denounces the existence of stable government at the time of introduction which forced the government to accept many compromise in this regard. He criticizes on the lack of serious consideration to the impact of smuggling from the long open boarder with India and Tibet. The lack of the highly motivated tax administration and proper accounting system are also impacting the function of VAT in Nepal.

### **2.3.3 Reviews from Dissertations**

Michele Guerard (1973), entitled "Brazilian VAT system" an unpublished dissertation submitted to Columbia University in 1973, describes, analyses and evaluates the Brazilian VAT against the background provided by two broader issues: one as a case study of the VAT in developing country and other as an illustration of the problem posed by inter-state tax co-ordination in a special setting of a federation caused by huge regional disparities. The Brazilian states adopted a broad based single rate (i.e. 15%) VAT in 1976 in the place of existing heterogeneous turnover taxes aiming to secure a greater degree of tax co-ordination among the states of the federation. The VAT was based on

modified origin principle, and it extended to retail level with minimum exemptions. The administration of the tax did not appear burdensome.

In the first year of its introduction, revenue increased by 54%, the 30% of which was due to price increase and 17% was the real increase. The industrial sector bore a heavier tax impact than the rest of the economy in relation to its own value added because of the non-deductibility of tax on inputs used by the industrial sector from the exempt sector. Manufacturing accounted for 60% of estimated VAT although it generated less than one fourth of the GDP. The Brazilian experience does suggest that the VAT techniques can be applied to the condition in developing countries with no great difficulty. The administration of VAT could be expected to pose initially a more difficult problem in developing countries which previous have no experiences in operating a broad based sales tax.

Babu Ram Subedi (1997), entitled “Applicability of VAT in Nepal” submitted to the Central Department of Economics, T.U, concludes that VAT is applicable in Nepal on the sense of tax performance. In Nepal, VAT is desired to achieve the goals of neutrality, revenue productivity, fairness and transparency. From his view, VAT is found to be the best alternative to eliminate the existing inefficiencies of tax system. VAT would generate more revenue with less distortion and will unify member of taxes producing very low amount of revenue because of its broad coverage. VAT being member of indirect tax and some exemption for equity goals, the focus of VAT should be on revenue generation in Nepal.

According to the study, VAT should not be taken as easy task; rather it is very challenging issue for Nepal. The major challenging issue for VAT implementation in Nepal is successful tax administration. The existing sales tax administration is not capable of handling VAT. Further, VAT need more active

administrative efforts. Other problems with VAT implementation in Nepal are; lack of account keeping system, lack of sufficient knowledge about VAT, illiteracy and low public awareness. The existing tax evading practices also seems a serious problem. More advantage of VAT can be achieved only if it is extension to the retail level but the extends so of VAT to retail level is impracticable and impossible in Nepal context.

Ghimire, Lalmani (1998), in his dissertation “Value added tax: key issues in Nepal” explains great importance for the effective implementation of VAT administrative capacity in Nepal. Organizational structure, audit and inspection system, reward and punishment, political intervention, selection of skilled and experienced manpower are needed to improve for effective implementation of VAT is considered as a broad based tax and potential advantages of it can be attained fully if the tax is extended through retail level. For the period of time, he suggested to improve following aspects: (i) administrative power and creditability (ii) identification of taxpayer (iii) registration (iv) educational programmers (v) incentives for small trades.

He also find some difficulties in implementation of VAT in Nepal. These are (i) rate structure (ii) small traders in large proportion (iii) lack of accounting records (iv) Illiteracy and high compliance cost (v) existence of open border. Strong administration, registration programmed, existence training programmed, technical data base system, combination of various revenue offices, high level VAT implementation term, coordination of VAT department, close cooperation between government and private sector etc. are essential prerequisites for the successful implementation of VAT in Nepal. Focusing on the ever increasing resource gap, inefficiency in sales tax and need of revenue for handling developmental works, VAT should be implemented in Nepal.

Sharma, Chinta Mani (1998), in his dissertation “Value added tax in Nepal: An administrative and policy issues”, examine several aspects of VAT administration such as its problems, constructions, possibility, operation and other aspects. In his dissertation, he has found the following findings;

- Most of the traders and businessman are lacked with the minimum concept of VAT. They are mainly facing pricing, billing and accounting problems.
- An adequate VAT education programmes are not conducted and VAT administration has also facing lack of administrative personnels.
- The relation between government and business community is broken, which has been barrier to implement VAT successfully.

His suggestions to the government to implement VAT successfully in Nepal are as follows:

- The government should pay attention of design the strong administration.
- The government should try to produce gazette manpower and train them well.
- Comprehensive educational programme should be launched by the government.
- At last, he concludes that VAT requires the strengthened administration for its effective and efficient implementation.

Bista, Raghu Bir (1999), in his research “Applicability and feasibility of VAT in Nepal”, focused the need of VAT for Nepal for several reasons. They are effective revenue mobilization, industrial development, strong administration, transparency and avoiding all tax loopholes. VAT helps to reduce the resource gap broadening the tax base and mobilizing additional resource by controlling tax leakage, unofficial trade and corruption through transparency and account based cross-checking. Positive and favourable effects of VAT on all sectors can

be aliened only if government can operate the VAT administration with effectively and efficiently.

In his research, the following findings can be gained.

- The sales tax system is failure to several cases; narrow tax base, inelasticity of tax rate, incapable and weak administration, tax leakage, corruption and political intervention. So, the entire tax reform is needed.
- A VAT is account based, invoice based and record based; it checks the tax loopholes such as under valuation, non-recording and unauthorized trade. It discourages such issues and problems existed in the sales tax system.
- VAT mobilizes the additional resources and rest of internal resources by broadening tax base and by discouraging the existing tax loopholes.
- For implementation of VAT, the public awareness level relating VAT and VAT administration should be good and it is a prerequisite in the preparation of VAT.

VAT administration should be strong and efficient in order to implement properly. But in Nepal, VAT administration has been facing the problems like corruption, incapability, inefficiency, delaying, ineffectiveness, inadequate physical environment, inexperienced and untrained employee and weak organization set up.

Dhakal Arjun (2000), in his dissertation “VAT and its revenue potential in Nepal”, analyzed the Nepalese tax structure along with the basic emphasis and historical background and potential revenue of VAT in Nepal. The increasing trend of the resources gap of Nepal is forcing the country to debt-trap situation. Domestic resource mobilization through the properly designed tax system is the best way to uplift the situation. In this process, Nepal is adopted the destination based, consumption type VAT operated by the tax-credit method. VAT encourages investment, supports economic growth and keeps price stable.

Exemptions and zero rating reduced the regressivity of VAT; however it makes the administration complex.

Kandel, Laxman (2004), in his dissertation “Revenue collection from VAT in Nepal with problems and prospects”, analyzed the theoretical aspect of VAT with describing the revenue collection from VAT with their problems and prospects. The government expenditure is increasing consciously but revenue resources are very limited which led the country to fiscal crises. In this situation value added tax revenue will play a significant role to increase the revenue of the government.

He has describe in the dissertation that contribution of value added tax revenue to total revenue is in increasing trend which is beneficial for sound economic development. Despite the various difficulties in the implementation of VAT, the collection trend of revenue through VAT is not so bad. It is expected that VAT will generate more and more revenue in the coming days. VAT generated about Rs. 7122.60 millions revenue in fiscal year 1997/98. It reached up to Rs. 11964.00 million in fiscal year 2001/02 which is about 68% increased in comparison to fiscal year 1997/98.

## **CHAPTER – III**

### **RESEARCH METHODOLOGY**

This chapter is dedicated to research methodology applied in the study for the achievement of designed objectives.

#### **3.1 Research Design**

It is an overall framework of plan study for the collection and analysis of data. Descriptive and analytical both the research designs have used to analyze the contribution pattern of VAT from Nepalese Public Enterprises with reference to Nepal Telecom.

To obtain the designed objectives of the study, opinions of the various 35 respondents associated with distinct denominations i.e. tax administrators, tax experts, tax payers, and NTC officials were collected through structured questionnaire. The questionnaire include methods of mobilizing domestic resources, reasons for unsatisfactory contribution of PEs towards public revenue, difficulties in collection of VAT of PEs, NTC contribution to VAT revenue, problems in VAT collection.

### **3.2 Nature and Source of Data**

The data used in this study are both primary and secondary. The sources of primary data are taken from the respondent, field visit and face to face interviews with selected persons included in the purpose sample. To collect the opinion of the respondents, the major tool used in survey research was an opinion questionnaire. The questionnaire was distributed to 45 persons. The questionnaire included the various aspect of value added tax concerning with public enterprises and Nepal Telecom. A total of 35 (77.77%) filed questionnaire were received. Among these 9 (25.71%) were tax administrators, 10 (28.57%) tax experts, 9 (25.71%) tax payers and 7 (20%) were Nepal Telecom officers.

The respondents were asked either to response Yes/No or tick the best answer one or to write their opinion. Some of the respondents gave chosen more than one answer and ranked them respectively. Information received from all of respondent was tabulated into the separate table format and they were presented in percentage of total numbers or points then analyzed into a descriptive way. The respondents were selected four denominations and code was used to represent each denomination in order to make easy the analysis. The following table shows denomination of respondents and code used to represent them.

**Table 3.1**  
**Group of Respondents and Code Used**

<b>S.N.</b>	<b>Denominations</b>	<b>No. of Respondent</b>	<b>Code Used</b>
1	Value added tax experts	10	A
2	Value added tax administrator	9	B
3	Value added tax payers	9	C
4	Nepal Telecom officers	7	D

Source: Field Survey

The major sources of secondary data are as follows;

- ) Economic survey and budget speech of various years Ministry of Finance, Govt. of Nepal
- ) Publication of CEDA, Tribhuvan University
- ) Books related to value added tax
- ) Reports and records of department of Inland Revenue (Taxation), Ministry of Finance, Govt. of Nepal
- ) Books related to public finance and Public Enterprises
- ) National level newspapers, journals, souvenir and news magazines
- ) Various annual report, record of Nepal Telecom

### **3.3 Data Processing and Analysis Procedure**

It is observed that the collected data does not depict the result itself. To draw required conclusion from collected data are classified, tabulated and analyzed in descriptive and analytical way.

For the purpose of analysis generally simple statistical tools have been used which are as follows:

- ) Simple Percentage
- ) Simple Average
- ) Correlation
- ) Graphs Chart and Diagram

## **CHAPTER – IV**

### **DATA PRESENTATION AND ANALYSIS**

#### **4.1 Government Revenue in Nepal**

The sources government revenue is divided into tax revenue and non tax revenue. Tax revenue is composition of custom duty; value added tax, hotel tax, contract tax, land revenue, home and land registration, income tax and other taxes. But non tax revenue is composition of revenue from forest, Dividend, royalty and sales of fixed assets, interest and loan amount, civil administration etc.

In 1952 when the government prepared and presented the budget to the people for the first time in Nepalese history, the revenue structure was typically that of traditional economy with 73% of government's revenue coming from non tax source and land tax. The share of non tax revenue alone was 43% ( Jha, 1984). But now days tax revenue is the most important sources of government revenue that occupies almost 80% share in the total government revenue.

Table no. 5.1 shows the contribution of tax revenue was 78% in the fiscal year 1995/96. The figure in percentage of tax revenue in the total government revenue has been finding fluctuating in different years. But the amount of tax revenue has been increasing in very year. In the fiscal year 1995/96, amount of tax revenue was Rs. 21668.0 million and in fiscal year 2005/06, it was Rs. 72282.0 million.



**Table 4.1**  
**Structure of Nepalese Government Revenue**

(In Rs. Million & Percentage)

<b>Fiscal Year</b>	<b>Total Govt. Revenue</b>	<b>Total Tax Revenue</b>	<b>Total Non Tax Revenue</b>	<b>% of tax Revenue</b>	<b>% of Non Tax Revenue</b>
1995/96	27893.1	21668.0	6225.1	78	22
1996/97	30373.5	24424.3	5949.2	80	20
1997/98	32937.9	25939.8	6998.1	79	21
1998/99	37251.0	28752.9	8498.4	77	23
1999/00	42893.8	33152.1	9741.6	77	23
2000/01	48893.6	38865.1	10028.8	79	21
2001/02	50445.5	39330.6	11115.0	78	22
2002/03	56229.7	42587.0	13642.7	76	24
2003/04	62331.0	48173.0	14158.0	77	23
2004/05	70122.7	54104.7	16018.0	77	23
2005/06	72282.0	57430.4	14851.6	79	21
2006/07	87717.0	71127.0	16590.0	81	19

*Source: Economic Survey, 2007/08*

The trend of non tax revenue collection was also fluctuating during the period of 1995/96 to 2005/06. The amount increase from Rs. 6225.1 million to Rs. 14851.6 million but in fiscal year 1996/97 and 2005/06, the non tax revenue were Rs. 5949.2 million and Rs. 14851.6 million which were Rs. 275.9 million and Rs. 1166.4 million decreased than the revenue of previous fiscal year.

Again, from the fiscal year 1997/98, the non tax revenue has been grown in increasing trend up to 2004/05. Regarding government revenue collection from non tax revenue in fiscal year 2004/05, its contribution in total government revenue is Rs. 16018.0 million. But in fiscal year 2005/06, the amount of non tax revenue is Rs. 14851.6.

## 4.2 Composition of Direct and Indirect Tax on Tax Revenue of Nepal

The structure of the Nepalese tax revenue can be presented in terms of consumption, income and capital based tax. Taxes on consumption are known as indirect tax and taxes on income as well as capital are known as direct taxes. Custom duties, excise duty, value added tax, entertainment tax, hotel tax, air flight tax and road and bridge maintenance tax are included in indirect tax and income tax, land tax, urban house and land tax, vehicle tax, wealth tax and other taxes are included in direct tax.

Composition of direct and indirect tax is presented in table no. 5.2. The table shows that the share of indirect tax is more than the share of direct tax. The contribution of indirect tax and direct tax was Rs. 17012.1 million and Rs. 4655.9 million that is 79% and 21% of total tax revenue respectively in the fiscal year 1995/96. From the fiscal year, 1995/96, the trend in % of indirect tax was declined up to year 1999/00 after that it was in fluctuating trend.

**Table 4.2**

### **Composition of Direct and Indirect Tax on Total Tax Revenue**

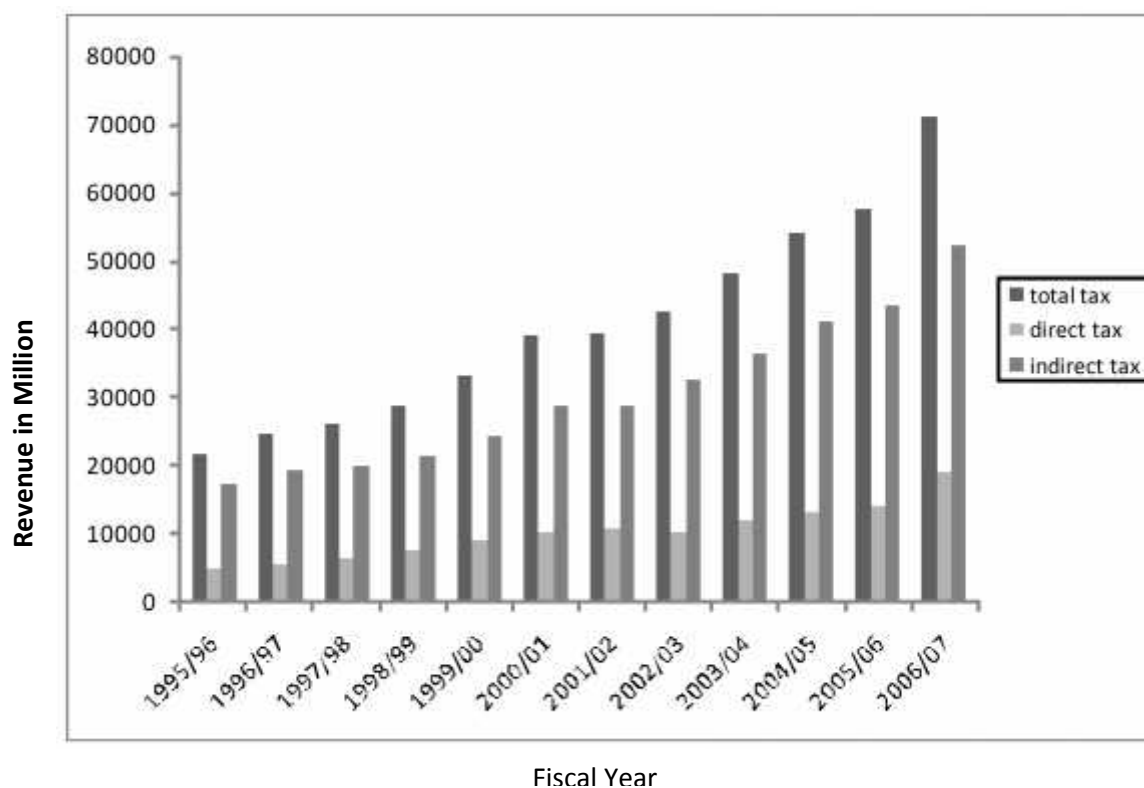
(In Rs. Million and Percentage)

<b>Fiscal Year</b>	<b>Total Tax Revenue</b>	<b>Direct Tax</b>	<b>Indirect Tax</b>	<b>% of Direct tax</b>	<b>% of Indirect Tax</b>
1995/96	21668.0	4655.9	17012.1	21	79
1996/97	24424.3	5340.0	19084.3	22	78
1997/98	25939.8	6187.9	19751.9	24	76
1998/99	28752.9	7516.1	21236.8	26	74
1999/00	33152.1	8951.5	24200.6	27	73
2000/01	38865.1	10159.4	28705.7	26	74
2001/02	39330.6	10597.5	28733.1	27	73
2002/03	42587.0	10105.8	32481.2	24	76
2003/04	48173.0	11912.6	36260.4	25	75
2004/05	54104.0	13071.8	41032.9	24	76
2005/06	57430.4	13968.1	43462.3	24	76
2006/07	71127.0	18980.0	52147.0	27	73

Source: Economic Survey, 2007/08

Figure 4.1

Composition of Direct and Indirect Tax on Total Tax Revenue



The table no. 5.2 reveals that our economy is heavily dependent on indirect tax on comparison with direct tax. Indirect taxation with a dominant role in tax structure could be taken as a symptom of developing country.

To divert the economy in the channel of development, those countries should increase the share of indirect tax. In Nepal, the share of indirect tax is increasing in figure only, but the share of indirect tax in percentage is decreasing in total tax revenue and it is not good symptom of economic development, the share of indirect tax is Rs. 52147.0 millions which has 73% of total tax revenue in the fiscal year 2006/07 whereas in fiscal year 1995/96, the share of indirect tax was Rs. 17012.0 millions which was 79% of total tax revenue. It clearly shows that the indirect tax is increasing in figure but

decreasing in percentage. Therefore, the attention should be focused on the sufficient resource mobilization through indirect tax.

### **4.3 Role of Value Added Tax in National Exchequer**

Likes other developing country, in Nepal more financial resources are needed to meet the increasing expenditure for regular and development activities. The objective of revenue collection is not only to finance growing expenditure but also to achieve other objectives like social justice, regional development, distributive justice etc. For these national goals, the indirect tax basically value added tax is assumed as best weapon because part of the indirect tax is higher than direct tax on total tax revenue. However, role of non-tax revenue in government expenditure can not be neglected.

General trend of value added tax on government tax revenue, total tax revenue and total indirect tax revenue of Nepal.

**Table 4.3**  
**Value Added Tax in National Exchequer**

(Rs. In Millions)

<b>Fiscal Year</b>	<b>GDP</b>	<b>Total Tax Revenue</b>	<b>Total Indirect Tax Revenue</b>	<b>Total VAT Revenue</b>
1998/99	366251	28752.9	21236.8	8765.9
1999/00	393566	33152.1	24200.6	10259.7
2000/01	441519	38865.1	28705.7	12382.4
2001/02	459443	39330.6	28733.1	12267.3
2002/03	492231	42587.0	32481.2	13459.7
2003/04	536749	48173.0	36260.4	14478.9
2004/05	589412	54104.0	41032.9	18885.4
2005/06	654055	57430.4	43462.3	21610.7
2006/007	727089	71127.0	52147.0	26095.6

*Source: Economic Survey, 2007/08*

For the purpose of analysis of the trend of value added tax in Nepal, here demonstrated value added tax in terms of percentage of total govt. revenue, total tax revenue and total indirect tax revenue. The following table shows the figure in percentage

**Table 4.4**  
**Value Added Tax as Percentage of GDP, Total Tax Revenue and Total Indirect Tax Revenue**

(Rs. In millions)

<b>Fiscal Year</b>	<b>VAT as % GDP</b>	<b>VAT as % of total tax revenue</b>	<b>VAT as % of indirect tax revenue</b>
1998/99	2.39	30.49	41.28
1999/00	2.61	30.95	42.39
2000/01	2.80	31.86	43.14
2001/02	2.67	31.19	42.69
2002/03	2.73	31.61	41.44
2003/04	2.70	30.06	39.93
2004/05	3.20	34.91	46.02
2005/06	3.30	37.63	49.72
2006/07	3.59	36.68	50.00

*Source: Economic Survey 2007/08*

#### **(1) Contribution of Value Added Tax to GDP**

Table no.5.4 Shows that the percentage of VAT to GDP from the fiscal year 1998/99 to 2006/07. The above table shows the trend of percentage of VAT to GDP increasing trend up to fiscal year 2000/01. After the fiscal year 2000/01, the percentage of VAT to GDP is decreased in fiscal year 2001/02 i.e. 2.67%. In the fiscal year 2000/01, the percentage of VAT is 2.80% and 2.67%, 2.73% and 2.70% in the fiscal year 2001/02, 2002/03 and 2003/04 respectively. In the fiscal year 2004/05, it is increased to 3.20% and 3.30% and 3.59% in the fiscal

year 2005/06 and 2006/07 respectively. From the table no.5.3 it shows that contribution of VAT to GDP is increased in amount every year. It means contribution of VAT to GDP will increase in coming fiscal year.

## **(2) Contribution of VAT to Total Tax Revenue**

In Nepal, tax structure is totally based on indirect taxes. VAT occupies major portion in total tax revenue. In Nepal, VAT contributes more than one third of total tax revenue. The share of VAT in total tax revenue started to rise continuously from the fiscal year 1998/99 to 2000/01. After the fiscal year 2000/01, percentage of VAT decreased in fiscal year 2001/02 because of political condition. In the fiscal year 2002/03, the percentage of VAT slightly increases to 31.61% from 31.19% in the fiscal year 2001/02. But in the fiscal year 2003/04, the share of percentage decreased to 30.06%. After the fiscal year 2003/04, the share of percentage of VAT increased up to the fiscal year 2006/07. We hope in the coming fiscal year the contribution of VAT to total tax revenue will increase.

## **(3) Contribution of VAT to Indirect Tax Revenue**

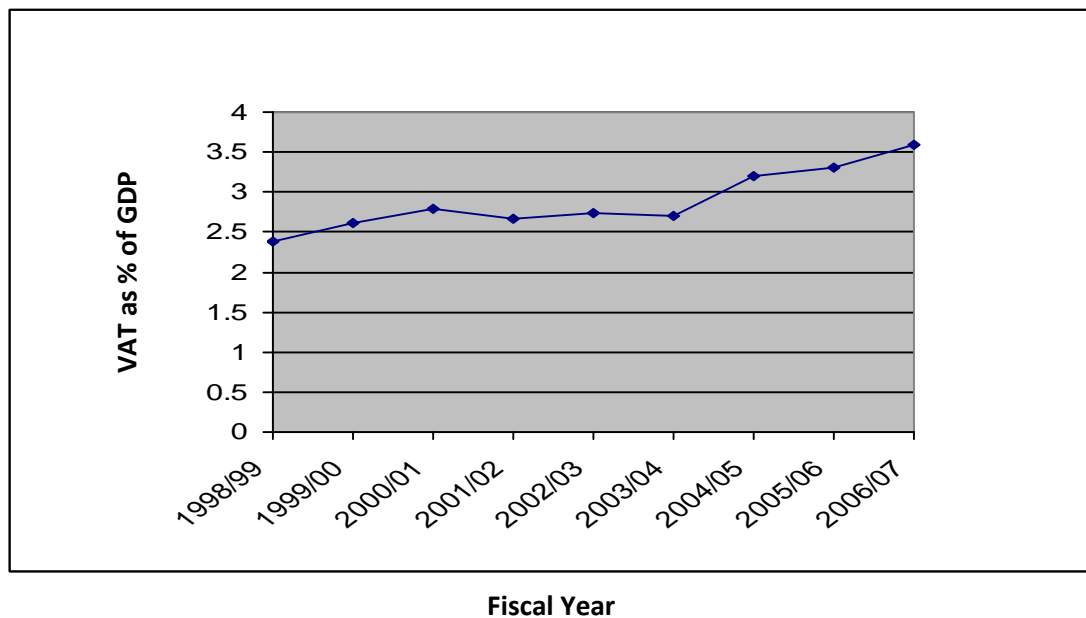
VAT is the most important factor of indirect tax. In Nepal it has been contributing significantly in tax structure. Contribution of VAT to indirect tax revenue was 41.28% in the fiscal year 1998/99. Then it rises almost every year up to fiscal year 2000/01 and after that it decreases slowly via: 42.69%, 41.44% and 39.33% in fiscal year 2001/02, 2002/03 and 2003/04 respectively. The contribution of VAT to indirect tax revenue increases from fiscal year 2004/05 which is 46.02%. The table shows that VAT has contributed almost 50% to indirect tax revenue (i.e. 49.72% in FY 2005/06 and 50% in FY 2006/07) from the fiscal year 2004/05. It is the reason that people have known well about VAT.

Similarly, Nepal has come to peace process which indicates that in the coming fiscal year the portion of VAT to indirect tax revenue will increase.

From table no. 5.3 it can be observed that the trend of VAT revenue is increasing in all respect. And it can be shown in the following figure.

**Figure 4.2**

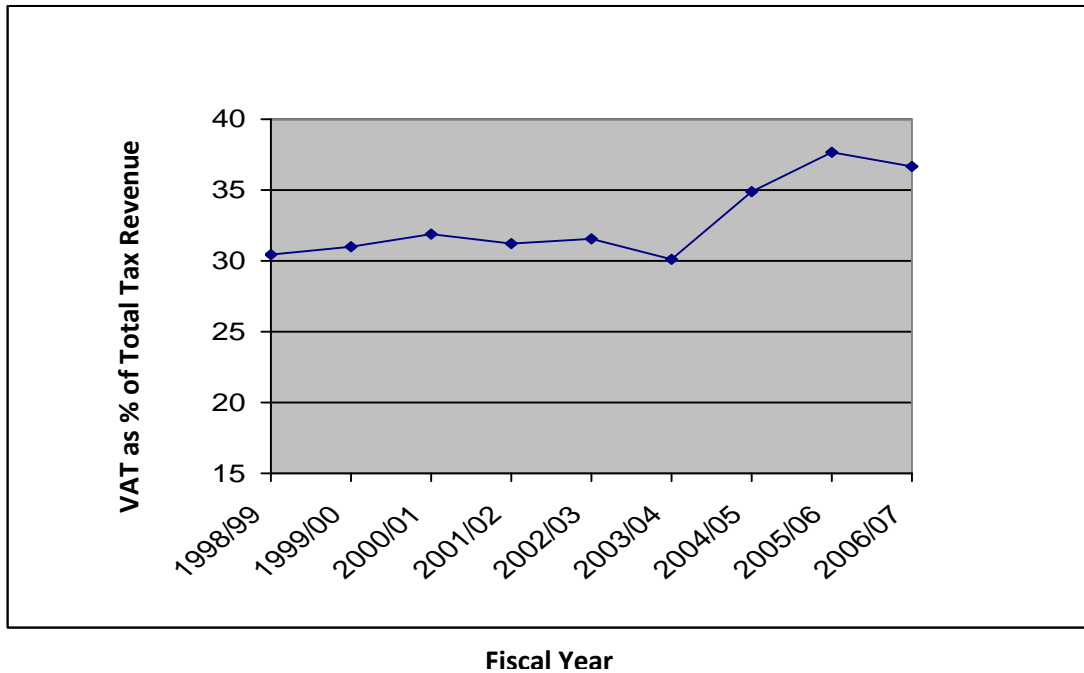
**VAT as a % of GDP Vs Fiscal Year Curve**



Value added tax revenue of Nepal as a percentage of GDP has increased gradually from 2.39% to 3.59% from the fiscal year 1998/99 to 2006/07 with slight deviation.

**Figure 4.3**

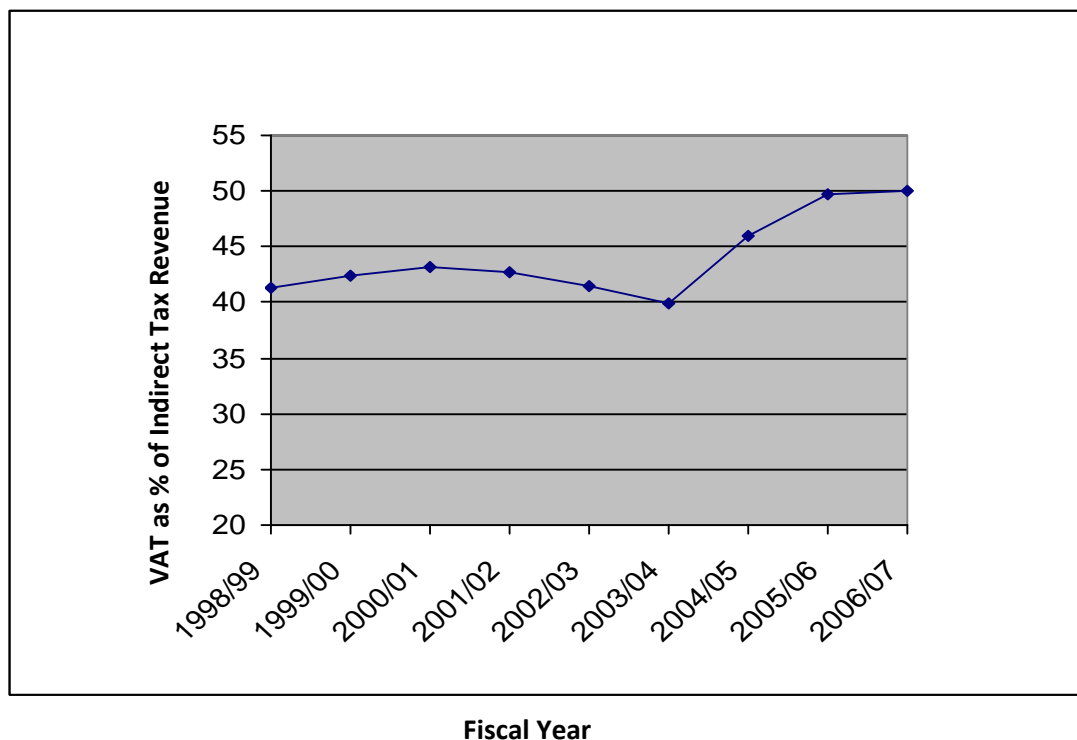
**VAT as a % of Total Tax Revenue Vs Fiscal Year Curve**



Value added tax revenue as a percentage of total tax revenue has increased gradually. It increased from 30.49% to 36.68% in the fiscal year 1998/99 to 2006/07 respectively. But in fiscal year 2001/02 and 2003/04, it decreased by 0.67% and 1.55% from previous year 2000/01 and 2002//03 respectively. Thus, the trend of lines is increasing with slight fluctuations.

**Figure 4.4**

**VAT as a % of Indirect Tax Revenue Vs Fiscal Year Curve**



As a percentage of total indirect tax revenue, it has gradually increased from 41.28% in the fiscal year 1998/99 to 43.14% in the fiscal year 2000/01. But in the fiscal year 2001/02, 2002/03 and 2003/004, it is decreased to 42.69%, 41.44% and 39.93% respectively.

To check the relation between value added tax revenue and other variables, correlation has been used. Since, correlation is a statistical tool that is easy to established mathematical relationship between two or more variables.

Here, the value of correlation has been computed by calculator.

### **Relation between GDP (at current price) and Total VAT Revenue**

Correlated value of two variables GDP (at current price) and Total VAT revenue is 0.991, where  $r = 0.991 < +1$ . The value is nearer to +1. Therefore, there is perfect positive correlation between GDP (at current price) and Total VAT Revenue. Therefore, it is concluded that GDP (at current price) have increased with an increase in Total VAT Revenue.

### **Relation between Total Tax revenue and Total VAT Revenue**

The value of correlation between Total Tax Revenue and Total VAT Revenue is 0.979. Since,  $r=0.979 < +1$ , so there is high degree of positive correlation between Total Tax Revenue and Total VAT Revenue. Thus, high degree of correlated value implies that with increment of Total VAT Revenue, Total Tax Revenue goes on rising.

### **Relation between Total Indirect Tax Revenue and Total VAT Revenue**

Computed value of correlation of Total Indirect Tax Revenue and Total VAT Revenue 'r' is 0.986. It is also less than +1. So there is high degree of positive correlation between Total Indirect Tax Revenue and Total VAT Revenue. Thus, we concluded that the increase in Total VAT Revenue increase the Total Indirect Tax Revenue.

### **4.4 Value Added Tax Revenue from Nepal Telecom**

Operating profit of Nepal Telecom has been Rs. 5980 millions in FY 2063/64 (Economic Survey 2064/65). Revenue of Nepal Telecom is increasing every year. It was Rs. 8875 millions in the fiscal year 2059/60 and Rs. 11059 millions in the fiscal year 2062/63. On the other hand net profit before tax was Rs. 4551 millions in the fiscal year 2059/60 and Rs. 6844 millions in the fiscal year 2062/63. Value added tax is also increasing. At present, most of the PEs has net operating losses; Nepal Telecom is looking successful public enterprises because it is operating under net profit position. Nepal Telecom is providing royalty, dividend, interest, income tax, value added tax and other taxes. Nepal Telecom is providing value added tax revenue Rs. 433 millions in the fiscal year 2059/60. Similarly, Nepal telecom has paid value added tax to government of Rs. 809.4 millions in the fiscal year 2063/63 and Rs. 1123.6 millions in the fiscal year 2063/64.

Revenue collection from value added tax of Nepal Telecom by government of Nepal plays a very much vital role in Nepal. Thus value added tax revenue from Nepal Telecom comes under the head of indirect tax revenue of government of Nepal. Value added tax is an important and reliable source of government revenue. Nepal Telecom's contribution is increasing every year with some ups and down.

**Table 4.5**  
**Value Added Tax Revenue from Nepal Telecom**  
**(Rs. In Millions)**

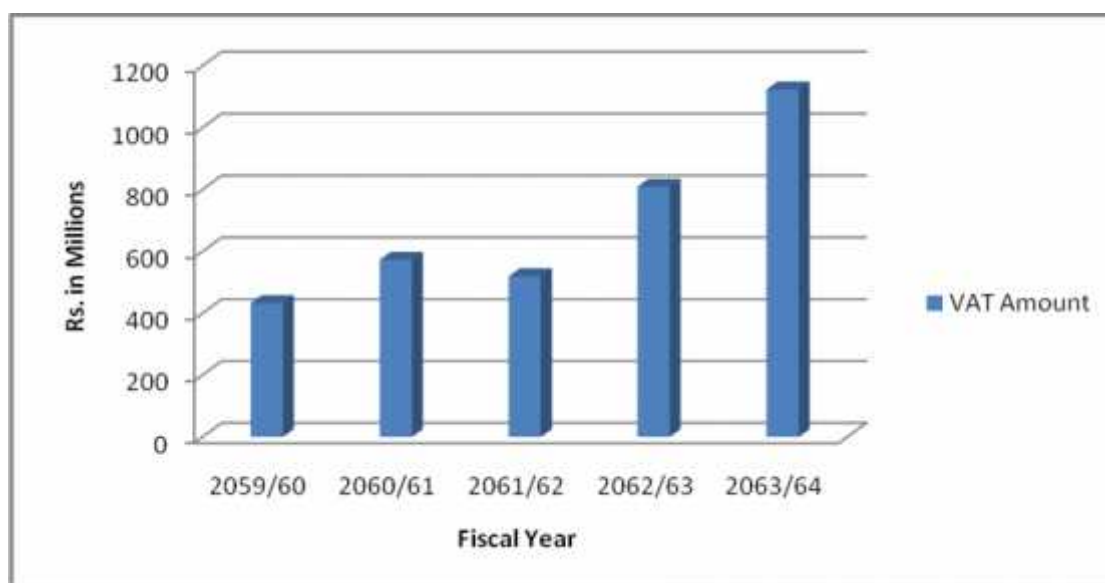
Fiscal Year	VAT Amount
2059/60	433.1
2060/61	572.7
2061/62	519.5
2062/63	809.4
2063/64	1123.6

*Source: Account dept. of NTC*

From the above table we know that contribution of value added tax revenue from Nepal Telecom is increasing year by year except the fiscal year 2061/62. The value added tax revenue in the fiscal year 2060/61 is amounted Rs. 572.7 millions but in the fiscal year 2061/62, it is decreased to amount Rs. 519.5 millions. But after the fiscal year 2061/62, it is increasing trend. In the fiscal year 2062/63, the contribution of Value added tax is amounted Rs. 809.4 millions and Rs. 1123.6 millions in the fiscal year 2063/64. We hope the contribution of value added tax from NTC will increase in the coming fiscal year. In the fiscal year 2063/64, Nepal Telecom has paid large amount of tax. NTC is the only one high tax payer to the government.

**Figure 4.5**

### Contribution of Value Added Tax from NTC



From the above figure we know that value added tax revenue from Nepal Telecom is increasing trend except the fiscal year 2061/62. After the fiscal year 2061/62, contribution of value added tax to government is increased 809.4 million in 2062/63 and 1123.6 million in the fiscal year 2063/64.

#### 4.5 Contribution of Value Added Tax from Nepal Telecom in GDP

Value added tax revenue from Nepal Telecom has been collecting every year by Government of Nepal. Total GDP is increasing every year. Even though value added tax from Nepal Telecom is contributing a little part of total GDP, it is contributing regularly. The following table shows the proportion of value added tax from Nepal Telecom on total GDP of Nepal.

**Table 4.6**

#### **Contribution of Value Added Tax from Nepal Telecom in GDP**

(Rs. In Millions and Percentage)

<b>Fiscal Year</b>	<b>Total GDP</b>	<b>Value Added Tax from Nepal Telecom</b>	<b>% of Value Added Tax from Nepal Telecom</b>
2059/60	492231	433.1	0.088
2060/61	536749	572.7	0.107
2061/62	589412	519.5	0.088
2062/63	654055	809.4	0.124
2063/64	727089	1123.6	0.155
Average	599907.2	691.66	0.115

*Source: Economic Survey 2064/65 and Report of Nepal Telecom*

The average contribution of value added tax from Nepal Telecom in national revenue (GDP) is only 0.115%. The contribution of value added tax from Nepal Telecom in national revenue is just 0.088% in the fiscal year 2063/64. The trend of value added tax from Nepal Telecom is increasing except the fiscal year 2061/62. In the fiscal year 2060/61, the percentage contribution by Nepal Telecom was 0.107% then it is decreased to 0.088% in the fiscal year 2061/62. But after this, it is started to rise up. Thus the amount of value added tax revenue is increasing every year. National revenue (GDP) is increasing drastically every year where value added tax revenue from Nepal Telecom is also increasing soft and slow manner.

### **Relation between National Revenue (GDP) and Value Added Tax from Nepal Telecom**

Correlated value of National revenue and value added tax revenue from Nepal Telecom is 0.943. Since  $r=0.943 < +1$  means less than one, so there is high degree of positive correlation between national revenue and value added tax revenue from Nepal Telecom. We may therefore, conclude that in general, total national revenue have increased with an increase in value added tax revenue from Nepal Telecom.

#### 4.6 Contribution of VAT from Nepal Telecom in Total Tax Revenue

Tax revenue includes consumption, income and capital based taxes. The following table shows the contribution of value added tax from Nepal Telecom in Total Tax revenue.

**Table 4.7**  
**Contribution of VAT from Nepal Telecom in Total Tax Revenue**

(Rs. In Millions and Percentage)

<b>Fiscal Year</b>	<b>Total Tax Revenue</b>	<b>Value Added Tax from Nepal Telecom</b>	<b>% if Value Added Tax from Nepal Telecom on Total Tax Revenue</b>
2059/60	42857.0	433.1	1.01
2060/61	48173.0	572.7	1.19
2061/62	54104.7	519.5	0.96
2062/63	57430.4	809.4	1.41
2063/64	71127.0	1123.6	1.58
Average	54738.42	691.66	1.26

*Source: Economic Survey 2064/65 and Report of Nepal Telecom*

The above table shows the position of value added tax from Nepal Telecom in total tax revenue of Nepal. The contribution of value added tax from Nepal Telecom was recorded 1.01% in the fiscal year 2059/60. The percentage contribution by Nepal Telecom in value added tax revenue is increasing except the fiscal year 2061/62. The contribution of value added tax revenue from Nepal Telecom the fiscal year 2060/61 is 1.19% and 0.96% in the fiscal year 2061/62. The average contribution of value added tax from Nepal Telecom in total tax revenue is 1.26%. The percentage contribution by Nepal Telecom was 0.96% in the fiscal year 2061/62 but after that it was increased to 1.41% in the fiscal year 2062/63 and 1.58% in the fiscal year 2063/64.

#### **Relation between Total Tax Revenue and Value added Tax Revenue from Nepal Telecom**

Computed correlation value of total tax revenue and value added tax revenue from Nepal Telecom is 0.942. Since  $r=0.942 < +1$  so, there is high degree of positive correlation between total tax revenue and value added tax revenue from Nepal Telecom. Therefore, we conclude that total tax revenue have increased with an increase in value added tax revenue from Nepal Telecom.

#### **4.7 Contribution of VAT from Nepal Telecom in Indirect Tax Revenue**

Indirect tax is contributing significantly in our tax structure. In developed countries, indirect tax plays a vital role. In Nepal, the indirect tax has dominated direct tax. Direct tax cannot generate more revenue because of the low level of income and standard of living in the country. According to economic survey conducted by ministry of finance, there is greater contribution of value added tax in indirect tax of Nepal. The composition of value added tax from Nepal Telecom in indirect tax revenue is mentioned below.

**Table 4.8**

#### **Contribution of VAT from Nepal Telecom in Indirect Tax Revenue**

(Rs. In Millions and Percentage)

<b>Fiscal Year</b>	<b>Indirect tax</b>	<b>Value Added Tax from NTC</b>	<b>VAT from NTC as % Indirect Tax</b>
2059/60	32481.2	433.1	1.33
2060/61	36260.4	572.7	1.58
2061/62	41032.9	519.5	1.27
2062/63	43462.3	809.4	1.86
2063/64	52147.0	1123.6	2.15
Average	41076.76	691.66	1.68

*Source: Economic Survey 2064/65 and Report of Nepal Telecom*

The above table reveals the position of value added tax from Nepal Telecom in indirect tax revenue of Nepal. The average contribution of value added tax from Nepal Telecom is 1.68%. The trend of value added tax from Nepal Telecom is increasing except the fiscal year 2061/62. The percentage

contribution of value added tax from Nepal Telecom in the fiscal 2060/61 was 1.58% and 1.27% in the fiscal year 2061/62. After the fiscal year 2061/62, it is started to increase and went up to 1.86% in the fiscal year 2062/63. Above figure shows that the value added tax from Nepal Telecom has a significant importance in total indirect tax revenue.

### **Relation between Indirect Tax Revenue and Value Added Tax Revenue from Nepal Telecom**

Computed correlated value indirect tax revenue and value added tax revenue from Nepal Telecom is 0.932. Since  $r=0.932 < +1$ , means less than one, so there is high degree of positive correlation between indirect tax revenue and value added tax revenue from Nepal Telecom. Therefore, Indirect tax revenue increases with an increment in value added tax revenue from Nepal Telecom.

### **4.8 Contribution of VAT from Nepal Telecom in Value Added Tax Revenue**

Almost every year, the role and importance of value added tax in our country has been increasing. So area of the value added tax is going to increase. Nepal Telecom is a corporation. Nepal Telecom is only the corporation which pays highest volume of value added tax to the government of Nepal among the other corporation. The following table shows the contribution of value added tax from Nepal Telecom in total value added tax revenue of Nepal.

**Table 4.9****Contribution of VAT from Nepal Telecom in Value Added Tax Revenue**

(Rs. In Millions and Percentage)

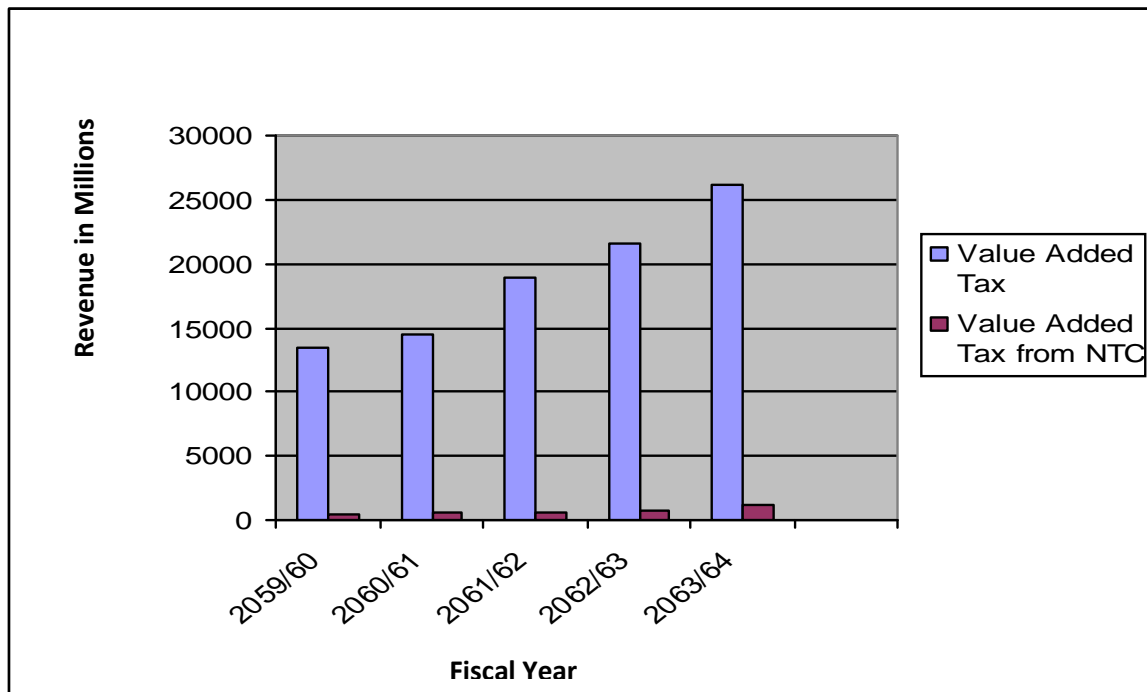
<b>Fiscal Year</b>	<b>Value Added Tax</b>	<b>Value Added Tax from NTC</b>	<b>VAT from NTC as % of VAT</b>
2059/60	13459.7	433.1	3.22
2060/61	14478.9	572.7	3.96
2061/62	18885.4	519.5	2.75
2062/63	21610.7	809.4	3.75
2063/64	26095.6	1123.6	4.31
Average	18906.06	691.66	3.66

*Source: Economic Survey 2064/65 and Report of Nepal Telecom*

The table shows the contribution of value added tax from Nepal Telecom in total value added tax revenue of Nepal. The average percentage contribution by value added tax from Nepal Telecom in total value added tax revenue is 3.66%. The percentage of value added tax from Nepal Telecom in total value added tax revenue was varied from 2.75% to 4.31%. In the fiscal year 2061/61 the percentage contribution by value added tax from Nepal telecom was 3.96% after that the percentage contribution was 2.75% in the fiscal year 2061/62 but again in fiscal year 2062/63 and 2063/64, it increased to 3.75% and 4.31% respectively. So we can say that the percentage contribution of Nepal Telecom in total value added tax revenue is increasing.

Figure 4.6

Contribution of VAT from NTC in Value Added Tax Revenue



Above figure shows that contribution of value added tax from Nepal Telecom in value added tax revenue. Contribution of value added tax from Nepal Telecom is increasing. When it is calculated in percentage contribution, in the fiscal year 2063/64, it is 4.31% of total value added tax revenue.

**Relation between Value Added Tax Revenue and Value Added Tax Revenue from Nepal Telecom**

Correlated of value added tax revenue and value added tax revenue from Nepal Telecom is 0.924. Since  $r=0.924 < +1$  so there is high degree of positive correlation between value added tax revenue and value added tax revenue from Nepal Telecom. Therefore value added tax revenue increases with increment in value added tax revenue from Nepal Telecom.

**4.9 Empirical Investigation**

An empirical investigation has been conducted to find out different aspect of Nepalese value added tax and Public Enterprises value added tax imposition in

Nepal. The major tool used in survey research was an opinion questionnaire. The questionnaire was distributed to 45 persons. The questionnaire included the various aspect of value added tax concerning with public enterprises and Nepal Telecom. A total of 35 (77.77%) filed questionnaire were received. Among these 9 (25.71%) were tax administrators, 10 (28.57%) tax experts, 9 (25.71%) tax payers and 7 (20%) were Nepal Telecom officers.

The respondents were asked either to response Yes/No or tick the best answer one or to write their opinion. Some of the respondents gave chosen more than one answer and ranked them respectively. Information received from all of respondent was tabulated into the separate table format and they were presented in percentage of total numbers or points then analyzed into a descriptive way. The respondents were selected four denominations and code was used to represent each denomination in order to make easy the analysis. The following table shows denomination of respondents and code used to represent them.

**Table 4.10**  
**Denominations of Respondents and Code**

S.N.	Denominations	Code used
1	Value added tax experts	A
2	„ „ „ administrators	B
3	„ „ „ payers	C
4	Nepal Telecom officers	D

### **Views on Value Added Tax as a Suitable Means of Rising Domestic Resource**

In order to know whether value added tax as suitable means of rising domestic resource, a question was asked, “In your opinion, is the value added tax a suitable means of rising domestic resource in Nepal?” The responses received from respondents are tabulated as follows.



**Table 4.11**

**Views on Value added tax as a suitable means of raising domestic resources**

<b>Respondents\Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	10	9	6	7	32	91.43
No	0	0	3	0	3	8.57
Total	10	9	9	7	35	100

*Source: Opinion Survey*

From the table no.5.14.2 we can found that the most of value added tax as a suitable means of domestic resource for raising revenue but some respondents do not recognize value added tax a suitable means of domestic resource mobilization. Thus the conclusion can be drawn that the value added tax is a suitable means of raising government revenue.

**Views on Soundness and Effectiveness of Value Added Tax System of Nepal**

The most effective part of value added tax system is its effectiveness and soundness. To know about the soundness and effectiveness of value added tax system a question was asked, “Do you think that the value added tax system of Nepal is sound and efficient?” the responses received from respondents are tabulated as follows.

**Table 4.12**

**Views on Soundness and Effectiveness of value added tax system of Nepal**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	7	2	1	1	11	31.43
No	3	7	8	6	24	68.57
Total	10	9	9	7	35	100

*Source: Opinion Survey*

There was 100% response received from the respondents. Majority of the respondents are disagreeing with sound and effectiveness of value added tax system of Nepal. 65.57% of total respondents are unsatisfied. Only 31.43% are satisfied with the sound and effectiveness of value added tax system of Nepal. As the corollary to the easier question was asked, “What is the major problem on value added tax system of Nepal?” the respondents, who said problem in the value added tax system, indicated the following problems;

- ) Value Added Tax Billing
- ) Narrow Tax Base/Coverage
- ) Smuggling, Under valuation and Unauthorized trade
- ) Weak Tax Administration
- ) Weak Public Consciousness Level
- ) Geographical Barrier

*Source: Opinion Survey*

From the above table we say that inadequate government economic policy is the main cause for unsatisfactory of soundness and effectiveness of value added tax of Nepal. Complexity in value added tax policy rules and regulation is second cause that effect in soundness and effectiveness of value added tax system of Nepal. After that lack of honesty, trained and competent tax personnel and lack of knowledge about value added tax to tax payers respectively are the min causes for unsatisfactory of soundness and effectiveness of value added tax system of Nepal. The other reason is the last cause in soundness and effectiveness of value added tax system of Nepal.

### **Views on Superiority of VAT Over Sales Tax**

VAT, a latest development of sales tax system is new innovation in the field of taxation. VAT is being preferred by many countries of the world, is superior over sales tax system. Without comparison with sales tax we can not say ‘VAT

is superior to other sales tax system.’ With base to effective revenue mobilization, the tackle to all tax evasion, wide tax base, transparent, value added tax is considered as superior than sales tax. The survey result on this aspect is summarized in the table below.

**Table 4.13**  
**Views on Superiority of Value Added Tax Over Sales Tax**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	10	9	6	6	31	88
No	-	-	3	1	4	12
Total	10	9	9	7	35	100

*Source: Opinion Survey*

According to opinion survey, 100% responses were received from the respondents. Majority of the respondents were said that value added tax is superior to sales tax i.e. 88% of total respondents. Only 12% of total respondents were said that value added tax is not superior to sales tax. The outcome proof that value added tax is superior to other sales tax system on the aspect of revenue mobilization, coverage, broaden tax base, transparent. But its superiority depends upon the strength of value added tax administration. So the value added tax administration is strong, then the success of value added tax system will prove its superiority.

#### **Views on future prospect of VAT in Nepal**

The observation on international experience of VAT is advantages to the revenue mobilization and the strong administration. However, nothing can be said about the possible results and effective until the implementation of VAT will start properly in Nepal.

The smuggling trade level is at peace point, which is creating the parallel economy as a challenge to the national economy, the tax leakage is at higher magnitude, the tax base of sales tax system is narrow and revenue collection is at the lower advantages. However, without proper implementation, there is big doubt whether VAT will be advantages in future or not. So during opinion survey, I asked “Do you think, future prospect of VAT in Nepal is bright?”

**Table 4.14**  
**Views on Future Prospect of VAT in Nepal**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	10	9	6	5	30	86
No	-	-	3	2	5	14
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

Among 35 respondents, questionnaire are distributed for ten tax experts, nine tax administrator, nine tax payers and seven NTC officers. From the above table it shows that hundred percent tax experts are in favour of bright future of VAT in Nepal, hundred percent tax administrators are in favour of bright future of VAT in Nepal, but sixty-seven percent of tax payers think that future prospect of VAT in Nepal is bright and thirty-three percent tax payers don't think that and seventy-one percent of NTC officers think that future prospect of VAT is bright but twenty-nine percent don't think so. From above survey, it shows that 86% of total respondents think that future prospect of VAT in Nepal is bright but 14% of the respondents don't think so.

At last, from the above field survey, it is concluded that future of VAT is bright in Nepal because as much as most of the respondents are in favour of sound future of VAT in our country Nepal.

### **Views on Single Rate of VAT 13% is effective**

VAT rate is very significant and sensitive for revenue mobilization. The source of VAT system upon the degree of VAT rate. Earlier VAT rate is subject to 10% which was below than sales tax 15%. But VAT rate is increased from 10% to 13% from the fiscal year 2062/63. VAT was expected to have a greater revenue yield on percent rate structure. However, this expectation is not achieve in practice basically due to its weak implementation aspect. In such situation field survey was conducted to identify the effectiveness of VAT at 13%. In during field survey, I asked the respondents “Do you think, single rate of VAT 13% is effective?”

**Table 4.15**

#### **Views on single rate of VAT 13% is effective**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	8	8	4	5	25	71
No	2	1	5	2	10	29
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

From the above table it seems that 8 tax experts out of 10 tax experts think that single rate of VAT 13% is effective but 2 tax experts think single rate of VAT 13% is not effective. Similarly 8 tax administrators out of 9 tax administrator, 4 tax payers out of 9 tax payers and 5 NTC officers out of 7 NTC officers think that single rate of VAT 13% is effective but 1 tax administrator out of 9, 5 tax payers out of 9 and 2 NTC officers out of 7 think single rate of VAT 13% is not effective.

From field survey, it is concluded that 71% of total respondents think single rate of VAT 13% is effective but 29% think single rate of VAT 13% is not effective.

### **Views on Existing Tax Structure of VAT**

Tax structure which covers basically base, rate coverage, exemptions etc. is one of the important aspects of the successful operation of VAT in any economy. The tax structure of VAT in Nepal is designed on the VAT Act 1996 and different laws and regulations are prepared in successive years. The field survey has been conducted to find out whether the existing tax structure is appropriate or not. I asked the respondents that “Do you think, the existing tax structure is appropriate?” The findings of this survey can be presented in the following table.

**Table 4.16**  
**Views on the Existing Tax Structure of VAT**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	3	2	3	2	10	29
No	7	7	6	5	25	71
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

Above field survey shows that 3 tax experts, 2 tax administrators, 3 tax payers and 2 NTC officers from out of 10 tax experts, 9 tax administrators, 9 tax payers and 7 NTC officers provide their view the existing tax structure is ok. But 7 tax experts, 7 tax administrators, 6 tax payers and 5 NTC officers provide their opinion on the existing tax structure of VAT is no and has to be improved. Out of total respondents, 29% think the existing tax structure of VAT is appropriate whereas 71% of total respondents think that the existing tax structure is not appropriate.

### **Views on Current Legal Provision and Rules of VAT**

Before the implementation of VAT, the government has prepared VAT Act 2052 B.S. and VAT regulation 2053 B.S. But the legal provision of rules, in general difficult to understand by all. The document of these enactment carry all the matters such as VAT administration and its operation, the tax officers, and its authorities, tax payers and responsibility, the procedure of VAT collection, identification of new tax payers, monitoring, cores checking, penalties and punishment. The field survey has been conducted to find out whether the present act and regulation are sufficient or not with reference to current system of VAT. I asked the respondents, “Do you think, the present act and regulation are sufficient?” The outcome/ attitude of the respondents on this aspect are presented in the table below.

**Table 4.17**  
**Views on Sufficient of Legal Provision and Rules of VAT**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	10	9	2	2	23	66
No	-	-	7	5	12	34
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

From the above table it shows that 66% of total respondents think that present act and regulation are sufficient whereas 34% of the respondents don't think that present act and regulation are sufficient. From the field survey I found that 10 tax experts, 9 tax administrators, 2 tax payers and 2 NTC officers out of 10 tax experts, 9 tax administrators, 9 tax payers and 7 NTC officers think present rules and regulation are sufficient but 7 tax payers and 5 NTC officers think the present rules and regulation is not sufficient.

### **Views on Effectiveness and Satisfaction of Contribution of VAT from Nepal Telecom**

In order to know the effectiveness and satisfaction of value added tax revenue from Nepal Telecom a question was asked “Do you think that contribution of value added tax from Nepal Telecom is effective and satisfactory?” The following table shows the response of the respondents regarding effectiveness and satisfaction of value added tax revenue from Nepal Telecom.

**Table 4.18**

**Views on Effectiveness and Satisfaction of Contribution of Value Added  
Tax Revenue from Nepal Telecom**

<b>Respondent/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	8	7	6	7	28	80
No	2	2	3	-	7	20
Total	10	9	9	7	35	100

*Source: Opinion Survey*

From the above table, it shows that 80% of total respondents think that the contribution of VAT from Nepal Telecom is effective and satisfactory whereas 20% of the total respondents think the contribution of VAT from Nepal Telecom is not effective and satisfactory.

**Views on Problem in VAT Collection from Nepal Telecom**

A question “have you found any problem in value added tax collection from Nepal Telecom?” was asked to know the problem and the response received on it is as follows.

**Table 4.19**

**Views on Problem in VAT Collection from Nepal Telecom**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	2	1	3	-	6	17
No	8	8	6	7	29	83
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

From the above table, it shows that 83% of total respondents think that there is no problem in VAT collection from Nepal Telecom. But, whereas 20% of the

total respondents think that there is problem in VAT collection from Nepal Telecom.

### **Views on Contribution of VAT from Nepal Telecom to National Revenue**

In order to know the contribution of value added tax revenue from Nepal Telecom to GDP a question was asked “Do you think that contribution of value added tax from Nepal Telecom to GDP is satisfactory?” The following table shows the response of the respondents regarding satisfaction of value added tax revenue from Nepal Telecom to GDP.

**Table 4.20**

#### **Views on Contribution of VAT from Nepal Telecom to National Revenue**

<b>Respondents/Response</b>	<b>A</b>	<b>B</b>	<b>C</b>	<b>D</b>	<b>Total</b>	<b>Percentage</b>
Yes	9	8	7	7	31	89
No	1	1	2	-	4	11
Total	10	9	9	7	35	100

*Source: - Opinion Survey*

From the above table, it shows that 89% of total respondents think that the contribution of value added tax revenue from Nepal Telecom to National Revenue is satisfactory. But, whereas 11% of the total respondents think that the contribution of value added tax revenue from Nepal Telecom to National Revenue is not satisfactory.

### **4.10 Findings**

- i. VAT has been most essential choice as ingredient of tax reforms of developing countries like Nepal which leads to revenue enhancement and sustainable economic development. There is tremendous scope for increasing the revenue from VAT and sound implementation of VAT will obviously increase its contribution in coming days more.

- ii. The government expenditure is increasing consciously but revenue resources are very limited which led the country to fiscal crisis. So VAT plays significant role to increase revenue.
- iii. Overview of current revenue structure of Nepal, the share of tax revenue has been greater than the share of non tax revenue. About three quarters of total revenue comes through tax revenue and one-third from non tax revenue which shows the dominant role of tax revenue to total revenue. Due to this reason, govt. heavily depends upon tax revenue and the foreign grants and aids, which leads country's situation towards fiscal crisis and resource gap.
- iv. The source of government revenue is divided into two tax revenue and non tax revenue. Tax revenue contributed 81% to government revenue whereas non tax revenue contributed 19% in the fiscal year 2006/07.
- v. Tax revenue is composition of indirect (tax on consumption) and direct tax (tax on income as well as capital). In developing countries like Nepal, indirect tax is significant. Direct tax can not produce more revenue because of low level of income and standard of living of people.
- vi. Indirect tax contribution on total tax revenue is 73% in fiscal year 2006/07 which shows a decreasing trend. After the fiscal year 2005/06 which was 76%. Direct tax contribution on total tax revenue is 21% in the fiscal year 1995/96 and 27% in fiscal year 2006/07 which shows increasing trend.
- vii. Contribution of tax revenue on GDP of Nepal is lower. It was recorded 0.8% in fiscal year 1995/96 and increased to 0.97% in fiscal year 2006/07.
- viii. The contribution of value added tax on total revenue was 30.49% in fiscal year 1998/99 and 36.68% in fiscal year 2006/07 which shows an increasing trend of value added tax contribution.

- ix. Indirect tax revenue includes sales tax, entertainment tax, hotel tax, contract tax, excise duty and other tax. The contribution of value added tax on indirect tax revenue was 41.28% in fiscal year 1998/99 and 50% in fiscal year 2006/07. This shows the value added tax is half of indirect tax revenue.
- x. Nepal Telecom has been contributing effectively to national revenue. It plays vital role in revenue collection. The share of value added tax revenue from Nepal Telecom to GDP is 0.088%, 0.107%, 0.088%, 0.124% and 0.155% in the fiscal year 2002/03, 2003/04, 2004/05, 2005/06 and 2006/07 respectively.
- xi. The share of value added tax from Nepal telecom to total tax revenue is 1.58% in the fiscal year 2006/07. The correlated value 0.942 reveal that 94% variable in value added tax from Nepal Telecom can be explained by total tax revenue.
- xii. The share of value added tax from Nepal Telecom on indirect tax revenue is 2.15% in the fiscal year 2006/07. The correlated value 0.932 reveal that 93% variable in value added tax from Nepal Telecom can be explained by indirect tax revenue.
- xiii. The share of value added tax from Nepal Telecom on total value added tax revenue was 3.22%, 3.96%, 2.75%, 3.75% and 4.31% in the fiscal year 2002/03, 2003/04, 2004/05, 2005/06 and 2006/07 respectively. Only in fiscal year 2004/05, the share of value added tax from Nepal telecom is decreased but in other fiscal year it is increasing.

### **Findings from opinion survey**

- i. Value added tax is a suitable means of raising domestic sources. It may enhance government revenue. 91.43% respondents are agreeing with this.
- ii. Majority of the respondents i.e. 68.57% are disagreeing with sound and effectiveness of value added tax system of Nepal. Major problems in

value added tax was value added tax billing, narrow tax base/coverage, smuggling, under valuation and unauthorized trade, weak tax administration, weak public consciousness level, geographical barrier.

- iii. Value added tax is being preferred by many countries of the world due to superiority to sales tax. With the base of effective revenue mobilization, wide tax base, transparent and easy tackle over tax evasion, VAT is considered as superior than sales tax. 88% of total respondents are thinking that value added tax is superior to sales.
- iv. From the opinion survey, it is concluded that 86% respondents are optimistic about future prospects of value added tax in Nepal is bright.
- v. 71% of total respondents are saying that single rate of value added tax 13% is effective.
- vi. Existing tax rate structure is not appropriate as said by 71% respondents.
- vii. 66% respondents are in favour of present act and regulations are sufficient but 44% respondents said that not sufficient.
- viii. 80% respondents are also in favour of effectiveness and satisfaction of contribution of value added tax revenue from Nepal Telecom.
- ix. 83% of total respondents are not found problem in VAT collection from Nepal Telecom. According to 17% respondents, who found problem.
- x. 89% of total respondents are satisfied on contribution of value added tax from Nepal Telecom to national revenue but 11% are not satisfied saying that it should be increased the contribution of VAT from Nepal Telecom.

## **CHAPTER - V**

### **SUMMARY & CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Summary & Conclusion**

Tax is a compulsory contribution to the government made without reference to a particular benefit received by the tax payer. Taxes are levied primarily to raise revenue for government expenditure. On the basis of its nature, tax can be classified broadly into direct and indirect tax. VAT can be taken as good example of indirect tax. VAT is definitely a new and modern tax system in comparison with other traditional taxes.

Value Added Tax is latest innovation in the field of taxation. Actually, VAT is considered as the most important tax reform in the 21<sup>st</sup> century, which has already been implemented popularly in more than over 125 Countries. VAT is multi-staged; commodity and services based tax which is levied on the value added of business enterprises at different stages of production and distribution. It affects only the added portion of price i.e. the value of goods and services added in various stages of transaction. It has nothing to do with the rest of the prices. Purchasers pay VAT to the sellers and sellers transfer it to government, deducting VAT paid on their business purchases from VAT amount collected from the consumers on their sales. The ultimate burden of VAT is sifted to the consumers. In this system, every person or business firms, which is above threshold limit, should compulsory be registered in VAT office. Registered person/business firms get credit facility on tax paid, on their purchases of raw materials, semi-produced goods and overheads. Small vendors whose annual taxable turnover is below threshold and business firms that deal with exempt goods only need not registration. The firms, below threshold, could be registered voluntarily.

VAT was first implemented in 1954 by the French government. Then, after almost all countries (more than 125 Countries) of the world are being attracted towards this system. Due to some special features such as input tax credit system, based on accounting system, less chances of cascading and pyramiding effect, this system is very popular throughout the world. VAT is self-policing in nature, so there is less probability of tax evasion. VAT plays a neutral role on the methods of production and distribution, which is a basic need for a good tax system. Similarly, the stepwise collection of VAT does not encourage tax evasion.

Developing countries like Nepal; lack of sufficient financial resources is the main constraints for the national economic development. For the developing activity government need sufficient resources and fund. Because of the internal conflict, political instability and global recession, the over all economic activities gradually shrunk and suffering from capital shortage to accelerate the economic growth. There is a sharp rise in the current expenditure of the Nepalese government. Due to the low revenue growth and institutional weakness, there is lack of adequate resources for capital expenditure. To meet the additional capital requirement, Nepalese government can use internal external resources. Internal resources are preferable for sustainable economic development. Nepal has been unable for proper mobilization on internal resources. Thus fiscal deficit of Nepal has been increasing.

To solve the fiscal deficit, tax revenue should play an important role. Tax revenue is the main source of government revenue. In this regard, it is need to raise the tax revenue by widening the tax base, refining the tariff structure at regular intervals. This can contribute to more in revenue mobilization.

Overview of current revenue structure of Nepal, the share of tax revenue has been greater than the share of non tax revenue. About three quarters of total revenue comes through tax revenue and one-third from non tax revenue which shows the dominant role of tax revenue to total revenue. VAT, the largest contributor to the national revenue basket, constitutes more than 40% of total indirect tax revenue. Due to this reason; govt. heavily depends upon tax revenue and the foreign grants and aids, which leads country's situation towards fiscal crisis and resource gap.

VAT system is a new system of taxation for Nepal. Government of Nepal adopted this system since November 16, 1997. The international of introducing VAT was initially expressed in 1992; VAT task force was created in 1993. After several years and preparation, VAT Act was finally passed through parliament in December 1995. VAT become effective through the Finance Bill of 1997. After that, formulation and passage of VAT Act, design of VAT regulations and its final approval preparation of VAT all has been done by Nepali standard. Due to effective VAT Act and regulation make well preparation for VAT in Nepal which has made VAT successful today.

Since Value Added Tax (VAT) has recent approach, it has also much potentiality power to generate revenue than earlier sales tax because it covers broad coverage and all level of production, distribution and sales. Revenue is the crucial element for the government to accomplish operating and development activities. Tax is the major source of revenue. It contributes a significant share in total tax revenue and a little share in GDP in Nepalese context. Revenue mobilization is one of the major concerns for Nepal.

VAT has number of difficulties for its implementation such as lack of public consciousness level, weak tax administration, unauthorized trade, narrow tax base coverage, VAT billing, irresponsible office personnel in VAT offices, lack

of trained and qualified manpower, corrupted nature of VAT personnel etc. to make VAT effective source of government revenue it is required to avoid the problems of its.

In the fiscal year 1995/96, contribution of total tax revenue to government revenue was 78%. In the fiscal year 2006/07, it was 81%. It shows that percentage of total tax revenue to government revenue is increasing. Similarly, total VAT revenue to GDP is 2.39% in fiscal year 1998/99 and 3.59% in the fiscal year 2006/07.

From the study we can also find out that VAT contribution from Nepal Telecom to GDP is 0.115%, to total tax revenue is 1.58%, to indirect tax revenue is 2.15% and to total value added tax revenue is 4.31% in the fiscal year 2006/07.

## **5.2 Recommendations**

On the basis of the findings mentioned above the major areas of recommendation are as follows:

1. An efficient, strong and fair administration is the most crucial for the proper implantation of VAT. But, VAT administration is still weak, traditional, corrupted in nature. In spite of these, there is lack of expertise, well trained and skilled officers in the VAT administration. So, informative programmes such as seminars, training, discussions, should be organized to make the tax officers skilled and capable in their field of job and service minded attitude needs to be developed in the mind of tax officers.
2. The tax administration should be very watchful to prevent any kind of malpractice, fraud and tax evasion. Utmost care should be taken to prevent any kind of bribing and corruption. Tax officials should effectively be monitored.

3. Many rules and regulations of VAT are only limited in papers and they are not seen in practice. All the rules and regulations should be in practice. Government should make effort to discourage under valuation, including purchases of some consignments, which are imported at an unrealistically low value. Audit and investigation system need to be improved and make effective, and strictly penalize those who do not follow the rules. Strict rules should be prepared also for tax officers and it is necessary to take action against these officers who are directly or indirectly involved in collusion and corruption, without any hesitation. Also the reward system should be made effective.
4. VAT is the resource of domestic revenue. It has substituted the old sales tax, household land tax, and in order to make it effective, VAT collection procedure should be made more flexible, convenient and systematic. By making the VAT collection procedure flexible maximum number of the tax payers should be brought within the boundary of VAT.
5. The supreme authority of ruling is in the basis of political leaders and political leaders are corrupt and their activities have enforced the personnel's for committing the corruption. Due to the corrupt mentality of political leaders and the lack of political instability, industrial and business organization have not been able to be established. For this purpose, peace and order should be maintained in the country. So that expected revenue can be collected.
6. Lack of proper billing system, is being the most challenging problem in Nepalese context. So consumers should be well informed to take the real bills which they have to pay and strict warning should be given to business that use to issue false bills/invoices. So issuing invoices for every taxable sells must be made compulsory.
7. There should be effective awareness programs through advertising media for taking invoice for every taxable purchase by consumers. Beside this,

every business firm should compel to patch a notice for consumers in from of counter informing about not forget to take bill.

8. Due to the open border with the neighboring country, illegal transactions have been taking place. Such kinds of transactions have helped for tax cheating. To discourage it, proper supervision and monitoring should be done cross checking is to be done time to time in such places.
9. Monitoring system of the VAT administration is not so effective. Because of this, taxpayers are still encouraged for tax evading practices. Many businessmen don't issue invoice for their selling and even do, follow the other improper invoices. So, an effective and efficient auditing, investigation and monitoring system should be developed.
10. The language of VAT Act should be simple and clear the definition made only should be clearly and well defined which encourage for the VAT payers towards the VAT coverage.
11. About Nepal Telecom, the service of NTC is not so good in now a day. The network problems are facing by the customers. It will lose the customers for Nepal telecom. If NTC lose the number of customers, it will decrease the revenue of NTC and ultimately it will also decrease the VAT revenue of government. So NTC should be solved the network problem.
12. To increase more revenue, NTC should be decreased the charges of services. So that number of customers will increase and it helps to increase the revenue of NTC.

## BIBLIOGRAPHY

- Amatya, Surendra Keshar, Pokhrel, Bihare Binod and Dahal, Rewanta (2004). *Taxation in Nepal*. Kathmandu.
- Bajracharya, P. & Shrestha, B.K. (1983). *Managerial Problem in Public Sector Manufacturing Enterprises in Nepal*. Kathmandu: CEDA
- Bista, Raghu Bir (1999). *Applicability and Feasibility of VAT in Nepal*. A Dissertation Submitted to the Central Department of Economics, T.U.
- Dahal, Madan Kumar (2052). *Review of Tax System*. Kathmandu.
- Dhakal, Arjun (2000). *VAT and its Revenue Potential in Nepal*. An Unpublished Master Degree Dissertation Submitted to the Central Department of Economics T.U.
- Encyclopedia of Management (2002). *Second Edition Harper Collins Publishers*.
- Ghimire, Lal Mani (1998). *VAT: Key Issue in Nepal*. An Unpublished Master Degree Dissertation for Management (MBA) T.U.
- Goode, Richard (1986). *Government finance in Developing Countries*. New Delhi: Tata McGraw Hill Publication Company Ltd.
- Hyman, David N. (1972). *Economic of Government Activity*. New York: Halt, Rirehart and Winstan Inc.
- K.C., Jit Bahadur (2006). *Tax Law and Tax Planning*. Kathmandu: Khanal Books and Stationary.
- Kandel, DR. Puspa Raj (2003). *Tax law and Tax Planning*. Kathmandu: Buddha Academic Publishers and Distributors Pvt. Ltd.
- Kandel, Laxman (2004). *Revenue Collection from VAT in Nepal with Problems and Prospects*. An Unpublished Master Degree Dissertation, T.U.
- Khadka, Rup Bahadur (1989). *VAT in Asia and Pacific Region*. Amsterdam: International Bureau of Fiscal Documentation.
- Khadka, Rup Bahadur (1991). *Nepalese Taxation: A Path for Reform*. Service. Germany: Alenauer Von Humbold Foundation.

- Khadka, Rup Bahadur (1993). *A Review of Nepalese Sales Tax International Bureau of fiscal Documentation VT Monitor*. Asthenia
- Khadka, Rup Bahadur (1995). *Probability of VAT in Nepal*. Rastra Bank Samachar, Nepal Rastra Bank, Kathmandu, Pp. 22-28
- Khadka, Rup Bahadur (1996). *A Report on The Government Tax System: Study Tour*. Kathmandu: Urban Development through Local Efforts.
- Khadka, Rup Bahadur (1996). *A VAT for Nepal*. International Bureau of Fiscal Documentation.
- Khadka, Rup Bahadur (2000). *The Nepalese Tax System*. Kathmandu: Sajha Prakashan.
- Lent, George E. (1973). *Value Added Tax in Developing Countries*. Washington D.C: IMF, Fiscal affairs Development.
- Margaret Nicholson (1989). *Accounting Skills*. New York: Mac Milan Education Ltd.
- Mathur, B.P. (1993). *Public Enterprises Management*. New Delhi: Mac Milan Publishing Company
- Michele Guerard (1973). *Brazilian VAT System*. An Unpublished Dissertation Submitted to Columbia University, USA.
- Ministry of Finance (2005/06 - 2006/07). *Economic Survey*. Kathmandu.
- Musgrave, R.A. & Musgrave, P.B. (1976). *Public Finance in Theory and Practice*. Tokyo: McGraw Hill.
- Nepal Telecom (2007). *Annual Report*. Kathmandu: Nepal Telecom.
- Pant, Prem Raj & Wolf, Howard K. (1970). *Social Science Research and Thesis*. Kathmandu: Buddha Academic Publishers & Distribution Pvt. Ltd.
- S.C. Won Chang and Mc. Lourdes B. Recente (1988). *The VAT Experience in Republic of Korea*. Asia Pacific Tax and Investment Research Center and Asian Development Bank.

- Sharma, Chinta Mani (1998). *Value Added Tax In Nepal: An Administrative and Policy Issues*. An Unpublished Dissertation Submitted to the Central Department of Management, T.U.
- Sharma, M. L. (1994). *C.A. Foundation Course*. New Delhi: S. Chand & Company Ltd.
- Shoup, Carl S. (1969). *Public Finance*. London: Wide Field and Nicholson,
- Shoup, Carl S. (1998). *Value Added Tax and Developing Countries*. Research Observer, The Washington D.C.: World Bank Vol.3, No.2.
- Shout, D.K. (1973). *Value Added Taxation and Growth*. R.W. Houghton Public Finance Selected Reading, Harmondsworth, London: Penguin.
- Shrestha, Purenshowar (1990). *Public Enterprises Management in Nepal*. Kathmandu: Ratna Pustak Bhandar.
- Silwal, Narayan P. (2002). *Value Added Tax (VAT): A Nepalese Experience*. Kathmandu.
- Subedi, Babu Ram (1997). *Applicability of VAT in Nepal*. An Unpublished Master Degree Dissertation Submitted to the Central Department of Economics T.U.
- Thapa, Govinda Bahadur (1994). *Value Added Tax in Nepalese Context*. **Mirmire**. Banker's Club, Kathmandu: Nepal Rastra Bank.
- Thapa, Govinda Bahadur *Implementation of VAT in Nepal*.
- Tripathy, Narayan (1985). *Value Added Tax, its Potential, Problem and Recommendation*. An Unpublished Master Degree Dissertation Submitted to T.U.

## QUESTIONNAIRES

Please tick (Right Sign) the answer of your choice or wherever appropriate put in order of preference from first to last number on the basis of numbers of alternatives.

**Name:-**

**Office / Organization:-**

**Designation:-**

**Occupation:-**

1. In your opinion, is the value added tax a suitable means of raising domestic resource in Nepal?

a) Yes (    )                      b) No (    )

2. Do you think, that the value added tax of Nepal is sound and efficient?

a) Yes (    )                      b) No (    )

3. Do you think, that value added tax is superior to sales tax?

a) Yes (    )                      b) No (    )

4. Do you think, future prospect of VAT in Nepal is bright?

a) Yes (    )                      b) No (    )

5. Do you think, single rate of VAT 13% is effective?

a) Yes (    )                      b) No (    )

6. Do you think, the existing tax structure is appropriate?

a) Yes (    )                      b) No (    )

7. Do you think, the present act and regulation are sufficient?

a) Yes (     )            b) No (     )

8. Do you think, that contribution of value added tax from Nepal Telecom is effective and satisfactory?

a) Yes (     )            b) No (     )

9. Have you found any problem in value added tax collection from Nepal Telecom?

a) Yes (     )            b) No (     )

10. Do you think, that contribution of value added tax from Nepal Telecom to national revenue is satisfactory?

a) Yes (     )            b) No (     )



