

# CHAPTER - 1

## INTRODUCTION

### 1.1 Background

The word tax simply denotes the certain charge that to be paid to the government in lieu of economic involvement with the legal obligation both tax experts and tax employees. It is the obligation of the tax payers in the sense that is their duty to pay tax on profit. They make and the obligation of tax administrators lays the duties and responsibilities to assess and collect the tax according to the support under certain rules and the assigned authority.

The Government of Nepal is to trying to raise the living standard of people conducting various economic development activities. For this our country needs to manage the various resources like man, money, machine and materials. To obtain these particular resources government receives income through external and internal sources. To achieve economic development, government accounts responsibilities towards their citizens, such as security, health care, education, reduce social inequalities and other development activities. It needs to accumulate huge amount of revenue. Every year government spends more portion of the fund or the protection of common people and creation of various socio-economic infrastructures like; transportation, drinking water, electricity, communication, irrigation etc. To meet the growing expenditure, government has to manage fund from different sources.

Income can be collected from both internal and external sources. External resource can be obtained as loan grants bilaterally or through international institution. External resources are uncertain and guided by socio -political motives of the donor countries. So, it is not good for healthy development if there is highly dependency on them. It is used for economic development, reconstruction, foreign exchange, to recover from crisis condition etc. Internal source include public borrowing, government bonds, surplus on public under

taxing and taxation. The internal sources should be mobilized effectively due to weakness of external sources. Nepal governments try to mobilize internal sources for regular and development activities.

Internal source of fund is own source derived within the country. Internal source of fund includes' both tax and non-tax sources. Tax sources include the amounts which are compulsorily contributed by tax payers to the government. Taxes are emphasized on all countries developed as well as developing countries because they have the option for increasing the yield of tax system. It shows that taxes are the better sources of public revenue and it has been taken as the best effective tool for raising the public fund.

Among internal resource taxation is a prime factor. Government mostly imposes tax to finance, various fare and social service. The amount which is legally collected from the people to manage the expenditure of the government from its net income is called income tax. According to the INCOME TAX ACT 2058 BS (2002AD), income includes all the income which is received from employment, business and investment.

**Tax is defined in different ways:**

Tax is compulsory Levy on individuals, household and firms to central and local government. It is simply a liability to pay an amount to the government. It is compulsory contribution from the taxpayers. According to find lays, "A compulsory contribution to public authorities to meet the general expenses of the government which have been incurred for the public good and without reference to special benefits." (Quoted from Bhattraï and Koirala, Tax Law & Tax Planning, Page: 1)

According to Plehn, "Taxes are general contributions of wealth levied upon person, natural or corporate to defray expenses incurred in conferring common benefits upon the residents of the states." (Quoted from Bhattraï and Koirala, Tax Law & Tax Planning, page: 1)

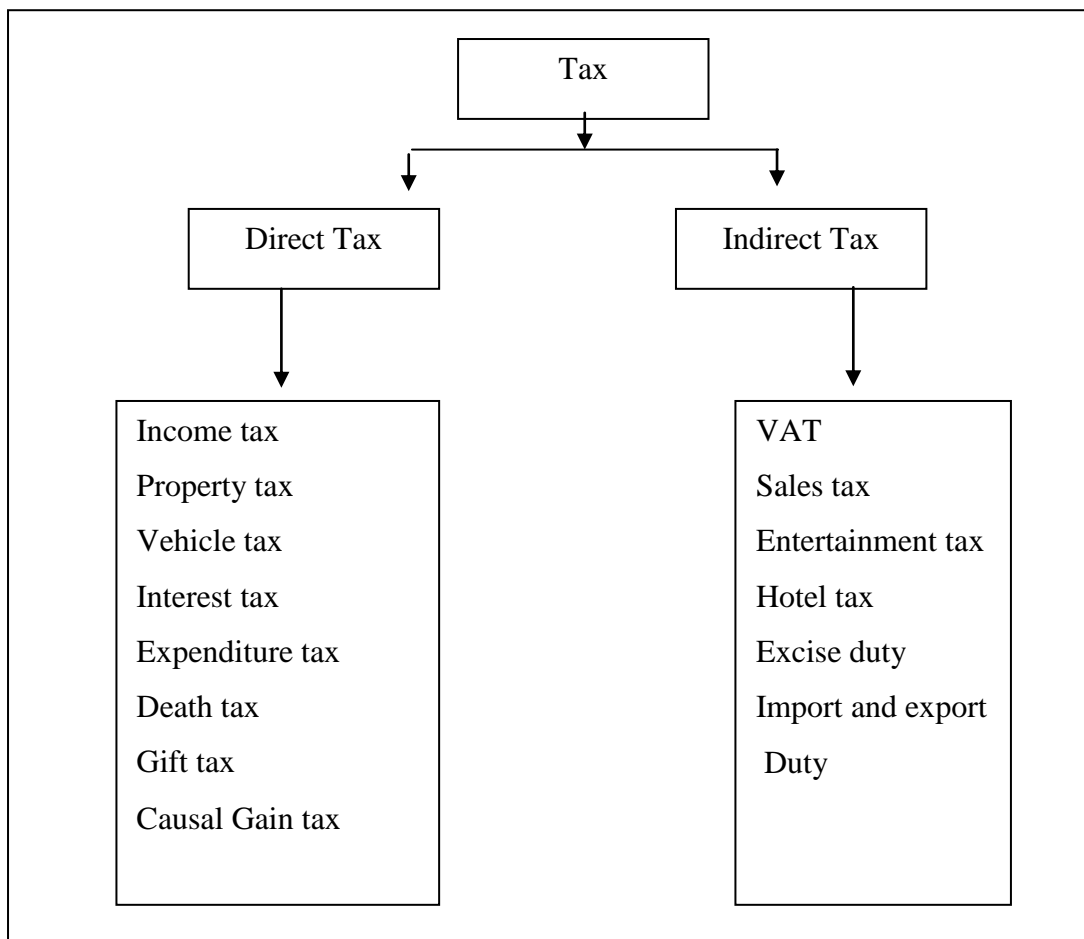
From the above definition it can conclude that:

- ✓ Tax is compulsory levy imposed by the government.
- ✓ It is levied on persons as per the prevailing laws.
- ✓ Those who pay tax do not get corresponding benefits from the government.
- ✓ It is spend for the common interest of the people,
- ✓ It is collected from haves and spends for the interest of have-nots in the society.

Basically tax can be classified into two board categories.

- ❖ Direct tax.
- ❖ Indirect tax

We can see different tax structure but in practice following the structure have been accepted.



**Direct tax:**

A direct tax is a tax paid by a person on whom it is legally imposed. Indirect tax the person paying and bearing tax is the same. It is the tax on income & property. For examples:

- Income tax
- Property tax
- Vehicle tax
- Interest tax
- Expenditure tax
- Death tax
- Gift tax
- Causal Gain tax

**Indirect Tax:**

An in direct tax is a tax imposed on one person but paid partly or wholly by another. In indirect tax the person paying and bearing the tax is different. It is the tax on consumption or expenditure. For examples:

- VAT
- Sales tax
- Entertainment tax
- Hotel tax
- Excise duty
- Import and export duty

## **1.2 Statement of the Problem**

Nepal is least developing country having weak economic growth rate. It has been facing serious gap and fiscal gap problem. Total expenditure was exceeding than total revenue in each subsequent year. The govt. expenditure is continuously rising due to weakness and large investment in selecting development projects and regular expenditure is increasing due to result increasing burden of debt serving and salary as well as allowances of government personnel. Thus, there is vast difference between expenditure and resources plus foreign aids. In the contest of Nepalese economy we can see the huge liquidity crisis. So, it can be reduced through the tax collection.

To raise the govt. revenue, it is necessary to raise the sources of revenue, which help to relive from serious bottleneck of resource gap in the process of economic development program.

To bridge the gap between total resources required and supply of the resources, income tax plays vital role in the government revenue. Collection of advance tax in the Nepal has faced various problems like tax evasion, poor tax administration, and unsound income tax, collection absurdity in tax law, lack of conscious people etc. If these problems are overcomes, and tax can be useful tool in the economic development of the country.

The contribution of the income tax to the nation budget must be increased to achieve the goal of national development and equal economic distribution. The goal can be obtained only if the government of Nepal takes steps or making the increased by bringing the new taxpayers into tax net and implementing the tax laws effectively so as to discourage the tax evasion practice. Loopholes must be traced out and monitored effectively. Large taxpayers who are hiding their income should be brought into tax bracket. So, shortcoming existed at present in income tax system must be avoided to fulfill the desired goal.

Specially, there are various problems in employment tax system in Nepal especially this study has been carried out to answer the following research questions.

- What is the structure of Government Revenue?
- What is the contribution of employment tax to government revenue?
- What are the major problems of employment tax in Nepal?
- What is the contribution of income tax from employment tax to Direct Tax revenue?
- Is the Tax administration is effective for employment tax?

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

The following specific objectives have been formulated for the purpose of our research work:

- To analyze the structure of Government revenue in Nepal.
- To analyze the contribution of income from employment to Government revenue of Nepal.
- To identify the existing problems and weakness regarding to increase effectiveness of employment tax in Nepal.
- To analyze the contribution of income from employment tax to direct tax revenue.
- To suggest the possible way for making income tax from employment effective and efficient.

## **1.4 Scope of Study**

The study covers the special provision & contribution of income to revenue collection in revenue of Nepal. The main scopes of study are given below.

1. Role of employment to generate income tax in Nepal.
2. Revenue from income from employment to income tax revenue of Nepal.
3. Role of income from employment income to Government Revenue Nepal
4. Comparative study on role of income from employment income to total government revenue.

## **1.5 Significance of the Study**

This study focuses mainly on revenue performance of employment taxation and also tries to find out the problem and difficulties associated in the collection of employment tax and a facilities and benefits as per the Income Tax Act 2058. It has been also tried to suggest and recommend in some possible areas of reform in income tax in reference to employment tax. There has been many ideas and research on various topic related to employment tax in Nepal. So this study is directed towards acquiring information about income tax collection from employment taxation.

Thus this will directly be beneficial for the 'policy makers, private sectors, researcher, professors, teacher, and people. Also, it will help researcher to carry out their research a step ahead on employment tax. Beside this study will provide a clear idea and knowledge to those who are interested and confused about employment to system.

## **1. 6. Limitation of the Study**

The study was not far from the limitations. The major limitations were as follows.

1. The study was based on the remuneration income/employee tax.
2. This study covers past 10 years of period (2002 to 2012) to make the trend analysis of income from employment income to the government revenue of Nepal.
3. Due to the lack of times and other difficulties the field study limited to Pokhara village for primary data.
4. This study is not concentrate on the planning, tax avoidance and tax evasion.
5. Most of the numerical data is taken from secondary data.
6. The study was based on laws, all rules, ordinance, regulations and circular of income tax.

## **1.7 Organization of the study**

For the systematic presentation of the report, the research is divided into five chapters as follows.

Chapter 1: Introduction

Chapter 2: Review of Literature

Chapter 3: Research methodology

Chapter 4: Presentation & analysis of data

Chapter 5: Summary, Conclusions & recommendation

## **1. Introduction:**

The foremost chapter is about introduction that includes the general background, statement of problem, objective of study, scope of study, significance of study and limitation of the study.

## **2. Review of Literature:**

The second part of the study has contained the review of literature. This part has been studied by dividing into two units as reviews of Act and review of related books, journals, and past research works. Many published and unpublished related materials were studied, presented and interpreted as per requirement.

## **3. Research methodology:**

The third part of the study is about resource methodology and includes research design, population and samples, nature and sources of data, data collection procedure & processing, tools, techniques and methods or analysis, research variables, weight of choice, and selection of respondent and respondent profiles.

## **4. Presentation & analysis of data:**

Presentation and analysis of data has been presented in the fourth chapter. This is one of the most important chapters and data related to the topic extracted from economic survey and annual reports published by Ministry of finance. The analysis has been presented accordingly with suitable methods of presentation. Similarly, presentation and analysis of opinion survey has been placed under this chapter. It is the main body of the chapter where descriptive and analytical analysis of the primary information collected through sampling method from various respondents has been studied, analyses and presented accordingly.

## **5. Summary, Conclusion & Recommendations:**

This is the final chapter of the study, in this chapter summary of whole study, conclusion & recommendations were made regarding improvement employment income and related issues.

## **CHAPTER - II**

### **REVIEWS OF LITERATURE**

#### **2.1 Introduction**

Literature review is an essential part of all studies. It is a way to discover what other researchers have covered and left in the area. A critical review of the literature helps the researchers to develop a thorough understanding and insight into previous research works that relates to the present study. It is also a way to avoid investigation problems that have already been definitely answered. Thus, a literature review is the process of locating, obtaining, reading and evaluating the research literature in the area of the student's interest. The purpose of literature review is to find out what research studies have been conducted in one's chosen field of the study and what remains to do. The primary purpose of the literature review is to learn not to accumulate.

#### **2.2 Conceptual Frameworks**

This chapter is basically concerned with the review of literature relevance to the practices of employee tax to government revenue. It covers the series and previous study on topic done by academicians and researchers within and outside the nations. This frame work could be helpful the gathering various knowledge and experiences. So the conceptual framework contains following background and experiences.

Different ways of minimizing the tax liabilities most of the person don't pay any more taxes then their obligations, permits and legitimate and sometimes questionable tax minimization schemes and practices are a developed in order to reduce tax liabilities. Every people want to reduce tax liabilities and every government wants to increase income.

### 2.2.1 Income Tax

Generally, income means the inflow of cash to the person or firm. Most of the people do not take the kind as an income. It is a best measure of economic well being of a person as well as of a nation. Higher income denotes the high living standard and lower income from rendering various types of service, selling goods and producing crops for their own use. Thus, income may be cash or kind that is received by a person for livelihood.

Economists define the term 'income' in a broad sense. It is an economic gain or receipt to a person during a particular time by way of wages, interest, profit and rent. The money income of the people is generally used for two purposes. Part of income is spent on consumption and part is saved. This definition can be expressed in the formula as follows.

$$Y=C+S$$

Where,

Y = Income

C = Consumption

S = Saving

But for the purpose of taxation, the definition of income is somehow different from the aforesaid definition. According to Income Tax Act 1974 (2031) "Income means the income earned or received in cash or kind from the sources mentioned in sec. 5". In this section five different head of income were mentioned. They were as follows: (ITA, 1974)

1. Agriculture
2. Industry, Business, Profession or Vocation
3. Remuneration
4. House and land rent

## 5. Other sources

The existing Income Tax Act 2002, which has been enacted since 2058 Chaitra 19, (April 1, 2002), has defined income in section 2(a) as "person's income from any employment business as calculated in accordance with this Act (ITA, 2002). It includes all sorts of income received for the provision of labor or capital or both of whatever form or nature in the taxable income.

Tax, in simple terminology, is a liability to pay an amount to the government. It is a compulsory contribution to the national revenue from the taxpayers according to law. In the word of Seligman, taxation is the "compulsory contribution from a person to the government to defray expenses incurred in the common interest of all reference to special benefit conferred."

From the definition given above, it can be said the firstly, a tax is a compulsory levy and those who are taxed have to pay it without getting benefit of services or goods from the government. Secondly, cannot receive any quid pro quo for the payment of tax. The taxpayer does not receive equivalent benefit from the government. Thirdly, the tax is paid to the government for running it. Fourthly, in case of tax, the amount is spent for common interest of the people. The tax is collected from haves and basically, spent for the interest of have-nots in the society. Fifthly, a natural or an artificial person pays the tax. (Kandel, 2004)

In conclusion, it can be said that tax is a liability to pay an amount to the state. The basis of a minimum amount from certain specified or that they own certain tangible or intangible property or those they carry on certain activities which have been chosen for taxation. (Kandel, 2001)

Income tax refers to the tax levied on the income of a person and profits of corporation for the specific time period, particularly one year. Income tax is levied on the taxable income of a person or a company after deducting allowable expense. Accounting profits may differ from taxable profits. For the computation of taxable income, generally incomes are added and expenses are subtracted and losses, which are allowed to deduct under the provision of

Income Tax Act are also subtracted. The, tax free incomes allowances and common expenses are also deducted to get taxable income. After giving the exemption limit as per law, the amount of tax to be levied on this computed income is the income tax.

### **2.2.2 Evaluation of Taxation**

In early days, taxes were collected at the time of emergencies, to finance wars and to provide communal services. Taxes were levied on the basis of welfare of the people. At that time tax was not compulsory payment. People voluntarily paid the tax because non-payment of tax was taken as sin in the Hindu tax system. According to Hindus scripture, the duty of king was to serve and secure his people, maintain peace and harmony and carryout social works, for those purpose king used to levy tax by collecting crops and cattle from farmers, gold and silver and other metallic goods from traders.

Great Britain was the first country in the world to introduce the income tax in 1799. It imposed income tax in order to finance war with France. Similarly, in U.S.A. the first federal income tax was imposed in 1862 with the same objective (to finance civil war). However, in the beginning these countries imposed income tax as temporary until 1862, Thereafter, since 1913 it was accepted permanent tax, This, income tax was adopted by different countries gradually. Italy started it in 1864, and New Zealand adopted in 1891, Australia and Canada have followed the income tax in 1915 and 1917 respectively. After the world war, the income tax became an important source of tax revenue in many developed countries. By 1939, it had become the most important source of revenue in most developed countries it had made appearance in a number of developing nations (Agrawal, 1980)

In our neighboring country India, the income (taxation was started in 1860 by the British government to relief from economic burden created due to first democratic revolution. It was then regularly collected after the publication of Income Tax Act 1886 (Dhakal, 2057).

In this way, income tax has become the regular source of national receipts for many developed and developing countries of the world. In the beginning, income tax was generally levied at a flat rate. The principle of progressive rate of income tax had been adopted by the United Kingdom and New Zealand since 1909. Now a day the progressive rate is commonly used rather than flat rate in all over the world.

### **2.2.3 Taxation in Ancient Nepal**

Reliable records about taxation in ancient and medieval Nepal are not available. However, tax been one of the major sources of government's revenue from the ancient time in Nepal. Taxes were then levied on the merchants, travelers and farmers in the form of cash, kind and labor. Some occasions gold and agricultural products were also paid as taxes; but the nature of these taxes were temporary. In the Lichhavi's regime, income taxes from agriculture and business were introduced as a direct tax for the first time in Nepal. Income tax, which was levied on business income, was called 'kara'. There was irrigation and religious tax also in existence during the regime of king of Ansubarma of Nepal.

### **2.2.4 Taxation in Unified Nepal (1768-1846)**

After unification of kingdom of Nepal, expenses for administration, military and other operational activities were increased significantly. During that period, taxation has been taken as main source of revenue and different types of taxes like land tax, transit tax, market duties, various levies and fines, forest product tax and mining tax were levied. Local administrations were directed "to take whatever is paid willingly by the people." Taxes were collected from the three levels (Agrawal, 1080)

- a. Royal Palace: To finance occasional and ceremonial needs. The taxes were broad based and progressive.

- b. Government: To finance administrative, military and other purposes assessed on official functionaries, occupational groups and other people.
- c. Local: Prerequisites of local officials, functionaries and mendicants.

The various taxes levied during this period were narrow in base and were imposed primarily on occupations and economic activities, not on income or property. The system of direct taxation was confined to land tax and special levies like "Darshanbhet", "Salami", "Walal" etc. After the unified period, land revenue System was divided into five main forms: Raikar, Birta, Guthi, Sera and Kipat. The main sources of revenue from land were Birta and Kipat.

King Prithvi Narayan Shah had introduced 'Pola' tax in 1772, which was regarded as a revolutionary measure in the fiscal system of Nepal. It was based on flat rate system and limited on small Birta owners. There was no taxation of income in the sense of modern income tax.

### **2.2.5 Taxation in Rana Regime (1846-1950 A.D.)**

Imposition and collection of taxes during 104 years oligarchic rule of the Rana family in Nepal prior to 1951 was the prerogative of the feudal rulers. Only those taxes, which suited the objectives, needs and whims of the ruling Prime Minister, were imposed. No budget was framed .during the Rana regime. Taxes were collected at the time of requirement due to lack of Income Tax Act and Finance act. The collected taxes were directly deposited into the Prime Minister's Account.

Land tax, custom and excise duties in the form of lump sum, contracts, royalties on felling trees, royalty on supply of porters and soldiers, entertainment taxes were the major source of revenue. There were no direct taxes in the country except land tax collected on a contractual basis and

"Salami" which the government employees used to payout of their salaries at a very small percentage.

Rana Prime Minister levied taxes for meeting specific expenditure of the royal household or extraordinary expenditure necessitated by war or other crisis rather than mobilizing revenue in the nation: During Nepal - Tibet war (1855/56), the first Rana Prime Minister Jung Bahadur had imposed a tax on the income or selected groups. Similarly, Bir Shamsher imposed a levy of 1 % in the official value of Jagir assignment of government employees in 1891, to finance the transportation of water pipe supply in the capital. Ranoddip Singh imposed a 50%, tax in the income made by fishermen in Deukhuri from the sale of fish in 1882.

### **2.2.6 Income Tax in Modern Nepal**

Actually, the modern .Income Tax Act was started in the year 1959 in Nepal. After the political revolution in February 1951 (2007 B.S. Falgun), the role of government has increased to developmental as well as philanthropic works. The government of Nepal had presented its first budget in 1952 (2008, Magh 21). The first five-year plan started in 1956. The planned activities of the government needed huge amount of source and means. So, huge revenue was demanded and Nepalese government started to levy Lax on income as permanent source. As a result, it issued first finance ordinance in 1959(2016) to impose Tax on business profit and remuneration. In 1960 (2017) the Income Tax Act named "Business Profit and remuneration. Act, 2017 was made with the provisions of finance ordinance 1959. That was the first Income Tax Act, which had 22 sections. But that act was found narrow and vague. So, it was replaced by the Income Tax Act 1962(2019). That act continued for 12 years and it was also replaced by the Income Tax Act 1974(2031). That act was amended for eight times. That tax act was replaced by new Income Tax Act, 2002 (2058). This is the fourth Income Tax Act of Nepal.

## **2.2.7 Gradual Development of Income Tax Act and Laws**

### **Business Profit and Remuneration Tax Act, 2017 B.S. (1960AD)**

The finance act 1960, made provisions for the taxation of business profits and remunerations. An ordinance was issued by the king to collect the tax. In 1960, parliament of Nepal, enacted, "Business Profit and Remuneration Tax Act 1960(2017)", which consisted of 22 sections with the enactment of that act, the salary tax or personal income Tax was levied upon those individuals whose personal income exceeded Rs. 6,000 per year. In the first three years, the exemption was Rs. 7,000. An examination of tax files in the Kathmandu District Office disclosed 57 personal income tax files of individual's taxes in one or more years.

The following were the salient features of the act.

1. Only remuneration and business profit were subject to tax. Deductions were not specified for the purpose of calculating the income.
2. Tax on remuneration was to be deducted at source.
3. The basis for calculating the tax liability for remuneration was the income of the current year and for the business profit, it was the profit of preceding year.
4. In case of default, fines up to Rs. 5,000 were prescribed.
5. The taxpayer was given the right to appeal against the tax assessment to local "Badahakim". Thereafter appeal could be lodged at revenue court. Every appeal could be accompanied by security deposit for the amount of tax payable.
6. The tax officers were empowered to assess tax on the basis of best judgment estimates.

7. Profits from industries were granted a rebate of 25% and profits from small industries were granted a rebate of 50 %.

As high discretionary power .in assessment of income tax granted to tax officers, various loopholes, narrow and vague tax base were the major shortcomings of that act which cause the Income Tax Act 1962(2019) came into existence.

### **Income Tax Act 2019 B.S. (1962 AD)**

The main purpose of the imposition of this act was not only raise government revenue but also reduce inequality in distribution of income and wealth with social justice. Create taxpaying habit of the taxpayers also the purpose of this act. There were 29 sections in the act. It was amended in 2029 (1978).

The main features of this act were as follows:

- a. Income tax was defined as all kinds of income such as, profit from business, profession, remuneration occupation, house and land rent, agriculture, insurance agency and other sources of incomes in addition to business profit and employment incomes.
- b. Tax assessment was specified on the basis of best judgment estimate to the tax officers.
- c. For the first time, provision was made for the installment basis of tax and agriculture income was brought under the scope of income tax but finance Act 2023 B.S. made provision that income from agriculture was fully exempted from the income tax. Against finance Act 2030 made agriculture income taxable.
- d. Provision for reassessment of tax as well as rectification of arithmetical errors was made against exempted from tax in 2034.
- e. Carry forward of loss was allowed for a two years period.

- f. Taxable income calculation method and deductible expenses were specific.

This act has some weakness so; this act was replaced by "Income Tax Act 2031 (1974)" so as to cope with the changing needs of the country.

### **Income Tax Act 2031 B.S. (1974 A D)**

Income Tax Act 2031 had 66 sections. It was amended for eight times to .make it more practical and to eliminate confusing term. Key features of this act were as follows:

- a. Clarified certain definitions relating to tax such as assessment of tax, income year personal status of the tax payers, non-resident persons, firm, company, family, philanthropic Work etc.
- b. Head and sources of income were classified into five categories for the income tax assessment. i. Agriculture ii. Industry, trade, profession or occupation iii. Remuneration iv. House and compound rent v. other sources.
- c. This act had identified the chargeable Income and admissible expenses of each head of income.
- d. Provision of self-assessment, small tax payers, tax assessment, fine/penalty appeal, tax deduction at source, tax refund, tax exemption, avoidance of double taxation etc.

### **Income Tax Act 2058 B.S. (2002 AD)**

In 2058, ITA/2058 (2002) was enacted by the parliament by replacing the existing Act. This Act is broad as compared to the previous Act and has been made in accordance with the global standard. ITA/2059 was framed by the government of Nepal (so called HMG/N during that period) to clarify some provision of the Act. Finance ordinances have been making slight amendments in the Act every year. This Act has classified the heads of income into three

categories VIZ, employment, business and investment. The main objectives of this act are as follows:

- a. To bring all income generating activities into tax net.
- b. To widen the tax base.
- c. To harmonize tax rates and concessions on equity grounds.
- d. To make income related provision clear and transparent.
- e. To minimize tax avoidance and tax evasion.
- f. To interlink Nepalese tax system with the tax system of foreign countries.
- g. Reducing the scope of discretionary interpretation of the tax authorities.
- h. To confine all the income related matters within the Act.
- i. Make income tax elastic and revenue productive.
- J. To make tax payers more responsible by enforcing the self assessment systems.
- k. To make tax system based on Account.

This act was broad, scientific and international standard the differences of this act with other act are made clear by its key features, they are as follows (Bhattarai and Koirala, 2004: 5).

- a. All income tax related matters are confined within the Act by abolishing all tax related concessions, rebates and exemption provided by different Acts. This Act has been made super in regard to all income tax matters.
- b. The Act has broadened the tax base. Unlike previous tax Act, tax rates have been spelled out in the Act. The tax rates and concession have been harmonized on equity grounds.

- c. The Act has introduced a pool system of charging depreciation. A provision has also been made for depreciating intangible assets.
- d. The act has first introduced the taxation of capital gains.
- e. The act has provided liberal loss set-off and carry forward/back ward provisions. Internal adjustments of losses have been clearly specified. Such provision has been made from international perspective.
- f. The Act has first introduced a provision for administrative review to allow the tax administration to correct mistakes made by the tax administrators internally.
- g. The Act has made provisions for a stringent fine and penalty for the defaulters. There have been made provisions for punishment in the fines up to Rs 300000 and imprisonment on conviction up to 3 years.
- h. Global incomes of a resident are made taxable. Non residents are also taxed on their incomes with source in Nepal.
- i. List of expenses is inclusive. All expenses relating to Income have been made admissible.
- J. The act has made provision for international taxation. Foreign Tax credit has been introduced for the first time.
- k. The Act has separated administrative and judicial responsibilities by distinguishing civil liabilities of the taxpayers from criminal liabilities.

### **2.2.8 Final Withholding Payment**

As per sec 92, following payments will be taxed as final withholding

- a. Dividend received from .resident Company.
- b. Rent for the lease or a building associated fittings and fixtures having a source in Nepal and individual other than in conducting a business receives that.

- c. Interest received by natural persons from bank, financial institute (but not related business)
- d. Gain from investment insurance received from resident company.
- e. Amount received from recognize retirement fund.
- f. Gain from unrecognized retirement fund.
- g. Meeting fees
- h. Amount received from accumulated home or sick leaves.
- I. Part time teaching salary, writing articles.

### **2.2.9 Tax Exempt Organizations**

Exempt organization means any entity that should not pay the tax, social and religious organization these are not operated for profit earning is provided with such facilities. ITA/2058 sec (2) dha has included the following entities with tax exempt organization.

- a. A religious educational or charitable organization of public charter reregistered without having a profit motive.
- b. A political party Registered with the election commission.
- c. A village development committee, municipality, or district development committee.
- d. An amount sporting association forward for the purpose of promoting social or sporting amenities not involving the acquisition of gain.
- e. Nepal Rastra Bank.
- f. The government of Nepal.
- g. An entity that has been declared as exempt organization issuing notice by the government.

### **2.2.10 Objectives of Income Tax in Developing Countries like Nepal**

Taxation has been a very essential element of a government from the very beginning of the state system. The main objective of taxation of any country was economic development. Income taxation is the best source of revenue generation in the hands of government for the purpose of internal resource mobilization in the developing countries. Appropriate taxation policy should help in promoting savings. Taxation services as major tool for transferring resources from the private to the public sector.

In Nepal, the broad objective of progressive taxation of income tax, property is to reduce the unequal distribution of wealth. It should be create the taxpaying habits among the people rather than collecting the government revenue. The other specific objectives of income tax are as follows:

- a. To discourage the growing tendency to invest in unproductive real estate and levy increased taxes to property owners,
- b. To collect some resource from established industries,
- e. To promote industrial development providing tariff protection.

After more than 40 years of introduction of income tax, Nepal has not yet developed proper systemic tax assessment. Though at the time of first implementation of income tax, the objective was to create a habit of tax paying to general public yet it has not achieved the goal till now. However among direct tax, income tax is an important source of revenue in developed as well as developing countries. All people pay tax of proportion of their income.

### **2.2.11.Problems of Income Tax Administration in Nepal**

From the very beginning, the contribution of .income tax to the revenue of the government has been very minimum. This is because the income tax system in Nepal has been facing many problems. The inefficiency of income tax administration is one of the reasons Income tax management in developing countries like Nepal has been facing many problems. The contribution of direct tax and income tax to the public revenue is very low to meet the growing public expenditure. Nepalese government has been using deficit financing. As the consequence of this, there is significant resource gap in Nepalese budget. The problem can be avoided only when the problems of tax administration is a complex technical matter. The major problems, which the income tax administration in Nepal has been facing, can be discussed as follows (Lamsal, 2002: 27).

- a. Failure to locate new taxpayer
- b. Assessment delay
- c. Poor taxpayer's compliance
- d. Failure to maintain proper account and records
- e. Lack of motivation of tax personal
- f. Existence of corruption
- g. Instability in government policy
- h. Complicated tax laws and procedures
- i. Lack of trained and competent tax personnel

### **2.2.12 Source of Income in Nepal under Income Tax Act 2058 (2002)**

Source of income considered as focal point for tax system. Computation of taxation depends upon the type and nature of income source, in every Income

Tax Act sources of income should be well defined. "Income Tax Act 2058" has divided the sources of income into three categories which are as follows:

- Income from employment
- Income from business
- Income from investment

### **2.2.13 Income from Remuneration/Employment**

Income from remuneration or employment is one of the important sources of income under the current income Tax Act. Remuneration means amount given to employee against the service provided by him. In cases of remuneration there used to be one getting service and another providing service. People who get service are called employer and person who provide service is employee. Certain conditions are required to come under remuneration; Income Tax Act 2058 has defined about employment as the past, present or prospective employment of future. Income Tax Act 2058 has specified the income from employment under section 8. As per the act, any type of income from any employment is taxable income. According to section 8 of the act, the remuneration received by a person from the employment is the following payment made by the employer:

- a. Wages, salary, leave pay; overtime pay fees, commission, gifts, prizes, bonus and other facilities.
- b. Amount received from retirement fund.
- c. Amount of contribution of the employer to a retirement fund.
- d. Amount received in reimbursement of personal expenses of the employee and related person.
- e. Amount received in lieu of acceptance of any condition with regarded to the terms of employment.

- f. Payment received for loss or termination of the employment.
- g. Other amounts as given in chapter 6 of the Act i.e. perquisites and any gains due to change in tax accounting required to be included.
- h. Any other payment made in respect of the employment.
- i. Dearness allowance, cost of living expenses, rent, retirement and transportation allowance and other personal allowances. However, according to section 38 of the "Income Tax Act 2058". Remote area allowance up to Rs 30000 for 'A' class area, Rs 24000 for 'B' class area, 18000 for 'C' class area, Rs12000 for 'D' class area and 6000 for 'E' class area is not included in taxable remuneration of the employee.

In addition to above items of remuneration, the following types of remuneration of person also are included.

- a. Market value of assets in case of the transfer of the assets.
- b. Value prescribed by Inland Revenue Department (Under section 27).
- c. The amount of expenses to be paid by the employer for following facilities of the employee as reduced by any contribution in this regard made by the employee.
- d. Service of housekeeper, cook, driver, and other domestic assistant.
- e. Service provided to the residence of the employee such as installation and cost of water, electricity and telephone.
- f. Any meal, refreshment or entertainment.
- g. Provision of residence to the employee, however, this amount is limited to only 2% of salary (sec.13 of Income Tax Rules)
- h. Availability of motor vehicles wholly or partly for private purpose. However such amount will be limited only up to 0.5% of this salary (sec 13, Income Tax Rules)

- i. Any facilities paid in cash or in kind as per chapter 7 of this Act.
- j. The amount of the difference of interest on loan paid by employee at concession rate from the standard highest rate.
- k. Discharge or reimbursement of costs incurred by the individual of his associates.

#### **2.2.14 Non-taxable Income under 'Income from Employment**

The following account is excluded in calculating an individual's payment from an employment.

- a. Amount excluded under section 10 and final withholding payment.
- b. Remuneration under bilateral or multilateral agreement with foreign government.
- c. Remuneration under the employment of public service of foreign government.
- d. Remuneration paid by Nepal Government to foreign national on condition of tax exemption.
- e. Allowance paid by Nepal of Government to Widows, senior citizens or disable persons.
- f. Remuneration derived by foreign national from foreign government.
- g. Pension received by retired army or police from public fund of foreign government.
- h. Reimbursement of expenses incurred for the employer.

Payment of an amount up to Rs500 for such a purpose. The amounts, which are deductible while deriving the net income from employment, are as follows:

- i. Contribution to approval retirement fund within the limit (sec.63)

- ii. [Rs 3 lakhs or one third of the employee's assessable income whichever is less]
- iii. Donation amount equal to 50% of taxable income or 100000 or actual whichever is less. But Nepal government may notify through official gazette that donation given to such institution will be expected for deduction to the notified limit. Such donation shall be allowed as per the notification.
- iv. For computation of tax liability, medical tax of 15% of the approved medical cost plus carried forward excess amount greater than the limit can be adjusted. However upper limit of medical tax credit is Rs750 per year. The remaining balance of uncovered medical tax credit can be recouped in next year. Similarly, amount of tax paid in foreign countries provided that such amount do not exceed average rate of Nepalese income tax can be adjusted.

### **Specimen**

#### **Computation of Assessable Income from Employment as per Income Tax Act 2058**

Particular	Rs	Rs
Salary & wages (8.2)	.....	
Leave pay (8.2)	.....	
Pay for overtime (8.2)	.....	
fees (8.2)	.....	
Prizes & gifts related to employment (8.2)	.....	
bonus (8.2)	.....	
Other facilities (8.2)	.....	
Commission (8.2)	.....	
Dearness allowance (8.2)	.....	
Cost of living subsistence's (8.2)	.....	
Rent (8.2)	.....	

Entertainment & transportation allowance (8.2)	.....	
Other personal allowance (8.2)	.....	
Reimbursement & transportation allowance (8.2)	.....	
Payments for the individual (8.2)	.....	
Agreement to any condition (8.2)	.....	
Regarding (8.2)	.....	
Other payments made in respect of employment payment (8.2)	.....	
Redundancy or loss related payment (8.2)	.....	
Retirement payment & contribution to retirement fund (8.2)	.....	
Amount of vehicle facility (27.1)	.....	
Amount of services of house keeper gardener or other domestic assistant (27.1)	.....	
Any meal refreshment on entertainment provided by employer (27.1)	.....	
Amount of service related to drinking water, electricity, telephone, and the like utilities in respect of the payees. (27.1)	.....	
Under payment of interest by employee to employer for the loan taken by the employees. (27.1)	.....	
Other amount to be included assessable from employment.	.....	
<b>Assessable income from employment</b>		.....

**Statement of total taxable income**

Particulars	Rs	Rs
Assessable income from employment	.....	
Assessable income from business	.....	
Assessable income from investment	.....	
Total assessable income	.....	

Less: Reductions		
1. Retirement contribution (section -63)	.....	
2. Donation (section -12)	.....	
<b>Total taxable income</b>		.....

### Calculation of Income Tax Liability

Particulars	Rs	Rs
First Rs..... (Individual) or Rs ..... (Couple)	.....	
Net Rs..... @ 15%	.....	
Balance Rs.....@25%	.....	
Add: surcharge @ 1.5% of balance taxable income	.....	
<b>Total tax liability</b>	.....	
Less:		
1. Advance tax paid	.....	
2. Medical tax credit (Rs. 750 or 15% of medical expenses whichever is lower....)		
<b>Tax payable</b>		.....

### 2.3 Review of related Studies

Since 1959/60, income tax was started in Nepal. After its establishment, many individuals and institutions have studied in this subject regarding legal aspect, administrative problems, historical aspect, trend of income tax and income tax structure etc. they have made appreciable efforts in the field of income tax.

Many dissertation, books, articles and newspapers reviewed while preparing this thesis. Many books in this field are written to fulfill the course requirement

of Tribhuvan University. An attempt is made here to review some of the books, thesis, articles, and reports, which have been written in field of income taxation in Nepal.

### **2.3.1 Review of Books**

*Kedar Bahadur Amatya (1965)* wrote a book entitled "*Nepal ma Ayakar Byabasitta*". In this book, he gave a simple description of "Nepal Income Tax Act 1962" with some examples how taxable incomes are derived from different sources of income. He has also analyzed basically the legal aspect of the income tax. This book is old concept and all things mentioned in it are not suitable at present. But it becomes the historical document in the field on income tax.

*Govinda Ram Agrawal (1980)* wrote a book entitled "*Resource Mobilization in Nepal*". In this book, he explain detail about resources mobilization through income tax; Nepalese policy, effective tax system and tax policy, income tax in Nepal, role of income tax in Nepalese tax structure, administrative and legal aspects of income tax in Nepal. His main contribution from this book is concerned to the empirical investigation of facts and figure about the income tax in Nepal.

*In 1998, Dr. Karna B. Poudyal published book entitled" Corporate Tax planning in Nepal"*. This book is very useful for examining the implications of tax factor in strategic planning, project planning and operational planning. It also investigates the tax planning practices being followed by Nepalese companies, besides examining the corporate tax structure in Nepal. The book is dependent basically in research information and found very essential to gain conceptual knowledge of tax planning. Although the book is not focused on

remuneration aspect, it is found very much useful to anyone who is interested in the subject of taxation.

**K. D. Dhakal (2001)** has presented extended, enlarged and modified edition of his book named. *“Income Tax and House & Compound Tax Law and Practice”*. This book is extremely based on the syllabuses of B.B.S third year. In this book he has described the provision made under income tax act the methods of income tax assessment have been described with numerical examples. His book is informative rather than analytical. He has not analyzed the role of income tax, income tax structure and defects of income tax system of Nepal. His book is more helpful to know about general information and provision made under “Income Tax Act 1974”.

**K.P. Aryal and Surya Prasad Paudel (2003)** wrote a book entitled *“Taxation in Nepal”* This book is based on ITA 2002. This book is divided into three parts. It has described about tax, features of ITA 2058, capital receipts or revenue receipt, special provision for entities and retirement saving, classification of taxpayers, head and source of income, assessment, collection and recovery, tax authorities and their powers, rights and duties etc. This book is also based on the B.B.S. level. Method of income tax has been dealt with numerical illustration. This book is useful for academic purpose and practical point of view of income tax in Nepal.

**Chandramani Adhikari (2003)** wrote a book entitled, *“Modern Taxation in Nepal”* Adhikari has described the Provisions and laws related to income taxation of Nepal according to new ITA 2002. This book has been divided into five chapters. First chapter has described about theoretical concept of taxation. Second chapter has described about income tax system in Nepal. In third chapter, writer has described about head and sources of incomes, employment or remuneration income, tax on pension income, international taxation etc. VAT has been described in part three. Fourth part has been described about property tax, house and compound tax etc. windfall gain tax and other provision has been described in fifth chapter. This book is written for students

of TU, especially for BBS, MBS and MPA students. However, it is useful to taxpayers, tax administrators and others.

*Puspa Raj Kandel (2003)* wrote a book entitled "*Tax Law and Tax Planning in Nepal*" which is based on government rules & regulation. It is very timely work and extremely helpful for the Master and Bachelor level students. The second edition has attached unofficial transaction of the tax laws. Both acts and rules related to value added tax and income tax appendices. But, he had not analyzed the role of income tax, tax structure and problem of income tax.

*Ishwor Bhattarai and Girija Prasad Koirala (2004)* in their book "*Tax Laws and Tax Planning*" described the theoretical and practical aspect of income tax with related provisions. It was based on TU syllabus. They were unable to describe the tax structure of Nepal and problems of income tax system.

### **2.3.2 Review of Thesis**

*Gobinda Lal Shrestha (1967)* in his thesis entitled "*Income Tax in Nepal.*" He has discussed about Income Tax Act and rules, historical background and administrative aspects of income tax. In his research he has pointed out various recommendations, some remarkable recommendations of the researcher were as follows.

*Hari Bahadur Bhandari (1994)* wrote a thesis entitled "*Contribution of Income Tax to Economic Development of Nepal*", concerned mainly on the contribution of income tax to public revenue. He noticed that the actual collection of revenue through income tax is lower than its estimated targets because of poor taxpaying habit of Nepalese taxpayers, poor tax administrative system and widespread evasion of income tax and so on. His study had been conducted with purpose of examining the income tax structure, trend of income tax collection and the above problem and to make suggestions to solve this problem. He had not mentioned the legal provision of income tax and problem of income tax system.

***Parmeshwor Pant (1996)*** in his thesis, "***A Study of Income Tax Management in Nepal***" has tried to show the income tax system and its role on national economy. He has identified various problems of income tax management in Nepal. Lack of managerial efficiency is one of the major problems of income tax in Nepal. Lack of effective personnel management, lack of reward and punishment system, poor income tax assessment procedure, poor tax information system, lack of taxpayer's education, very narrow coverage of income tax is the major problems of income tax.

A dissertation entitled '***Self-Assessment under Income Tax Act in Nepal***' presented by ***Mr. Shree Krishna Kharel in 1996*** has examined the review while doing self-assessment and problems faced by the self-assessment of tax is a suitable instrument of raising domestic resource and the effectiveness of self assessment of tax depends upon its appropriate reformation so he has suggested to reform income tax as well as administration for effective self-assessment.

***In 2001, Mr. Satyendra Timilsina*** wrote a thesis named "***Personal Income Taxation in Nepal. A Study of Exemption and Deduction***". He has analyzed the system of tax exemption and the deduction and suggested to improve tax system so that government can collect more revenue, he has suggested reintroducing standard deduction, different exemption for couple considering dependents and increased moral of tax officials. Furthermore, he has also suggested adjusting exemption limit based on inflationary condition of the nation every year.

***Bibha Pradhan (2001)*** had conducted a research in the topic, "***Contribution of Income Tax from Public Revenue of Nepal with Reference to Nepal Telecommunication Corporation.***" In this study, she has explained the conceptual framework of public enterprises and NTC, conceptual framework of income tax, contribution of income tax to the public revenue and share to NTC to the income tax. She also found that NTC has contributed highest income tax

in total income tax revenue from PEs. NTC shared 44% share of total income tax revenue from PEs, which was 84% in the FY 1993/94. Except in FY 1991/92 and 1996/97, the collection of income tax from NTC has been increasing gradually during the study period. Her suggestions are about the income tax system, promotion and reward to efficient and honest personnel motivation to personal tax education to tax payer and officers.

**Mr. Keshav Raj Gautam (2004)** has described about contribution of income tax to national revenue of Nepal. He has mainly focused about conceptual framework, legal provision, and structure of income tax. He has connected an empirical investigation about various aspects of income tax in Nepal.

He has found that the contribution of direct and indirect tax revenue were 20.63 percent and 79.40 percent respectively in 2002/03. Income tax revenue has occupied third position based on mean contribution other sources of revenue; the contribution of income tax to total revenue was 8.84 percent. It may enhance the revenue of government, promote to distribute justice and encourage private sector investment. Nepalese government expenditure is increasing at the faster rate than the increase in revenue the resource gap has existed in Nepalese economy and it is increasing trend, tax/GDP ratio of Nepal is found satisfactory, the exemption limit is not satisfactory. He has made the specific suggestion for a sound and effective income tax system. They were establishment, promotion and reward system to efficient and honest tax personnel, increasing public participation to minimize the tax evasion, strict action against corruption, income tax, rules, and regulation should be clear and simple. The provision of times, penalties and punishment should be at a higher rate for income tax evaders; more deduction should be provided for export promotion and separate income tax department should be established (Gautam, 2004).

*In 2004, Mr. Girija Prasad Koirala has presented a dissertation entitled "Contribution of Employment Income to Income Tax Revenue of Nepal."*

The objectives of the study were: to analyze the contribution of income tax from employment income to public revenue of Nepal, to examine and analyze the effectiveness of income tax revenue collection from employment income to show the contribution of income tax from employment income to total tax revenue and income tax revenue of Nepal and to recommend possible measures regarding taxation of employment income and increasing the share of employment income in income tax revenue of Nepal.

He has found that contribution of employment income to total income tax revenue of Nepal has not been satisfactory due to various reason like low pay scale of the employees, ineffectiveness in the implementation of tax Act, tax evasion is not often practiced in employment income due to already deducted at sources while receiving salaries, employees have faced problem while paying income tax such as poor responses from tax administrators, mental pinch, unnecessary delays etc.

He has suggested that checking income tax evasion and bringing new taxpayers into tax bracket should increase contribution of income tax to tax revenue and direct tax bracket should increase contribution of income tax to tax revenue and direct tax revenue. Making TDS effective also help to increase income tax's share in tax and direct tax revenue. The troubles faced by employers should be minimized. Tax administrator should be made more responsible, tax clearance certificate should be provided immediately to the employees after paying income taxes, taxation knowledge in the employees should be provided, the refund of tax should be made with no delay. Procedural complication in paying income taxes should be minimized, employees should be made such that they do not feel mentally pinched by paying income tax become a sense of contributing to the nation, and standard exemption limit and deduction for expenses should be provided to the tax payers.

**Mr. Jhalak Mani Lamsal (2005)** has presented a dissertation entitled "***Effectiveness of Remuneration Tax in Nepal.***" The objectives of his study were to identify the major problems and weakness of remuneration tax in Nepal, to check out the, major facilities and benefits provides by Income Tax Act 2058 on the remuneration tax. He has found that contribution of remuneration tax in total income tax revenue of Nepal has not been found satisfactory due to unfair and weak administration, complexity in income tax policy, rules and regulation, no provision of any expenditure; it is high burden of tax on low level income earners. He has also found that current exemption limit for the senior and disable citizen should not be necessarily more than that of other citizen.

**Sushil Dahal (2005)**, presented thesis on "***A Study on Contribution of Income Tax on Government Revenue.***" The main objective of his study was to analyze the impact of income tax evasion and government revenue of Nepal and give appropriate suggestion to improve the tax system. The objective of his study was i) To analyze the existing nature of the taxable income of Nepal, ii) To examine the ways and cause of income tax evasion in Nepal, iii) To estimate the volume and tendency of income tax evasion in small trade sector. In order to achieve objective of his study, has used both primary and secondary data. He has explained income tax for the economic development of Nepal has been increasing significantly in recent years as compare to past fifteen years but it does not mean that the share is that much satisfactory.

He recommended that there should be honest and efficient tax administration, tax payers should be highly literate. Up-to date record of existing as well as potential taxpayer should be kept at tax office. Programs should be formulated to find out the new groups of income taxpayers.

**Soraj Regmi (2006)**, presented master degree thesis entitled "***Effectiveness of Remuneration Taxation in Nepal.***" This study has covered objectives with (a) To assess the present position and contribution of remuneration tax on public

revenue in Nepal, (b) to identify the major problems and weaknesses regarding to increase effectiveness of remuneration taxation in Nepal, (c) To check out the major facilities provided by the Income Tax Act 2058 on the remuneration taxation and, (d) To recommend possible measures required to improve effectiveness of remuneration taxation. To fulfill the above objectives Mr. Regmi has used the primary as well as secondary sources of data. He has taken 90 total sample sizes from tax administrators 30, tax experts 30 and employees 30.

He found that in Nepalese revenue structure, tax revenue has always been greater than three times of not-tax revenue. In 1994/95, out of total revenue of Rs.24, 605.20 million, 79.90% i.e. Rs. 19,660.00 millions has been contributed by tax revenue. In 2003/04, 77.29% i.e. Rs.48, 173.00 million so total revenue has been collected as tax revenue on total revenue of Rs. 62,331.00 millions. According to his major findings from primary data, remuneration tax is contributing significantly to the income tax revenue of Nepal. Income tax evasion is being practiced with hiding the situation of double employment condition.

He has recommended that mainly tax administrator should be motivated to do something for the nation. They should strictly implement the rule and regulations. They shouldn't take tax of monitoring is only for formality. Effective implementation of the provision of fines, penalties and punishment should be made for income tax defaulter.

Regmi has only focused on the effectiveness of remuneration taxation in Nepal. He could not have explained about the implementation problem, reform of areas of income tax. But, this study has focused on the implementation of scenario of income tax in Nepal, implementation problem of income tax, reform areas and contribution of income tax to public revenue has focused. So, this study is different from the previous study.

**Mr. Subash Subedi (2007)** has presented a thesis entitled "*Effectiveness of Remuneration Tax in Nepal.*" The objective of this study were: to identify the major problems and weakness of Remuneration tax in Nepal to check out the major facilities and benefits provide by Income Tax Act 2058 on the remuneration tax. He has found that contribution of remuneration tax in total income tax revenue of Nepal has not been found satisfactory due to unfair and weak administration, complexity in income tax policy, rules and regulation, no provision of any expenditure; it is high burden of tax on low level income earners. He has also found that current exemption limit for the senior and disable citizen should not be necessary more than that of other citizen.

**Mr. Rama Kanta Subedi (2007)** has conducted study on "*Employment Income Tax System of Nepal and its Contribution to Revenue Collection.*" This study was based on the provision made in taxation policy and contribution of employment income tax to total revenue, total tax revenue total direct tax revenue and income tax revenue of Nepal. Especially the study was based on secondary data. According to him income tax from employment has been increasing every year. It occupied 7.96% in an average to total income tax. The amount of remuneration tax is ranged from minimum of Rs.56700 thousand to maximum of Rs.1675900 thousand in the fiscal year 2049/050 and 2061/062 respectively. The result of coefficient of variation shows that the remuneration income tax collection in Nepal has higher deviation in rising way over the study period. He further wrote the employment income tax has very insignificant role on total revenue and income tax revenue which shows that the share of employment income tax has vary insignificant role on total revenue and total tax revenue. This study was suggesting the government to classify the tax extension limit according to the income of individual and make it proportional the size of individual and make it proportional to the size of family that can encourage more people to pay the tax.

***Bhawani Upreti (2007)*** had conducted a research in the topic "***Contribution of Income Tax to Government Revenue in Nepal with Special Reference to Nepal Telecom.***" In this study, she has explained the conceptual framework of income tax, contribution of income tax to the government revenue and share on NTC to the income tax. She also found that NTC has contributed significant amount of income tax in total income tax revenue from PES, NTC shared 67.25% of total income tax revenues from PES, which was 80.36% in the fiscal year 2002/03. She also found except in fiscal year 1999/00 and 2000/01 the collection of income tax from NTC has been significant during the period. Her suggestions are about the income tax system are, timely assessment of tax, educated and trained tax officer, coordination between related authorities and clear cut rules and regulation.

***Mr. Hari Neupane (2008)*** has conducted "***A Study on Revenue Potential of Employment Tax in Nepal.***" He has described the story of income tax and employment tax, legal provisions relation to income tax administration aspects of income tax, tax structure and government. He has conducted an empirical investigation taking 50 persons and companies as a sample. In this study he has found that the source of tax revenue is 78% in average, the share of direct tax to be total tax revenue is 20% in average whereas the share of indirect tax to total tax is 80% in average the share of income tax to be total direct tax is 67% in average substantial share of income tax in total direct tax revenue. There is strong potential of employment income in total tax revenue. There is average 48% share of employment income in total income tax revenue.

He has found that the government policies / acts / rules / regulations concerned with the employment income tax are not effective in increasing tax paying habit of Nepal. He has suggested widening the tax coverage making consciousness to tax payers, minimizing the problems and weakness of the tax system, reform the tax assessment procedure and tax administration procedure. His study has not been related to the tax incentives and facilities.

***Kamal Acharya (2008)*** has conducted a thesis entitled on "***Contribution on Income Tax Revenue with Consideration to Income from Employment***" he has mentioned about conceptual framework, contribution of income tax to government revenue of Nepal, contribution of employment tax to total revenue, total tax revenue, direct tax revenue and income tax revenue of Nepal. He found that the contribution of employment income in total income tax revenue is insignificant, it is only 16.28% in F.Y. 2005/06 and it is highest percent during his study period. From primary data he has suggest different suggestion, such as tax assessment provision should be made clear and simple, provision of fines and penalties for tax evaders, establish coordination between tax policy maker, tax personnel and other related authority, making tax deduction at source for increase the share of employment income in the tax revenue of Nepal etc.

***Mr. Mahendra Kuwar (2008)*** carried out the study on the topic "***A Study on Problem and Prospects of Remuneration Taxation in Nepal.***" The objectives of the study were to review the income tax structure. Analyze the contribution of income tax from remuneration of analyze the assessment process of remuneration tax identify the existing problem. During the study be found that Nepalese tax Revenue consists have direct and indirect tax Revenue Tax has been heavily dominated by indirect tax revenue. Among direct taxes, income tax has the largest share of contribution. The main problem of Remuneration in taxation is to pay low income weak administration and complexity in income tax policy roles and regulation. No action for promotion regeneration tax, contribution of employment tax has not been found satisfactory.

***In 2008, Mr. Rajan Shrestha*** has submitted a dissertation on the topic "***Effectiveness of Remuneration Taxation in Nepal.***" The objectives of this study were: to assess the present position and contribution of remuneration tax in Nepal, to identify the major problems and weakness regarding to increase effectiveness of remuneration taxation in Nepal, to check out major facilities provided by the Income Tax Act, 2058 on remuneration taxation and to

recommend possible measures required to improve effectiveness of remuneration taxation. The study was based on both primary as well as secondary data. Primary data were collected by opinion survey. For analysis and test of hypothesis both analytical and descriptive method were used.

**Gita Ghimire (2008)** had been conducted a research in title *contribution of income tax in government revenue of Nepal*. His thesis was prepared as the requirement of partial fulfillment of master's degree under management faculty of Shankar Dev Campus. From this thesis, he identified what contribution portion was covered by income tax in government revenue as a research problem. To get are research's answers question the impact of income tax evasion an government revenue of Nepal and give appropriate suggestion to prove the tax system so that the government can collect more revenue and use it in the way of economic development of the country. To conduct the study, he a doubted the historical research design, primary and secondary data used to get those data a questionnaire was developed and necessary tools and chart was applied for that research. From that research, he reached in conclusion and say what is contribution portion of tax and non tax revenue in Nepal and its importance as well as what is the main factor in evasion of tax which was been lack of consciousness of tax and low tax paying habits etc.

**S.N. Shahu (2009)** presented his thesis "*Contribution of Income Tax in National Revenue of Nepal*" has focused his study on role and contribution of income tax in the process of economic development. He has found only 0.35% of population in Nepal comes under the category of taxpayers. He has also observed that in the composition of government revenue of Nepal, income tax comes in the fourth place from the viewpoint of different items contribution. The first three places are occupied by custom excise and sales tax respectively.

**Mr. Min Prasad Lamsal (2009)** has presented a thesis entitled "*Employment Income Tax is Effective Government Revenue*" (A case study of Kathmandu valley). The objectives of this study were to review the income tax structure of

Nepal, to analyze the contribution of income tax from remuneration to public revenue of Nepal, to identify the major problems and weakness of employment tax in Nepal. He has only Research on Kathmandu valley. He has used primary and secondary data. He has found that contribution of employment tax in Nepal income tax revenue of Nepal has not been found satisfactory due to unfair and weak administration. Although this report is not focused on employment aspect. It is found very much useful to anyone who is interested the subject of taxation.

**Mr. Raj Kumar Subedi (2010)** has presented a dissertation entitled "***Income Tax on Employment Income and its Impact in Revenue Collection.***" The main objectives of the study is to assess the impact of income tax on government revenue of Nepal to analyze the problem of resource mobilization and resources gap in Nepal to identify and predict the share and trend of employment income tax in government revenue of Nepal. He has recommended various types of problems and the employees faced while paying remuneration tax. Most of the data were primary sources and some were from secondary sources. To achieve the objective of the study 60 sample sizes from Kathmandu valley has been taken, Data were collected through opinion survey, field visit and questionnaires were also collected from interview with the respondents and additional information was also collected from interview with the respondents. He has suggested making broad the income tax base and establishment of standard accounting system.

**Mr. Guru Prasad Subedi (2010)** carried out a study on the topic of "***Employment Tax Reform in Nepal and its Contribution to National Revenue.***" The objectives of the study were to examine the current provision of Income Tax Act. During the study be found that the current provision made for income tax from employment in Nepal under ITA is complication for an average tax payer. IRD has not been able to provide adequate knowledge either to the tax payer or administration to the act and the author suggested that. For collect the maximum revenue tax administration system must be improved.

*Indra Prasad Poudel (2010) "Income Tax in Nepal, A Study of Dedications and Examples."* The main objectives of the study is to gain an insight into the deduction and exemptions of present income tax and give appropriate suggestions to improve the tax system. So that the government can collect more revenue and use then in the process of national development. He has explained problems weakness of income tax to government revenue and suggested possible to make provision of deducting expenses. For better education of the children actual medical expense of taxpayers, house rent expenses, educational expenses of him/herself. If he/she is studying and life insurance premium of taxpayer.

*Naba Raj Baral (2011)"The Patient of Employment and Wages in Manufacturing Industries in Nepal."* a case study of Lekhnath Municipality. He has explained problems and weakness of income tax system. Contribution of income tax system, contribution of income tax to government revenue and suggested possible areas of improvement. He has prepared on short time based on secondary data and some primary data. So the outcome of the study may not represent the extent of the problem. For the country as a whole and primary data have been collected through opinion survey of tax payers and tax practioner available in Lekhnath Municipality only.

### **2.5.3 Review of Reports**

*Govinda Ram Agrawal* started the new phase of Nepalese income tax study from the elaborated and vibrantly explained research work "**Research Mobilization for Development; The Reform of Income Tax in Nepal**" published by CEDA in 1978. Agrawal presents details about income tax in Nepal, analyzing vibrantly about role of income tax, legal aspect, administrative aspect, role of income tax for resource mobilization and other important facts. This study focused the various aspects of income tax in Nepal. Some of the important objectives of this study were as follows:

- a. To examine the problem of growing resource gap in Nepalese finance in the context of the role of income tax.
- b. To examine the ways and means for increasing tax consciousness in the Nepalese public.
- c. To examine the optimize and elasticity of income tax in Nepal including projection of income tax.

**Thapa, G.B. (2002)** wrote an article in Business Age entitle to "***Tax System and It's Reforms in Nepal.***" In his article, he has explained why tax reform? What tax reforms are? According to him traditional tax system was characterized by too many and too high rates myriad of tax incentives and tax holidays according to multiple objectives to taxes, scheduler rather than global approach to income taxation, too many income brackets and high progressively, complicated and ambiguous tax laws and by laws. The high tax rate encourages tax avoidance and evasion and also gave birth to the inaccurate economy. Tax system was to be made internationally compatible to attract foreign investment. According to him, before reform programs was implemented in FY 1986/87, Nepal's tax system was almost administratively unmanageable interns of tax rate incentives, deduction, tax holidays etc. without much revenue being collected from them and revenue mobilization was stagnant to less than 10 percent of GDP. It was just 8.7 percent in FY 1985/86 before the reform program was introduced.

One important feature of the tax reform programmed in Nepal has been the highest tax rates have been drastically reduced to minimum possible level without broadening the tax base. The efforts made by the government to broaden the tax base have been mostly quashed by the tax payers because broadening the tax base would entail the withdrawal of the tax incentives and tax holiday which would be disadvantageous to the tax payers. Thus they opposed and resisted the government's base broadening efforts. As a result, revenue mobilization through tax reforms could not be as marker out as expect.

Thapa has criticized the old Income Tax Act, 2031. He has concluded that revenue collection has not been improved as expected after the reform of Income Tax Act, 2031 due to the lack of political commitment and the inefficiency of the tax administration.

He suggested that reforms of income tax through reduction in income tax bracket and marginal rate. Similarly, reforms of VAT through full-fledged VAT applied up to retail level.

**Trephati (2006)** has published an article titled "*Aadhunik Kar Prasasan Ka Bibidh Pacchhyaharu*" on journal "Rajshow" - 2006, Jan-Feb. Vol-3. He has overviewed and explained the different aspect of income tax administration in his article. He further mentioned that, tax policy, tax law, tax objective or administration, organization, capable manpower, transparency, self-assessment of income and its inspection, tax examination and research, up to data records of tax payers and the use of information technology, physical facilities etc are the different aspects of tax administration.

He has analyzed all the above mentioned aspects of modern tax administration detailed and he concludes that the modern tax administration is not functioning well because there is the lack of full implementation of tax law, lack of transparency in both tax payers and administrator, lack of adequate tax officers, frequent change in policy and laws, lack of adequate training to people working at tax offices etc.

He further concludes that, although there exists some defects in modern tax administration, it is improving its way of functioning, and he is hopeful to see the well functioning tax administration in near future.

**Kamal Deep Dhakal** had written an article entitles "*Historical Perspective on Income Tax in Nepal*" in 2008, this article has describe previous Income Tax Act and shown main fatigue of Income Tax Act 2058 are as follow:

1. Provision of set off and forward of losses,

2. Classification and pooling of depreciable assets,
3. Tax on capital gain,
4. International taxation,
5. Medical tax credit,
6. Withholding payment and qualification allocation and characterization of the amounts.
7. Some of the significant findings and recommendations were as follows:

**Findings:**

1. Needs for additional resource mobilizations were growing by 85 times in Nepal and she was experiencing a serious and growing problem of resource gap.
2. Income tax has been a fast growing category of tax revenue in Nepal.
3. The individual taxpayers contributed more than 50% of the total income tax revenue.

**Recommendations:**

1. Additional domestic resource should be mobilized through taxation.
2. Tax structure of Nepal needs to be redesigned in order to increase the role of direct tax.
3. Income tax should be reformed in Nepal (Agrawal 1978).

**2.4 Research Gap**

The rate of government expenditure is exceeding the rate of government revenue almost every year. Nepal has been facing persistent budget deficit from the beginning of her development phase. Mobilization of internal resources through income taxation is one of the vital solutions for collecting revenue. In

this regard, contribution of income tax to government revenue of Nepal is conducted.

Nepalese income taxation has been playing a significant role in government revenue. Contribution of income tax is increasing every year but it is not satisfactory to meet the budget deficit. Tax evasion and inefficient administration are found to be the major causes for low income tax collection. So this study has been undertaken analytically and intensively to analyze the contribution of income tax to government revenue considering tax evasion in Nepal. Projections of future trend of income tax and empirical analysis of primary data have been done. This research will be equally beneficial to the policy maker, planners, tax administration, researchers, students and the persons interested in income tax of Nepal.

## **CHAPTER III**

### **RESEARCH METHODOLOGY**

#### **3.1 Introduction**

Research methodology refers to the various sequential steps which are adopted by a researcher in studying a problem. It would be appropriate to mention that research projects are not susceptible to be studied. Thus an entire process by which we attempt to solve the problem is called research methodology. This chapter is devoted to the methodology applied in the study to achieve the goals. Both primary and secondary sources of data were used in the study. Opinion survey techniques were adopted while collecting primary data. Questionnaires were distributed to income tax experts and tax employees so as to know their opinion towards various aspects of the study. Economic survey was used as the major sources of secondary data. Different financial and statistical tools were used to analyze the collected data. In this study, correlation, simple average, percentage and chi-square test for hypothesis have been used to analyze the collection data.

#### **3.2 Research Design**

The analysis of the study is based on certain research design keeping as the objectives of the study in mind. Generally, research design means definite procedures and techniques which guideline profound ways for research ability. Most of the materials of this study are concerned with past phenomena in numerical or theoretical terms. The study oriented to:

##### **I Analytical Research**

In analytical research, the researcher uses the facts and the information already available and analyzes to make a critical evaluation of the materials. Analytical research was carried in terms of role of total tax revenue, income tax revenue in composition of direct tax etc.

## **II Descriptive Research**

Descriptive research includes surveys and facts finding enquiry of different kinds. It is concerned with finding of facts relating to the subject matter, obtaining important data and getting new areas of knowledge by describing them descriptive research will be carried out in this study on contribution of employment tax to government revenue of Nepal.

## **III Empirical Analysis**

An empirical analysis has been conducted in order to find out various aspects. Contribution of income tax to government revenue of Nepal and effectiveness in collection of income tax has been taken into consideration. To find the stated objectives opinion surveys of respondents were conducted. Respondents have been classified into tax experts and tax employees. For this, questionnaire was developed and responses were collected from the respondents regarding the subject matter.

### **3.3 Data Collection Procedure**

A set of questionnaire was developed and distributed to the selected respondents in order to get actual accurate, fast and reliable information. Distribution work was done by personally rather than sending by any other means. Additional valuable information was also collected from interview with the respondents as well as group discussion with taxpayers.

### **3.4 Population and Sample**

All the tax experts and tax employees of Nepal were considered as total population. Out of them tax experts and tax employees of the Pokhara valley were considering as target sample. Out of target population 60 respondents have been taken as sample size.

## Groups of respondents and size of sample

Table 3.1 Groups of respondents and size of sample

S.N.	Groups of respondents	Sample size
1	Tax experts	30
2	Tax employees	30
	Total	60

Source: Opining survey 2013

### 3.5 Nature and Sources of Data

Both primary as well as secondary data have been used in this study. The primary data were collected from opinion of tax experts and tax employees. Primary data were obtained through the questionnaire method.

In most of the cases, face to face interview and discussion with selected persons included in the purposive sample. The secondary data have been obtained through economic surveys, budget speech, journals and newspaper.

Most of the data are collected from secondary sources. The major sources of data are as follows:

- ✓ Annual report of IRD/N of different years.
- ✓ Economic surveys, budget speech, journals and newspaper
- ✓ Economic survey of various years, published by MOF.
- ✓ Nepal Rastra Bank's Economic Bulletin of various times.

### 3.6 Procedures of Processing and Analysis of Data

After the classification, coding and editing of data, it was presented into tabulated form with separate format systematically in order to achieve the

desire objectives. It has been presented into various tables, figures, and graphs according to the subject in order. Available and collected data has been presented and analyzed in descriptive way with the help of sample statistical tools, such as percentage; average, correlation, chi-square test for hypothesis etc.

### **3.7 Period Covered**

The research study has been based on historical data. So the study covers the data of past ten year's period i.e. from 2002/03 to 2011/12.

## **CHAPTER - IV**

### **PRESENTATION AND ANALYSIS OF DATA**

#### **4.1 Analysis of Secondary Data**

This chapter focuses on the presentation and analysis of secondary data. The secondary data have been obtained from economic survey, budget speech and other related newspapers. The available data related to the study have been tabulated, presented and analyzed and interpreted to reach at some findings. The data collected from economic survey and other related newspapers have been analyzed by dividing into various subheadings. Structure of government revenue of Nepal, structure of income tax revenue of Nepal, contribution of income tax in total revenue, total tax revenue and direct tax revenue of Nepal, tax and non tax revenue of Nepal, structure of direct tax revenue In Nepal, resources gaps of Nepal for the ten period i. e. 2002/03 to 2011/012.

##### **4.1.1 Revenue Structure of Nepal**

This income of the government through all sources like taxes, fees, fines and penalties, grant, gift, donation etc are called public revenue. In general public revenue are divided into two main headings namely tax revenue and no-tax revenue. Tax revenue contributes about three quarter of total revenue while non - tax revenue represents about one quarter of total revenue at the central level. The trend and composition of tax revenue and non-tax revenue in the recent years and given in table 4.1

**Table 4.1**  
**Composition of Tax and Non Tax Revenue of Nepal**  
**From Fiscal Year 2002/03 to 2011/12 Rs. in Million**

Fiscal Year	Total Revenue		Tax Revenue		Non Tax Revenue	
	Amount	In %	Amount	In %	Amount	In %
2002/03	30373.5	100	4424.3	80.41	5949.2	19.59
2003/04	32937.9	100	25939.8	78.75	6998.1	21.25
2004/05	37251.0	100	28752.9	77.19	8498.1	22.81
2005/06	42893.7	100	33152.1	77.29	9741.6	22.71
2006/07	48893.7	100	38865.1	79.49	10028.8	20.51
2007/08	50445.6	100	39330.6	77.97	1115.0	22.03
2008/09	56229.8	100	42587.0	75.74	13642.7	24.27
2009/10	62331.0	100	48173.0	77.29	14158.0	22.71
2010/11	70122.7	100	54104.7	77.16	16018.0	22.84
2011/12	76214.0	100	57262	75.13	18952	24.87
Average				77.64		22.36

*Sources Economic Survey 20011/12 Ministry of Finance, Government of Nepal*

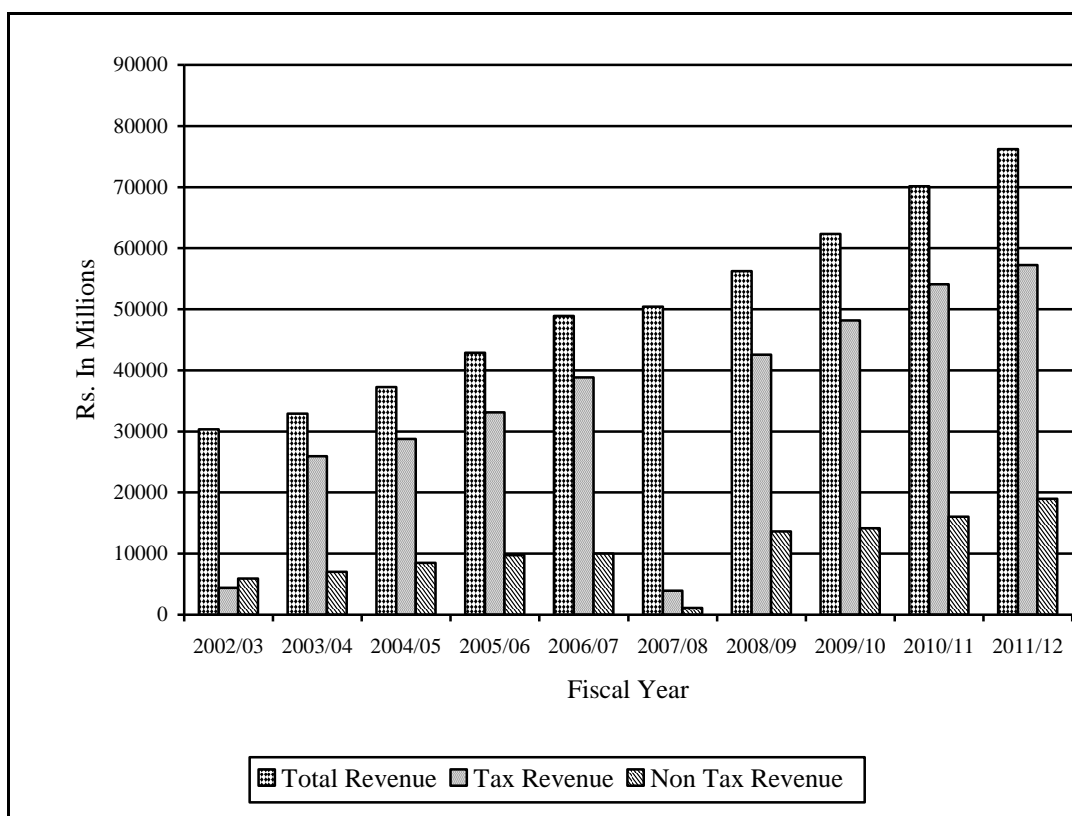
Total revenue of Nepal, consists tax revenue, non-tax revenue, non-tax revenue land revenue and registration and miscellaneous taxes. Table 4.1 shows the composition of tax and non tax revenues in Nepalese revenue structure for latest ten years i.e. from fiscal years 2002/03 to 2011/12. Nepalese revenue structure, tax revenue has always been greater than three times of non tax revenue. This means there is heavy contribution of tax revenue in total revenue of Nepal. Tax revenue in amount has always been increasing per year than the previous year. Its percentage contribution has always been fluctuating with in the lower limit of about 76% to the upper limit of about 81 %. But non-tax revenue has lowest contribution as compared to tax revenue. Its contribution to total revenue has remained below 25%.

The average share of tax revenue and non-tax revenue has been 77.64% and 22.36% respectively. This indicates that the role of tax revenue is very much

important in revenue mobilization of Nepal and to meet the increasing expenditure of government. So, tax revenue has been placed as a major source of government revenue in Nepal.

In 2002/03 out of total revenue of Rs. 30373.5 million, 80.41 i.e. Rs 4424.3 million has been contributed by tax revenue and in 2011/12, 75.13% i.e. Rs. 57262 millions of total revenue has been collected as tax revenue. Similarly, in 2002/03 out of total revenue 19.59% i.e. Rs. 5946.2 millions and in 2011/12 out of total revenue of Rs. 76214 million 24.87% i.e. Rs 18952 million has been contributed from non non-tax revenue. Although the contribution of both tax and non-tax revenue to total revenue seems to be increasing simultaneously, the dominant role is that of tax revenue.

**Figure: 4.1**  
**Revenue Trend Nepal (2002/03 - 2011/12)**



### 4.1.2 Tax Revenue Structure of Nepal

Tax revenue is consists of direct tax and indirect tax revenue. The tax on income and capital is known as direct tax whereas, tax on consumption is known as indirect tax. Direct tax includes income tax, land revenue and registration, house and land tax, property tax, vehicle tax etc. and indirect tax includes sales tax, custom duties, excise duties, entertainment tax, contract tax hotel tax, air flight tax etc. Tax revenue is one of the principle source of the government revenue, it is a compulsory contribution imposed by a public authority. It covers the following heads such as persons, organizations, business firms and even, foreigners who are doing business of consuming goods or service in Nepal. The magnitude to total tax revenue as the sum of direct and indirect tax is presented in table 4.2.

**Table 4.2**  
**Contribution Direct and Indirect Tax in Total Tax revenue of**  
**Nepal from Fiscal year 2002/02 to 2011/12**

Fiscal Year	Total Revenue		Direct Tax Revenue		Indirect Tax Revenue	
	Amount	In %	Amount	In %	Amount	In %
2002/03	22424.3	100	5340.0	21.86	19084.3	78.14
2003/04	25939.8	100	6187.9	23.85	19751.9	76.15
2004/05	28752.9	100	7516.1	26.14	21235.8	73.86
2005/06	33152.1	100	8951.5	27.00	24200.6	73.00
2006/07	38865.1	100	10159.4	26.14	28705.7	73.86
2007/08	39330.6	100	10597.5	26.94	28733.1	73.06
2008/09	42587.0	100	10105.8	23.73	32481.2	76.27
2009/10	48173.0	100	11912.6	24.73	36260.4	75.27
2010/11	54104.7	100	13071.8	24.16	41032.9	75.84
2011/12	57262	100	14160	24.73	43102	75.27
Average				24.93		75.07

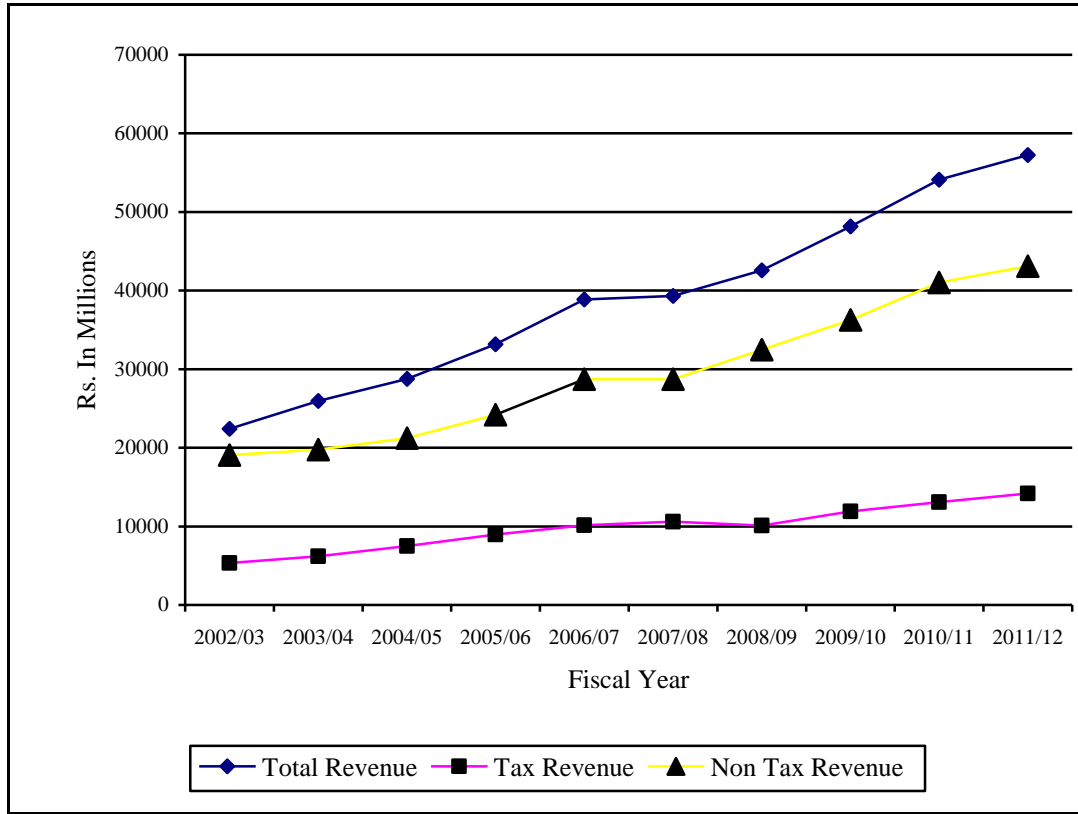
*Sources Economic Survey 20011/12 Ministry of Finance, Government of Nepal*

From the above table and below figure, it is clear that the role of Nepalese tax structure is dominated by indirect tax revenue. In 2002/03, out of total tax revenue of Rs. 24424.3 millions, Rs. 5340.0 millions and Rs. 19084.3 millions have been contributed by direct tax and indirect tax revenue respectively. It means about 21.86% and 78.14% of total tax revenue have been collected by direct and indirect tax revenue respectively. In 2011/12, Rs. 14160 millions and Rs. 43102 millions out of total revenue have been collected as direct and indirect tax revenue respectively. That is, 24.73% and 75.27% of total tax revenue have been collected from direct tax and indirect tax revenue respectively.

The average share of direct tax revenue in total tax revenue for period from 2002/03 to 2012/013 is 24.93% and the share of indirect tax revenue is 75.07%. Comparison of direct tax and indirect tax revenue shows that Nepalese economy is heavily relied up on indirect taxation. But in development countries like USA, UK etc, direct tax plays a leading role for internal resource mobilization whereas in developing countries like Nepal, indirect tax play pioneering role by dominating direct tax. To divert the channel of development, it is necessary to increase the share of direct tax, ultimately decreasing the share of indirect tax. So, attention should be focused on the sufficient resources mobilization through direct taxation.

Figure No: 4.2

**Trend of Direct and Indirect Tax Revenue**



**4.1.3. Structure of Income Tax in Nepal**

Nepalese income tax structure is made by combination of income tax from public enterprises, semi public enterprises, private corporate bodies, individuals, remuneration and tax on interest. This is presented in table 4.3.

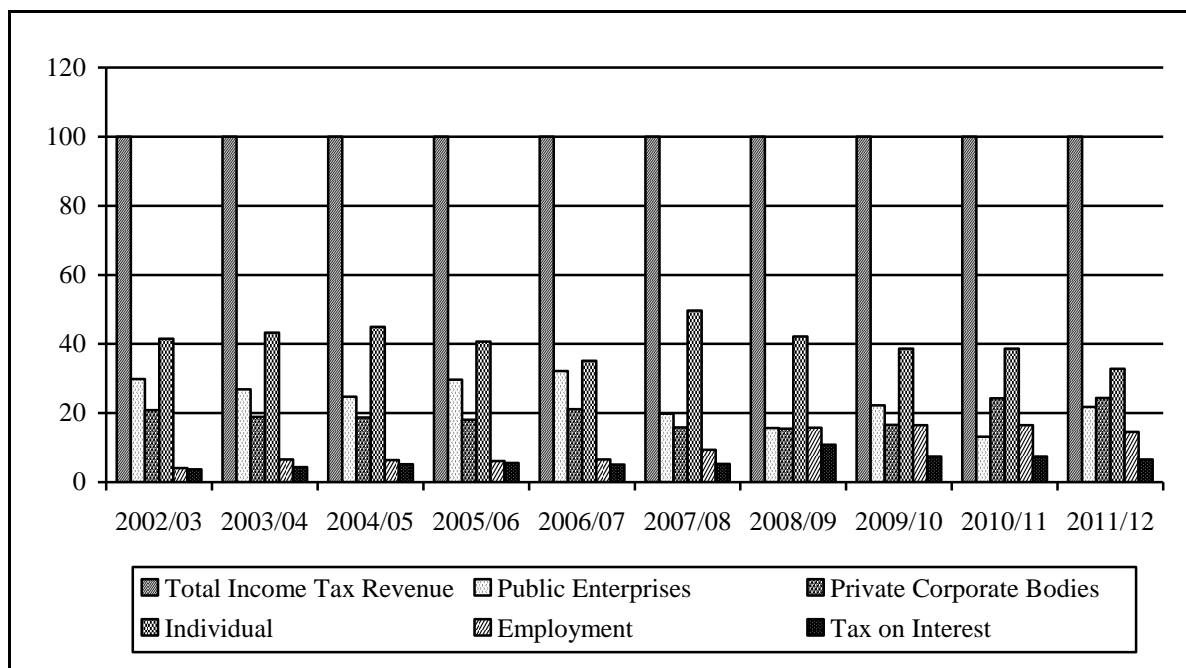
**Table No. 4.3 (a)****Composition of Income Tax in Nepal****From Fiscal Year 2002/03 to 2011/12, Rs. in million**

Fiscal Year	Total Income Tax Revenue	Public Enterprises	Semi Public Enterprises	Private Corporate Bodies	Individual	Employment	Tax on Interest
2002/03	4123.4	1231.1	-	858.4	1711.4	168.1	154.5
2003/04	4898.1	1317.8	-	925.1	2120.8	322.2	212.2
2004/05	6170.2	1526.5	-	1155.0	2772.7	396.5	319.5
2005/06	7420.6	2198.8		1339.5	3016.4	451.5	414.4
2006/07	9114.0	2928.0	-	1924.3	3200.5	597.3	463.9
2007/08	8903.7	1769.3	-	1412.0	4419.1	835.6	467.7
2008/09	7966.2	1251.0	-	1236.3	3362.3	1252.6	864.0
2009/10	9245.9	2056.6	-	1531.3	3533.4	1391.2	733.4
2010/11	10159.4	1332.4	-	2467.8	3926.3	1675.9	757.0
2011/12	11653.68	25354	-	2836.8	3819.5	1697	764.98
Average							

**Table No. 4.3 (b)****Composition of Income Tax in Nepal in Percentage****From Fiscal Year 2002/03 to 2011/12 Rs. in million**

Fiscal Year	Total Income Tax Revenue	Public Enterprises	Semi Public Enterprises	Private Corporate Bodies	Individual	Employment	Tax on Interest
2002/03	100	29.86	-	20.82	41.50	4.08	3.74
2003/04	100	26.90	-	18.89	43.30	6.58	4.33
2004/05	100	24.74	-	18.72	44.94	6.43	5.19
2005/06	100	29.63		18.05	40.65	6.08	5.59
2006/07	100	32.13	-	21.11	35.12	6.55	5.09
2007/08	100	19.87	-	15.86	49.63	9.38	5.26
2008/09	100	15.70		15.52	42.20	15.72	10.86
2009/10	100	22.24	-	16.56	38.21	15.05	7.93
2010/11	100	13.12	-	24.29	38.65	16.50	7.45
2011/12	100	21.76	-	24.34	32.77	14.56	6.57
Average		23.60	-	19.42	40.67	10.09	6.21

**Figure No: 4.3**  
**Composition of Income Tax in Nepal**



Here, public enterprises consist of 100% government ownership and semi public enterprise includes 51% of government ownership. Private corporate bodies mean public limited companies; individuals denote sole traders, partnership and private companies. Remuneration refers to salaries earned by government and non-government sector employees.

From the above tables and figure, total income tax revenue seemed to have an increasing trend except in certain years. In 2002/03, 4123.4 million was raised from income tax and in 2011/12, Rs. 11653.68 million was raised as income tax revenue. In 2007/08 and 2008/09 a slight fall was observed in income tax revenue. It has fallen by and Rs. 937.5 million 2008/09 respectively.

The income tax contribution of individuals has occupied first position in total Income tax revenue of Nepal. From the year 2002/03 to 2011/12, the amount of individual income tax revenue is found in increasing trend except in coming years with the amount of Rs. 1711.4 million to Rs. 3819.5 million. There is about fifty percentages contribution by individuals in the total income tax

revenue. The average contribution of individuals in total Income tax revenue from 2002/03 to 2011/12 has been 40.67%.

Income tax from public enterprises has occupied second position regarding its contribution in total income tax revenue of Nepal. In 2002/03, out of total income tax revenue of Rs. 4123.4 millions, Rs. 1231.1 millions has been contributed by public enterprises. It is about 29.86% contribution except few years; its contribution has been increasing. In 2011/12 out of total income tax revenue of Rs 11653.68 million, Rs 25354 million has been contributed by public enterprises. The average contribution of public enterprises in total income tax revenue comes to be about 23.60 percentages.

Private corporate bidders have occupied third position in total income tax revenue of Nepal. In 2002/03, out of total income tax public corporate bodies have contributed revenue of Rs. 4123.4 millions. It is about 20.82% contribution. In 2011/12, private corporate bodies in total income tax revenue of Rs. 11653.68 millions contributed Rs. 2836.8 million. The average contribution of private corporate bodies from 202/03 to 2011/12 came to be 19.42 percentages.

Income tax from remuneration has occupied fourth position in total income tax revenue of Nepal. In 2002/03, out of total income tax revenue of Rs. 4123.4 millions, Rs. 168.1 millions was contributed by employment income tax from the fiscal year 2002/03 to 2011/12 R; income tax from employment has increasing. In 2011/12 Rs. 1697 millions was contributed by income tax from employment in total income tax venue of Rs. 11653.68 millions. The average contribution of income tax from employment came to be 10.09 of total income tax revenue.

**4.1.4 Contribution of Income Tax from Employment to Total Revenue, Total Tax Revenue, Direct Tax Revenue and Income Tax Revenue of Nepal:**

The Contribution of income tax from employment in total revenue, total tax revenue, direct tax revenue and indirect tax revenue of Nepal is shown by the following table.

**Table No. 4.4**

**Contribution of Income Tax from Employment to Total Revenue, Total Tax Revenue, Direct Tax Revenue and Income Tax Revenue from 2002/03 to 2011/12**

Rs in million

Fiscal Year	Income Tax from Employment	Total Revenue	In %	Total Tax Revenue	In %	Direct Tax Revenue	In %	Income Tax Revenue	In %
2002/03	168.1	30373.5	0.55	24424.3	0.69	5340.0	3.15	4123.4	4.08
2003/04	322.2	3237.9	0.98	2599.8	1.24	6187.9	5.21	4898.1	6.58
2004/05	396.5	37251.0	1.06	28752.9	1.38	7516.1	5.28	6170.2	6.43
2005/06	451.5	42893.7	1.05	33152.1	1.36	3951.5	5.04	7420.6	6.08
2006/07	597.3	48893.7	1.22	38865.1	1.64	10159.4	5.88	9114.0	6.55
2007/08	835.6	40445.6	1.66	39330.6	2.123	10597.5	7.88	8903.7	9.38
2008/09	1252.6	56229.8	2.23	42587.0	2.94	10105.8	12.39	7966.2	15.72
2009/10	1391.2	62331.0	2.23	48173.0	2.89	11912	11.68	9245.9	15.05
2010/11	1675.9	70122.7	2.39	54104.7	3.10	13071.8	12.82	10159.4	16.50
2011/12	1697	76214	2.23	57262	2.96	14160	11.98	11643.68	14.56
Average			1.56		2.02		8.13		10.05

*Sources Economic Survey 2001/12 Ministry of Finance, Government of Nepal*

### **Contribution of Income Tax from Employment to Total Revenue of Nepal:**

In total revenue of Nepal, income from employment has very much insignificant contribution. Out of total revenue of Rs. 30373.5 millions, Rs. 168.1 million has been contributed by income tax from remuneration in 2002/03. It was about 0.55% of total revenue. In 2011/12, out of total revenue of Rs. 76214 millions, Rs. 1697 millions has been contributed by employment income tax. It was about 2.23% of total revenue. The average contribution of income of income tax from remuneration was about 1.56% which seems to be very insignificant.

### **Contribution of Income Tax from Employment to Total Tax Revenue of Nepal**

In Total tax revenue of Nepal, contribution of employment income tax has also very insignificant. Out of total tax revenue of Rs. 24424.3, Rs. 168.1 million has been contributed by income tax from remuneration in 2002/03. It was about 0.55% of total revenue. In 2011/12, out of total revenue of Rs. 76214 millions, Rs. 1697 millions has been contributed by employment income tax. It was about 2.23% of total revenue. The average contribution of income of income tax from remuneration was about 1.56% which seems to be very insignificant.

### **Contribution of Income Tax from Employment to Total Tax Revenue of Nepal:**

In total tax revenue of Nepal, contribution of employment income tax has also very insignificant. Out of total tax revenue of Rs. 24424.3, Rs. 168.1 million has been contributed by income tax from employment in 2002/03. It was about 0.69% of total tax revenue. In 2011/12 out of total tax revenue of Rs. 57262 millions, Rs 1697 million has been contributed by employment income tax, which was about 2.9% of total tax revenue. The average contribution in total tax revenue from employment income tax was about 2.02% from fiscal year 2002/03 to 2011/12.

### ***Contribution of Income Tax from Employment to Direct Tax Revenue of Nepal:***

The contribution or remuneration income tax to direct tax revenue has not been satisfactory. The contribution has floating trend. In 2002/03 out of total direct tax. Revenue of Rs. 5340.0 millions, Rs. 168.1 millions has been contributed by employment income tax. It is 3.15% of total direct tax revenue. In 2011/12, out of total direct tax revenue of Rs. 14160, Rs 1697 million has been contributed by employment income tax. It is about 11.98% contribution. In average 8.13% of direct tax revenue has been contributed by income tax from employment from fiscal year 2002/03 to 2011/12.

### **Contribution of Income Tax from Employment to Income Tax Revenue of Nepal:**

Income tax from remuneration is a source of income tax revenue. The contribution of remuneration income tax revenue has not been so satisfactory. The percentage contribution has been fluctuating. In 2002/03, out of total income tax revenue of Rs. 4123.4 million, Rs 168.1 million has been contributed by income tax from remuneration. It is about 4.08% of income tax revenue. In 2011/12, out of total income tax revenue of Rs. 11053.63 millions, Rs. 1697 millions has been contributed by income tax revenue. In average 10.05 of income tax revenue has been contributed by income tax from remuneration from fiscal year 2002/03 to 2011/12.

## **4.2 Empirical Investigation**

### **4.2.1 Introduction**

An empirical investigation has been conducted in order to find out various aspects of contribution of income tax to government revenue, for this questionnaire was developed and responses were collected from the respondents. A set of 60 questionnaires were received from the respondents out of 60 questionnaires distributed to them. Respondents were classified into two

group i.e. tax experts and tax employees. The responses have been analysis in order to facilitate the descriptive analysis of the study.

The questionnaire was asked for either Yes/No responses or asked for ranking of the choices. According to number of alternatives where the first choice was the most important. For the purpose of analysis, most important choices were assigned according to the number of alternatives. If the number of alternatives were four, the first preferred choice would get four points and last preferred choice would get one point. Any alternative which were not ranked didn't get any point. The total point' available to each choice were converted into percent with reference to the total points available for all choices. The choice with the highest percent score was ranked as the most important choice and then on fifth the percent score was ranked as the last choice. The following table shows the group of respondents.

**Table 4.5: Groups of the Respondents**

S.N.	Groups of respondents	Sample Size
1.	Tax expert	30
2.	Tax Employee	30
	Total	60

*Sources: Opinion Survey: 2013.*

#### **4.2.2 Opinions Regarding Employment Tax is a Suitable Measure to Collect Government Revenue:**

In order to know whether employment Income tax is a suitable measure to collect government revenue, the first question was asked. "Do you think that employment tax is a suitable measure to collect government revenue?" The responses received from the respondents are tabulated below

**Table No.: 4.6****Contribution of Employment Tax to Government Revenue**

Respondents	Yes		No		Total	
	No.	Percent	No.	Percent	No.	Percent
Tax Experts	12	40%	18	60%	30	100
Tax Employees	16	55.33	14	46.67%	30	100
Total	28	46.67	32	53.33	60	100

*Sources: Opinion Survey*

From the table, it is clear that 46.67% respondents showed their satisfaction regarding the employment income tax is a suitable measure to collect public revenue and only the 53.33% of total respondents showed their dissatisfaction in favor of remuneration tax is a suitable measure to collect government revenue. Thus it can be concluded from the above result that contribution of employment income tax to government revenue is significant.

**4.2.3 Opinions Regarding Problems Faced by Tax Payers:**

To know whether employees are facing problems in payment of employment tax, do you think there are problems being faced by employee regarding payment of employment tax? If yes, please rank the causes. Responses received regarding this is as presented below.

**Table No: 4.7****Contribution of Employment Tax to Government Revenue**

S.N.	Alternatives	Total Point x	Total Point y	Rank for x (R <sub>1</sub> )	Rank for y (R <sub>2</sub> )	D=R <sub>1</sub> -R <sub>2</sub>	D <sup>2</sup>	Over all points	%	Rank
1	Hesitation to pay because of flow income	8	10	2	1	1	1	18	30.00	1

2	Inappropriate	1	7	5	2	3	9	8	13.33	4
3	Lack of awareness of tax payers	6	6	3	3	0	0	12	20	3
4	Inefficient tax administration	11	95	1	4	-3	9	16	26.67	2
5.	Complicated	4	2	4	5	-1	1	6	10	5
6.	Other	0	0	6	6	0	0	0	0	6
							$\sum d^2$ =20	60	100	

*Note: X refers to tax experts and y refers to employees)*

By formula,

$$r = 1 - \frac{6\sum d^2}{n(n^2-1)}$$

$$r = 1 - \frac{6 \times 20}{6(6^2-1)}$$

$$= 0.43$$

The correlation indicates that there is high degree of positive correlation between tax experts and employees ranking regarding the problems being faced by taxpayers regarding payment of employment tax.

It can be concluded from above a result that in the opinion of the respondent's hesitation to pay because of low income is the major problem of employment tax. Inefficient tax administration is the second and lack of awareness to tax payers is the third problem faced by the employees while paying remuneration tax. Inappropriate rate and exemption limit, complicated rules and regulation occupied fourth and fifth rank.

#### 4.2.4 Attitude towards Tax Evasion Practice in Employment Taxation in Nepal

In order to find out whether the income tax evasion is practiced in Nepal or not, the question was asked. 'In your opinion is there problem of tax evasion in employment in Nepal'? The responses of respondents are tabulated below:

**Table 4.8**  
**Income Tax Evasion in Nepal**

Response	Groups		Total	Percentage
	Total Experts	Employees		
Yes	24	22	46	76.67
No	6	8	14	23.33
Total	30	30	60	100

*Source: Opinion Survey*

The above table reveals that 76.67% of respondents supported tax evasion as a major problems of tax evasion in Nepal. Rest of 23.33% was against the above view. It can be noted that almost all the person with denominations are in favor of the question.

#### Test of Hypothesis

Null Hypothesis (Ho): There is no significance difference in opinion of tax experts and employees regarding the tax evasion practice in remuneration taxation in Nepal. Alternative Hypothesis (HI): There is significance difference in opinion of tax experts and employees regarding the tax evasion practice in remuneration taxation in Nepal.

The Test of statistic under null hypothesis is:

$$X^2 = \sum \frac{O_f - E_f}{E_f}$$

Where, O f = Observed Frequency

Ef = Expected Frequency

$$= \frac{\text{Row Total} \times \text{Column Total}}{\text{Grand Total}}$$

Computation of  $\chi^2$ :

<i>Of</i>	<i>Ef</i>	$(Of - Ef)^2$	$(Of - Ef)^2$	$(Of - Ef)^2 / Ef$
24	23	1	1	0.0667
6	7	-1	1	0.2000
22	23	-1	1	0.667
8	7	1	1	0.2000
	Total	1	1	0.5334

Sources: *Opinion Survey + Statistical Tools*

The Calculated  $\chi^2 = 0.5334$

The Degree of Freedom =  $(r-1)(c-1) = (2-1)(2-1) = 1$

Level of Significance ( $\alpha$ ) = 5% = 0.05

Tabulated value of  $\chi^2$  at 5% level of significance for 1 degree of freedom is 3.841.

Here, calculated value of  $\chi^2$  is 0.5334, which is lower than the tabulated value 3.841, so null hypothesis is accepted. This means there is no significance difference in the opinion of tax expert and employees regarding the practice of tax evasion in remuneration taxation in Nepal.

In order to know the main reason for tax evasion the respondents were provide six reasons and were requested to rank them. The response has received are tabulated below:

#### 4.2.5 Opinion Regarding Factor for Increasing Employment Taxation to contributed Income tax Revenue of Nepal

To increase the income tax revenue employment tax plays vital role. In order to know the most important factor for increasing employment tax a question put forward to the respondents asking 'How employment tax can be increase to contribute the income tax revenue of Nepal?' the responses received from respondents are tabulated as follows:

**Table No. 4.9**  
**Calculation of Rank Correlation Coefficient**

S.N.	Alternatives	Total Point x	Total Point y	Rank for x (R <sub>1</sub> )	Rank for y (R <sub>2</sub> )	D= R <sub>1</sub> - R <sub>2</sub>	D <sup>2</sup>	Ove r all poin ts	%	Rank
1	Increase tax rates	2	3	5	4	1	1	5	8.35	4
2	Bringing new taxpayers into tax net	12	11	1	1	0	0	23	38.33	1
3	Reeducation in exemption limit	3	2	4	5	-1	1	5	8.33	5
4	Making TDS effective	8	9	2	3	-1	1	17	28.33	3
5.	Increase in pay scale of the employees	4	4	3	2	1	1	8	13.33	2
6.	Other	1	1	6	6	0	0	2	3.33	6
							$\sum d^2 = 4$	60	100	

*Note: X refers to tax experts and y refers to employees)*

By Formula

$$r = 1 - \frac{6\sum d^2}{n(n^2-1)}$$

$$r = 1 - \frac{6 \times 4}{6(6^2-1)}$$

$$= 0.88$$

The correlation indicates that there is high degree of positive correlation between the tax experts and employees ranking regarding the important factor for increasing employment tax to contribute income tax revenue of Nepal.

From the above table, it can be concluded that Opinion regarding factor for increasing employment tax by the respondents were ranked as follows:

1. Bringing new taxpayers into tax net
2. Making TDS effective
3. Increasing pay scale of the employees
4. Increase in tax rates
5. Reduction in exemption limit

**6. Others:**

- Giving more facilities to the taxpayers
- Strong monitoring for hiding the situation of double employment condition
- Increasing tax awareness to the taxpayers

#### 4.2.6 Attitude Regarding Important Factor for Effectiveness of Employment Taxation in Nepal:

In order to know the most important factor for effectiveness of employment tax in Nepal respondents were requested to rank their responses on given choices. The question was 'What is the most important factor for effectiveness of employment tax in Nepal?' responses regarding this question are presented in the table below:

Table No. 4.10

#### Effectiveness of Employment Tax in Nepal

S.N.	Alternatives	Total Point x	Total Point y	Rank for x (R <sub>1</sub> )	Rank for y (R <sub>2</sub> )	D=R <sub>1</sub> -R <sub>2</sub>	D <sup>2</sup>	Over all points	%	Rank
1	Honest tax prayers	23	10	2	2	0	0	23	23.6	1
2	Honest tax officers	14	8	1	4	-3	9	22	22.9	2
3	Effective income	5	5	5	5	0	0	10	10.4	5
4	Clear act, rules and regulation	8	9	4	3	1	1	17	17.7	4
5.	Increase in pay scale of the employees	9	13	3	1	2	4	21	21.8	3
6.	Other	2	1	6	6	0	0	3	3.31	6
							Σd <sup>2</sup> =14	96	100	

$$r = 1 - \frac{6 \Sigma d^2}{n(n^2 - 1)}$$

$$r = 1 - \frac{6 \times 14}{6(6^2 - 1)}$$
$$= 0.60$$

The correlation indicates that there is high degree of positive correlation between the tax experts and employees ranking regarding the important factor for effectiveness employment income tax revenue of Nepal.

Hence, it can be concluded that the important factor for effectiveness of employment tax are ranked by the preference of the respondents which are as follows:

- 1) Honest taxpayers
- 2) Honest tax officers
- 3) Increase in pay scale of the employee
- 4) Clear act, rules and regulation
- 5) Effective income tax administration

From the above ranking- honest tax officers is the most important factor to be considered for the effectiveness of remuneration tax in Nepal.

#### **4.2.7. Respondent view regarding to the exemption limit and people investment in life insurance / citizen investment trust.**

To know that respondents opinion about the exemption limit & people investment in life insurance & citizen investment trust. A question was asked "Has the exemption limit inspired people to investment in life insurance / citizen investment trust"? The responses are tabulated below.

Table 4.11

For the Exemption Limit & Investment in Life Insurance/Citizen Investment Trust

Response/Respondents	Yes		No		Total	
	No	%	No	%	No	%
1. Tax experts	29	97	1	3	30	100
2. Tax Employees	14	47	16	53	30	100

*Source: Opinion Survey, 2013*

Respondents were asked whether the exemption limit has inspired people to investment in the insurance/citizen investment trust 97 percent out of 30 respondents from tax expert group respondent the question positively. But most of the respondent 53 percent from tax employees group answered the question negatively.

### **Chi-Square ( $\chi^2$ ) Test**

#### **Null hypothesis (H<sub>0</sub>):**

There is no significance difference between tax experts and tax employees view regarding to the exemption limit and people investment in life insurance /citizen investment trust.

#### **Alternative hypothesis (H<sub>1</sub>):**

There is significance difference between tax experts and tax employees view regarding to the exemption limit and people investment in life insurance /citizen investment trust.

Level of significance	0.05
Number of rows	2
Number of columns	2
Degree of freedom	1
Tabulated value	3.841
Chi-Square statistics	0.595

Since chi-square test statistic 595 is smaller than tabulated value 3.841, Null hypothesis is accepted. This means that the view of tax experts and the employees is not significantly different.

### **Conclusion**

The visions of tax experts and tax employees on the employment tax are found to be similar in this regard. It means that both of them viewed that the exemption limit has inspired people to invest in life insurance and citizen investment trust.

#### **4.2.8. Respondent opinion regarding to the provision of exemption for remote area allowance.**

**Table 4.12**

**For the Provision of Exemption for Remote area Allowance**

Responses/ Respondents	Yes		No		Total	
	No	%	No	%	No	%
Tax experts	12	40	18	60	30	100
Tax Employees	3	10	27	90	30	100

*Source: Opinion Survey, 2013*

The table shows the controversial view of administrators and Tax Employees. In the response of the question whether the exemption for remote area allowance has inspired people to go and work in remote area 40 percent respondents from tax experts respond positively and rest of the respondents negatively.

**Chi-Square ( $\chi^2$ ) Test**

**Null hypothesis (H<sub>0</sub>):**

There is no significance difference between tax experts and Tax Employees view regarding to the provision of exemption for remote area allowance.

**Alternative hypothesis (H<sub>1</sub>):**

There is significance difference between tax experts and Tax Employees view regarding to the provision of exemption for remote area allowance.

Level of significance	0.05
Number of rows	2
Number of columns	2
Degree of freedom	1
Tabulated value	3.841
Chi-Square statistics	12.578

Since the chi -square test statistics (12.578) is greater than the chi- square tabulated value (3.841), null hypothesis is rejected. This means that the view of tax experts & Tax Employees is significant different.

## **Conclusion**

The vision of tax experts and Tax Employees is found to be different in this regard. Employee thinks that the provision of exemption in remote allowance has not inspired people to go and work in remote area. But tax experts view that people are somehow inspired by the provision.

**4.2.9. Respondent opinion regarding to the provision of exemption for medical tax credit provided by Income Tax Act, 2058.**

**Table 4.13**

For the provision of exemption for medical tax credit provided by Income Tax Act, 2058

Responses/ Respondents	Yes		No		Total	
	No	%	No	%	No	%
Tax experts	18	60	12	40	30	100
Tax Employees	3	10	27	90	30	100

*Source: Opinion Survey, 2013*

The table presented that almost all respondents from Tax Employees group - 90% are of the view that the exemption for medical tax credit facilities provided by Income Tax Act 2058 is not adequate whereas most of the respondents from administrator 60% said that they are adequate.

**Chi-Square ( $\chi^2$ ) Test**

**Null hypothesis (H<sub>0</sub>):**

There is no significance difference between tax experts and Tax Employees' view regarding to the provision for medical tax credit provided by Income Tax Act 2058.

**Alternative hypothesis (H<sub>1</sub>):**

There is significance difference between Tax Experts and Tax Employees' view regarding to the provision for medical tax credit provided by Income Tax Act 2058.

Level of significance	0.05
Number of rows	2
Number of columns	2
Degree of freedom	1
Tabulated value	3.841
Chi-Square statistics	14.286

Since the chi-square test statistics (14.286) is greater than the chi-square tabulated value (3.841), null hypothesis ( $H_0$ ) is rejected. This means that the View of tax experts & Tax Employees is significantly different.

### **Conclusion**

Tax Employees view that the provision of exception for medical tax credit provided by Income Tax Act 2058 is inadequate. But most of the tax experts view the provision to be adequate.

#### **4.2.10: Opinion towards More Appropriate Method for Assessing of Income Tax**

To know the respondent's Opinion about More Appropriate Method for Assessing of Income Tax The question "which method is more appropriate in Nepal while assessing income tax?" Was asked the responses received from the respondents are tabulated as follows.

Table 4.14

For more appropriate method of assessing of Income Tax

S.N.	Alternatives	Tax expert and Tax Administrators	Tax payers	Overall Points	%	Rank
1	Self assessment	22	19	41	32.53	1
2	Assessment on the best judgment	20	11	31	24.60	2
3	Assessment on the basis of account submitted by the Tax Employees	14	10	24	19.05	4
4.	Tax settlement commission	17	13	30	23.82	3
	Total			126	100	

*Source: Opinion Survey, 2013.*

While ranking together the Opinion of both groups the corresponding prioritized reasons for more appropriate methods for tax assessment are as follows:

1. Self- assessment
2. Assessment on the best judgment
3. Tax settlement commission
4. Assessment on the basis of accounts submitted by the Tax Employees.

From the above table it is concluded that the self- assessment is the more appropriate method for tax assessing of income tax. Calculation of Rank correlation:

S.N.	Alternatives	Total Point x	Total Point y	Rank for x (R <sub>1</sub> )	Rank for y (R <sub>2</sub> )	D=R <sub>1</sub> - χR <sub>2</sub>	d <sup>2</sup>
1	Self assessment	22	19	1	1	0	0
2	Assessment on the basis of best judgment	20	11	2	3	-1	1
3	Assessment on the basis of account submitted by the tax employees	14	10	4	4	0	0
4	Tax settlement commission	17	13	3	2	1	1
	Total						Σd <sup>2</sup> =2

Source: *Opinion Survey, 2013.*

Where, x = tax experts Y = Tax Employment

We have,

$$r = 1 - \frac{6 \sum d^2}{n(n^2 - 1)} = 1 - \frac{6 \times 2}{4(42 - 1)} = 0.8$$

The correlation indicates that there is high degree of positive correlation between tax experts and tax employees ranking regarding the more appropriate method for assessing of income tax.

#### 4.2.11 Specific objectives of income tax in Nepal

In order to know the specific objective of income tax respondents were requested to rank the responses on given choices. The question was "in your opinion what should be the specific objective of income tax in Nepal?" The following table shows the rank wise responses received from the respondents.

**Table: 4.15**

**Specific Objective of Income Tax in Nepal**

S.N.	Objectives	Tax Expert	Tax Employees	Overall Point	%	Rank
1.	To enhance the government revenue	16	17	33	35.94	1
2.	To meet the government expenditure	13	14	27	29.34	2
3	To achieve national economic development	12	9	21	22.82	3
4	To check inflation	6	5	11	11.9	4
	Total			92	100	

*Source: Opinion Survey, 2013.*

From the above table it is addressed that the specific objective of income tax in Nepal should be enhance the government revenue and other objectives are ranked follows.

1. To enhance the government revenue
2. To meet the government expenditure
3. To achieve National economic development
4. To check inflation

#### 4.2.12 Opinion towards Factors Responsible for Income Tax Evasion

In order to know the opinion towards the factors responsible for income tax evasion, the question was asked to the respondents. "In your opinion, what are the factors responsible for income tax evasion?" the responses received from the respondents are listed below:

**Table: 4.16**

#### **Opinion towards factors responsible for Income Tax Evasion**

S.N.	Alternatives	Tax Expert	Tax Employees	Overall Point	%	Rank
1.	Defective tax administration	18	19	37	25.7	1
2.	Inappropriate income tax policy	13	17	30	20.83	3
3	Loopholes in Income Tax Act	10	7	17	11.80	5
4	Lack of consciousness in Tax Employees	6	15	11	7.63	6
5	Corruption in tax authority	8	10	18	12.5	4
6	Lack of political	16	15	31	21.54	2

	commitment					
	Total			144	100	

*Source: Opinion Survey, 2013.*

From the table it is clear that the main factors responsible for income tax evasion is defective tax administration and other factors are ranked below in order of preference:

1. Defective tax administration
2. Lack of political commitment
3. Inappropriate income tax policy
4. Corruption in tax authority
5. Loopholes in Income Tax Act
6. Lack of consciousness is Tax Employees

From the above analysis we can conclude that tax administration should make more effective and provide political commitment to reduce tax evasion.

#### **4.2.13 Opinions towards Problem Faced by Employee while Income Tax**

To know the respondents opinion regarding the problems faced by employees while paying income tax the question was asked, the question was "What types of problem that employee faced while paying income tax?" The responses received from the respondents are tabulated below:

**Table: 4.17****Opinion towards Problem Faced by Employee while Paying income Tax**

S.N.	Problems	Tax Experts	Tax Employees	Total Points	%	Rank
1	Lack of knowledge about taxation (how to return file)	13	12	25	29.41	2
2.	Procedural complication	14	17	31	36.47	1
3	Weak and immature treatment by tax administration	4	5	9	10.58	4
4	Hesitation to pay income due to low income	10	10	20	23.54	3
	Total			85	100	

*Source: Opinion Survey, 2013.*

From the above table, it is known that most important problem faced by employees while paying income tax is procedural complications. While ranking together the opinions of both the groups, the corresponding prioritized problems are as follows:

1. Procedural complications
2. Lack of knowledge of taxation
3. Hesitation to pay income tax due to low income
4. Weak and immature treatment by tax administrators

#### 4.2.14 Opinion towards Increase the Income Tax Revenue

In order to know the opinion towards increase the income tax revenue a question was asked to the respondents. How can we increase the income tax revenue in Nepal?" The responses received from the respondents are listed below:

**Table: 4.18**

#### Opinion towards the Reasons to Increase Tax Revenue in Nepal

S.N.	Alternatives	Tax Expert	Tax Employees	Overall Point	%	Rank
1.	Educating Tax Employees	11	12	23	33.35	1
2	Simplifying tax laws	2	10	12	17.39	4
3	Incentives of regular tax employees	9	5	14	20.28	2
4	Timely assessment to tax	5	8	13	18.84	3
5	Imposing fines and penalties	4	3	7	10.14	5
	Total			69	100	

*Source: Opinion Survey, 2013.*

From the table it is clear that the main factor to increase the tax revenue from corporation is education and other preferences are ranked below in order.

- 1 Educating Tax Employees
- 2 Incentives to regular Tax Employees
- 3 Timely assessment of tax
- 4 Simplifying tax laws
- 5 Imposing Fines and penalties

From the above analysis we can conclude that each Tax Employees have to be given knowledge about tax. Tax Employees should have conclusion regarding about tax system. Simplifying tax laws is also important factors for increasing income tax revenue of Nepal.

#### **4.2.15 Opinion towards Major Problems in Income Tax System**

In order to know the major problems in income tax system of Nepal, respondents were requested to rank the responses on given choices. The question was " Which are the major problems in income tax system of Nepal?" The responses received from respondents are tabulated below:

**Table: 4.19**

#### **Opinion towards Major Problems in Income Tax System**

S.N.	Alternatives	Tax Expert	Tax Employees	Overall Point	%	Rank
1.	Inadequate economic policy	15	16	31	15.97	2
2	Inefficient income tax administration	17	18	35	18.04	1
3	complicated Income Tax	14	15	29	14.94	3

	Act					
4	lack of education to tax employees	7	10	17	8.76	6
5	lack of training to tax employees	12	13	25	12.88	4
6	difficulties maintaining account for tax purpose	6	10	6	8.29	7
7	lack of expert in tax management	5	8	13	6.70	8
8	Practice of tax evasion	8	12	20	10.30	5
9	Inappropriate rate and exemption limit	3	5	8	4.12	9
	Total			194	100	

*Source: Opinion Survey, 2013.*

From the above table it is clear that the major problem of income tax system is inefficient income tax administration and other problems are ranked below in order of preference.

1. Inefficient income tax administration
2. Inadequate economic policy
3. Complicated Income Tax Act
4. Lack of training to incentives to employee

5. Practice of tax evasion
6. Lack of education to Tax Employees
7. Difficulties in maintaining account for tax purpose
8. Lack of tax expert in tax management
9. Inappropriate rate and exemption limit

### Calculation of Rank Correlation Co-efficient

	Alternatives	Total Points x	Total Points y	Rank for x (R <sub>1</sub> )	Rank for y (R <sub>2</sub> )	D=R <sub>2</sub> - R <sub>1</sub>	d <sup>2</sup>
1	Inadequate economic policy	15	16	2	2	0	0
2	Inefficient income tax administration	17	18	1	1	0	0
3	Complicated Income Tax Act	14	15	3	3	0	0
4	Lack of education to Tax Employees	7	10	6	8	-2	4
5	Lack of training & incentive to employee	12	13	4	4	0	0
6	Difficulties in maintaining accounts for tax purpose	6	10	7	6	1	1
7	Lack of expert in tax management	5	8	8	5	3	9
8	Practice of tax evasion	8	12	5	9	-4	16

9	Inappropriate rate and exemption limit	3	5	9	7	2	4
							$\sum d^2=34$

Source: Opinion Survey, 2013

Where, X = Total expert

Y = Tax Employees

We have,

$$r = 1 - \frac{6 \sum d^2}{n(n^2 - 1)} = 1 - \frac{6 \times 34}{9(9^2 - 1)} = 0.72$$

The correlation indicates that there is high degree of positive correlation between tax experts and tax administrators' views and taxpayers' views ranking regarding the major problems in income tax system in Nepal. So, for effectiveness income tax system we should make efficient income tax administration.

### **Suggestion regarding employment taxation in Nepal:**

There was an open question is that "Have you any suggestion regarding employment taxation? Please specify, if any. The responses received from the respondents are given below:

- Dashain allowance, transportation allowance, dearness allowance and medical expenses paid by the employer should be made tax exempted.
- Taxpayers should be made aware of the taxation provision and tax planning.
- Increase penalties for tax defaulters, effective monitoring, encourage paying tax, simplified administration and making more progressive tax system help to collect more employment tax.

- Double employed employees should be bringing into tax net.
- Exemption limit provided for couple and family is not adequate as compared to existing inflation rate, individuals so exemption limit for couple should be increased.
- Attempts must be made simplify for tax procedure, tax tables and manuals with practical examples should be prepared and distributed on large scale to clear the provisions regarding employment income tax.
- The staffs who are working in private sector like hospital, nursing home, school and college and their other organization and earned taxable income must be brought into tax bracket for increasing tax revenue.
- Revenue administration should be made flexible.

### **4.3 Major Findings of the Study**

Following findings have been drawn out from the secondary data analysis and primary data conducted with tax expert and tax Employees, are as under:

#### **4.3.1 Major Finding from Secondary Data:**

- Nepalese revenue consists of tax and non tax revenues. Tax revenue is composed of both direct and indirect tax revenue. There is dominant role of indirect tax revenue in Nepalese tax structure. The contribution of direct tax and indirect tax to total tax revenue was 21.86% and 78.14% respectively in 2002/03, which became 24.73% and 75.27% respectively in 2011/12. It reveals that tax structure of Nepal is not justifiable on equity ground and progressiveness.
- Direct tax revenue consists of income tax, land tax, registration and miscellaneous i.e. urban house and land tax, vehicle tax and others. Among them, income tax has occupied first place regarding its contribution to total direct tax revenue of Nepal. From 2002/03 to

2011/12 the average contribution of income tax revenue to total direct tax revenue was 24.93%.

- Income tax has been considered as suitable source for mobilizing internal resources. It can be used as a positive instrument to boost up government revenue collection to develop the economic condition of Nepalese people and to fulfill resources gap problem.
- Income tax is collected from the income of public enterprise, semi-public enterprises, private corporate bodies, individual, employment and tax on interest. All those sector of generating income were in increasing trend except semi public enterprise tax. Among them, employment tax has occupied fourth position in total income tax. It has been increased from 4.08% to 14.56% during the period of 2002/03 to 2011/12. The average contribution of income tax from employment falls to be 10.09% of total income tax revenue.
- Resource mobilization is the main challenge in the developing countries. Nepalese economy is facing a serious problem of resource gap from early period. The gap has been widening every year

#### **4.3.2 Findings from Primary Data**

The major finding of the opinion survey is pointed out as below:

1. 56% of the respondents responded that all people were not well informed about tax system and only 44% of the respondents accepted that few people were well informed about tax system.
2. The vision of tax experts and tax payers is found to be different in this regard. Employee thinks that the provision of exemption in remote allowance has not inspired people go to work in remote area. But tax experts view that people are somehow inspired to work in remote area by the provision.

3. Tax payers view that the provision of exemption for medical tax credit provided by Income Tax Act 2058 is inadequate. But most of the tax experts view that amount of medical tax credit must be adequate.
4. All people of Nepal are not well informed about tax system and the more appropriate method for assessing income tax is self-assessment.
5. Defective tax administration is more responsible factors for being income tax evasion in Nepal and compulsory maintenance of account is the effective ways of controlling income tax evasion. Self-assessment of tax must be implemented effectively.
6. A specific objective of income tax in Nepal is to increase the government revenue and new area of income tax should be covered in course of collecting tax.
7. Major problem faced by the tax administration is undue delay in making assessment. So it should be reduced as soon as possible and a complicated tax law is also the problem.
8. Majority of the respondents opined that tax avoidance is practiced while paying income tax.
9. In Nepal many employees faced problems in paying income tax due to complicated system.
10. It is clear that provision of fines and penalties under income tax system must be implementing to collect more income tax.

## CHAPTER V

### SUMMARY, CONCLUSION AND RECOMMENDATIONS

#### Summary

Nepal is an agriculture based developing country with low per capital income, is facing serious problems of resource and fiscal gap. Thus leading the country toward poverty. Dependency of foreign aid and loan is continuously growing and yet it isn't enough to conduct development activities in the country. To meet the additional funds government has been using external and internal sources of income. Internal sources seem preferable because external sources are uncertain and guided by socio political motives tax and non tax revenue are major internal sources to collect government fund.

This study is about the tax revenue and is specific with employment tax. The specific objectives of the study were to review the tax structure of Nepal, to analyze the contribution of income tax from employment to public revenue of Nepal, to identify and analyze the existing problems and to suggest possible way to make employment tax effective and efficient. Various books articles description and other relevant materials were reviewed in order to get the clear idea for the research work. Various concepts of taxation have been discussed in the conceptual framework of study. Meaning of tax, classification of taxes, historical background of income tax and concept of employment tax has been taken into consideration.

Primary and secondary data have been used in this study. Opinion survey method has been used to collect primary data and economic survey for major secondary data. A set of questionnaires were developed and distributed among policy makers, professor, tax officers, auditors, accountants and employees working in various sector like bank, company, government office and private organization.

Data obtained from survey with the respondents have been tabulated and analyzed. Hypothesis have been set out and tested in order to see the similarity or dis-similarity in the options. Comparative analysis for different years has been done in the analysis part of the study, major findings of the study data have been put at the end of the related sub chapters.

The lists of the study and some recommendation have been given to increase the effectiveness of employment taxation in Nepal.

## **Conclusion**

Based on the finding of the study, following conclusions have been made.

1. Tax revenue has greatest share of contribution to internal sources of income than non-tax revenues.
2. Nepalese tax revenue consists of direct and indirect tax revenue. Tax has been heavily dominated by indirect tax revenue; among direct taxes, income tax has the largest share of contribution.
3. Income tax is collected from various sources of income; employment income is one of them. The contribution of income tax revenue is not satisfactory. It may be due to low pay scale of employee, inefficient implementation of act, loopholes on the provision, delaying tax assessment etc.
4. Employment tax is a suitable means of collecting government revenue according to opinion survey.
5. An action for promotion of employment tax contribution in total income tax isn't satisfactory. It is probably because of weak administration, complexity in income tax policy, lack of actions for promotion of employment tax.

6. Defective tax administration, unwillingness of tax payers to pay tax, lack of unconsciousness in taxpayers, hiding income, inappropriate income tax policy are the factors for responsible tax evasion.
7. Exemption, cost of living, inflation rates, pay scale of the employee's number of dependents, education expenses for children and medical expenses should be considered to adjust the exemption limit.
8. Various problems that hinder the payment of poor responses from tax administrations, mental pinch, unnecessary delays, complicated rules and regulation hesitation to pay because of low income etc should be attempted to be resolved.

To increase the contribution of employment income to income tax revenue of Nepal, the employee who is working in private sector should immediately be brought into tax net.

### **Recommendation**

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

1. Total tax consists of direct tax revenue and indirect tax revenue. Nepalese tax revenue is having dominated by indirect tax revenue. The direct tax revenue plays more significant role in the economic development of the country than indirect tax. New area of tax net should be brought into the direct tax in order to increase direct tax revenue.
2. Making the tax deduction at source is the most important provision to increase the share of employment income to tax revenue of Nepal and there is no chance to make tax avoidance.
3. Out of total tax revenue, the contribution of income tax revenue is very low. So the contribution of income tax revenue to tax revenue and direct tax revenue should be increased by controlling tax evasion, tax

avoidance practices by bringing new tax employees into tax brackets, launching tax incentives programs, tax revenue may be increased with the help of sound tax planning.

4. To generate more contribution from employment tax the slabs should be adjusted with the rate of inflation that all earners must compulsorily pay the tax without evasion.
5. Effective public participation is necessary to minimize the tax evasion. The tax authorities should do continuous effort in order to develop the positive attitude among taxpayers.
6. Tax rules and regulation should be clear, simple for all taxpayers as well as for tax administrators. Income assessment and tax collection provision should be made simple and clear, so that tax payers would be encouraged.
7. Factors like average cost of living, inflationary condition of the country pay scale of the employee number of dependents should be considered to adjust exemption to the individuals and couple allowance.
8. Effective implementation of the provision of fines, penalties and punishment should be made for income tax defaulter.
9. Income tax policy should be revised timely and the authorities involved in formulating income tax policy must have thorough knowledge about income tax. To ensure this regular and effective training system, reward prize and punishment system should be implemented.
10. Both taxpayers and staffs of tax officials must be friendly behave and should be morally and ethically sound.

## Appendix - I

### Questionnaire to tax experts / tax administrator & tax payers

Dear Sir

First of all, I would like to introduce myself as a thesis researcher of Prithivi Narayan Campus stating in the final year of MBS. As you know, the students of this level have to write a dissertation of the subject of their specialization in order to fulfill the partial requirement of master's degree.

The study entitled "*EMPLOYMENT TAXATION & ITS CONTRIBUTION TO GOVERNMENT REVENUE VALLEY*" under the MBS programmed, faculty of management, Tribhuvan University. This study aims to analyze the different aspects of knowledge regarding employee tax & income tax. It shall be highly obligated for your valuable, spontaneous, frank opinion & information of your institution which is certainly considered at the basic sources to meet the board goal of this research work. This information will be kept confidential & not referred to anybody with your information whatsoever.

I assure that the information you provide me will solely be utilized in research work. I hope for your kind co-operation and support with many-many thanks.

#### **Instruction**

You are requested to answer the following questions. There is more than one possible response in the following questions. Please put the tick mark on the appropriate answer & write response in the blank space & number i stand for the most important & vice versa.

Yours sincerely!

Name of student Shiva Raj Adhikari

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T.U. Red No.: 7-2-48-3954-2004

Roll No.: 79/065



- c. Unwillingness of taxpayers to pay tax
- d. Defective tax administration
- e. Procedural Complication
- f. Hiding income

4. How employment tax can be increased to contribute the income tax revenue in Nepal? Please rank the option.

- a. Increase tax rates
- b. Bringing new taxpayers
- c. Reduction in exemption limit
- d. Making TDS effects
- e. Increase pay scale of the employee
- f. Others: .....

5. What is the most important factor for effectiveness of employment tax in Nepal? Please rank.

- a. Honest taxpayers
- b. Honest tax officers
- c. Effective tax administration
- d. Clear act, rules and regulation
- e. Increase in pay scale of the employee
- f. Others: .....

6. Has the exemption limit inspired people to invest in life insurance / citizen investment fund?

- a) Yes
- b) No

7. Has the exemption for more area allowances inspired people to go and work in remote area?

- a) Yes
- b) No

8. Which method is more appropriate in Nepal while assessing income tax (please rank).

- a. Self assessment [   ]
- b. Assessment on the basis of best judgment. [   ]
- c. Assessment on the basis of account submitted by the tax payers. [   ]

d. Assessment by the tax settlement committee. [ ]

9. In your opinion, what should be the specific objective of income tax in Nepal (please rank).

a. To increase the government revenue. [ ]

b. To meet government expenditure. [ ]

c. To achieve national economic development. [ ]

d. To check inflation. [ ]

10. In your opinion, what are the factors responsible for income tax evasion (please rank)

a. Defective tax administration [ ]

b. Inappropriate income tax policy [ ]

c. Loopholes in income tax policy [ ]

d. Lack of consciousness in tax payers [ ]

e. Corruption in tax authority [ ]

f. Lack of political commitment [ ]

11. What types of problem faced by employee while paying income tax? (Please rank)

a. Lack of knowledge about taxation [ ]

b. Procedural complication [ ]

c. Weak and immature treatment by tax administrators [ ]

d. Hesitation to pay tax due to low income [ ]

e. Others (please specify) .....

12. In your opinion, how can we increase the income tax revenue of Nepal? (Please rank)

a. Educating tax payers [ ]

b. Simplifying tax laws [ ]

c. Incentives to regular tax payers [ ]

d. Timely assessment to tax [ ]

e. Imposing fines and penalties [ ]

13. What are the major problems in income tax system of Nepal (please rank)

a. Inadequate economic policy [ ]

- b. Complicated Income Tax Act , rules and regulation [   ]
- c. Inefficient income tax administration [   ]
- d. Lack of education to tax payers [   ]
- e. Lack of training and incentives of employee [   ]
- f. Difficulties to maintaining account for tax purpose [   ]
- g. Lack of experts in tax management [   ]
- h. Practice of tax evasion [   ]
- i. Inappropriate rate and exemption limit [   ]

Once again, I would like to hearty thank for your valuable co-operation.

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