

CHAPTER I

INTRODUCTION

1.1 Background of the study.

In economics, fiscal policy is the use of government revenue collection (mainly taxes) and expenditure (spending) to influence the economy. According to Keynesian economics, when the government changes the levels of taxation and government spending, it influences aggregate demand and the level of economic activity. Fiscal policy often attempts to stabilize the economy over the course of the business cycle.

Changes in the level and composition of taxation and government spending can affect the following macroeconomic variables, amongst others, in an economy:

- i Aggregate Demand and the level of economic activity
- ii Savings and Investment
- iii Income Distribution

Fiscal policy can be distinguished from monetary policy, in that fiscal policy deals with taxation and government spending and is often administered by an executive under laws of a legislature, whereas monetary policy deals with the money supply, lending rates and interest rates and is often administered by a central bank (Pokharel, 2008).

Government revenue is revenue (money/income) received by a government. It is an important tool of the fiscal policy of the government. Revenues earned by the government are received from sources such as taxes levied on the incomes and wealth accumulation of individuals and corporations and on the goods and services produced, exports and imports, non-taxable sources such as government-owned corporations' incomes, central bank revenue and capital receipts in the form of external loans and debts from international financial institutions. The sources of finance used by the central government are mainly taxes paid by the public (Parajuli, 2009).

Income taxes are important source of revenue to government in both developing and developed countries. But the amount of revenue to be generated by government from such taxes for its expenditure program depends among other things, on the willingness of the taxpayers to comply with tax laws of a country. The failure to follow the tax provisions suggests that a taxpayer may be committing an act of noncompliance Tax

non-compliance occurs through failure to file tax return, misreporting income or misreporting allowable subtractions from taxable income or tax due. Following the increasing cases of tax noncompliance, especially tax evasion and its consequences on the capacity of government to raise public revenue, great amount of attentions has been paid to the issue of tax compliance globally by public policy makers and researchers, from the past few decades till now. As part of these research efforts, Allingham and Sandmo (1972) developed a theory known as A-S models to explain tax compliance behavior. This theory was derived from Becker's (1968) deterrence theory. The general conclusion of the theory is that compliance depends largely on tax audit and penalty. However, the theory had been criticized for paying more emphasis on economic factors and ignoring completely social and psychological perspective of tax noncompliance (Fischer, 1993). Scholars suggested that tax noncompliance decision may be affected by factors not considered in the basic model, or may be affected in ways not captured approximately by the theory (Alm, 1999; Spicer and Lundstedt, 1976). The failure of the traditional theory to provide a comprehensive understanding of tax noncompliance created avenue for a research gap into the phenomenon. This research opportunity made many researchers (Andreoni, J (1998); Chan et al., 2000; Jackson and Milliron, 1986; Manaf, 2004; Yaniv, 1999; Torgler, 2003etc) to extend A-S model to cover other factors. In the first major work on tax compliance, Jackson and Milliron (1986) identified fourteen factors as factors influencing tax compliance and these fourteen key factors were later categorized by Fischer into four main determinants. However, Fischer et al. (1992) did not consider the fact that the relationship between tax compliance and some of its determinants may be moderated by other variable(s) as suggested in Kirchler et al. (2007). The present study contributes to tax compliance literature by taking advantage of the weaknesses noted in previous studies (Allingham and Sandmo, 1972; Chan et al., 2000; Fischer et al., 1992). First, the focus of the study is on individual tax compliance behavior in a developing economy. Secondly, the study further extended Fischer's model by incorporating the moderating effects of taxpayer's financial condition and risk preference. However, the study is primarily undertaken to determine the relationship between the business owner of SME's attitude and tax compliance behavior as well as the moderating effects of SME's financial condition and risk preference on the relationship. With respect to Nepal, it witnessed a very a

dynamic and favorable economic indicators stable prices, surplus balance of payments, average annual growth of 4 percent during the era of 90's but with the insurgency in the country the economic indicators turned out to be unfavorable as its effect in the long run Nepal being in the LDCs with the poverty and low per capita income (Khadka, 2001).

Hence, to carry out the development works the government needs to collect revenue sources of revenue may be external and internal. External represents grants, foreign loans, borrowings, etc. whereas internal sources are taxes, direct, indirect etc. they are the requirement for the healthy development of the nation as in external sources the nation has to pay interest and loan after certain time and when government borrows foreign loan, they have to abide the terms and conditions policies as per the lender though being policies favorable or unfavorable to the nation.

Tax revenue can also represent as tax and non-tax revenue. The examples of non-tax revenue are fees, royalties, administrative and business income etc. whereas tax revenue depends upon the fiscal policy, government policies, choices tax system and structure and how they are implemented. Taxation system is one of the most useful indicators inured to monitor and get the glance of the various economic indicators of the nation. Income tax, VAT, Excise duty, Sales Tax, Entertainment Tax, etc. are the examples and sources of the indirect tax. These taxes are indirect in nature. From the name itself it suggests the nature of indirect tax is the burden of tax is shifted to the ultimate customer. Surprisingly in the developing nation like Nepal the sources of revenue tend to increasing more from the indirect taxes than direct taxes (Kandel, 2009).

At present scenario of Nepal government Inland Revenue department VAT seems to be the important and reliable source of the government revenue earlier it used to be sales tax collected at manufacturing/import point leading to the narrow tax base collection, moreover tax evasion was also rampant. Hence, the implementation of more scientific and safer tax system was the necessity which led to the introduction of VAT. Value Added Tax (VAT) is an indirect tax and was the new concept when introduced some opposed it some proposed it with their different views and mentality however with the pace of time it emerged as the Nepal government's favored tax system. It replaced the impoverished taxes such as Sales Tax, Contract Tax, Hotel

Tax, and Entertainment Tax that were to be in use at that time. From the name itself it is clear that VAT is imposed on the process of production and distribution activities of the firm. Value Added implies the difference between the purchase and selling price as it calculates the entire expenses in the process of manufacturing/ preparing the goods and services ready for sale in addition with the profit margin. Unlike other taxes the characteristic of VAT it is imposed at each stage from import, manufacturing, wholesale to retail distribution. Government of Nepal implemented VAT formally after it was passed from parliament act at the beginning of F/Y 2054/55 has completed more than 18 years of implementation. (Inland Revenue Department, 2015) VAT has been the most favored choice for the developing nation like Nepal due to its reforms with the improved form of other notable taxes such as sales tax which led to revenue enhancement and economic efficiency. VAT being the multi- point tax provided number of opportunities for the Inland Revenue department to gain the access to different revenue points identify them. As it has been proven to be the important instrument for the mobilization of internal resources. Hence there is still scope of increasing revenue from VAT with widening the nature of business that are to be engulfed in the bracket of VAT. Moreover, the tax reform of VAT adoption is essentially connected with effort to increase the revenue for the government for the developing nations (Koirala, 2010).

1.2 Problem statement.

With the advancement of technology and science the world has been turned into a global village. World is moving towards the more advancement and sophistication of the 21st century. But in case of Nepal, it still lacks the effective mechanism for resource mobilization though the development has been witnessed but still the progress indicator is not noteworthy. Growing expenditure of deficit financing, heavy burden of external loan, widening gap of balance of payment with high import low export, deficit budget. The expenditure of the government has been increasing at a faster rate surpassing the revenue and this gap has been in the increasing trend year after year. The foreign grant and loan to the government calculated to be 13.84 percent of total expenditure. The drawback of these foreign grant's percentage increasing in the government total expenditure leads to its vulnerabilities in the economy of the foreign influence (Nepal, 2013).

Nepal's lower revenue collection which leads to poor mobilization is due to the defective system (Lamsal, 2016). It was anticipated that VAT could be the one of the dependable sources to tackle the problem of low revenue collection.

VAT in most of the countries were successfully implemented but in case of Nepal at initial days due to unstable government, inability of the revenue department not being able to make the audit system systematic and lack of awareness among the people also (Rawal, 2010).

During its initial days it used to be the topic of discussion between business community and the government regarding its advantaged and disadvantages. Issues such as design of VAT, its implementation, applicability and its effect among the denizens of the society were the outcry at its initial days therefore, it is important to evaluate VAT with the identification of the present problems not only through the theoretical aspect but from practical implementation aspect as well because in reality to generate the revenue the Inland Revenue department (IRD) needs to implement the VAT successfully in the market (Sapkota, 2009). VAT gap is the result of unaccounted systematic default of VAT design. Theoretically, it is simply a gap between expected and actual VAT collection, however, in practice it pictures the entire compliance level of VAT implementation. VAT gap arises due to evasion and fraudulent behavior of taxpayers. Some taxpayers intentionally search ways to evade tax while some unintentionally do. Especially small taxpayers often try to avoid tax to raise their saving and extend their business (Acharya, 2016). A conclusion can be derived from detailed studies that the issues that arises for the successful operation of VAT specially depends upon two factors, i.e., business owners' interpersonal aspect and the administrative policies and their ways of implementation. Hence, to explore and assess the reasons behind the deviation between expected and actual value of VAT revenue collected, a detailed and thorough investigation and analysis on the prevailing status of behavior and attitude of the (individual/business), regarding the knowledge of VAT among the small, medium enterprise owners' awareness among the provider of VAT invoice, attitude and behavior of SME owners with respect to VAT. The research questions posted for the purpose of this study were: -

- i What is the level of awareness vis-à-vis VAT administration among SME business owners of Nepal?

- ii What are the attitudes of SME business owners' regarding VAT administration in Nepal?
- iii What is the behavior of SME business owners of Nepal vis-à-vis regarding VAT payment?

1.3 Objective of the study.

The main objectives of the study are to assess the status of the VAT administration in Nepal. The other objectives are:

- i To identify the level of awareness of SME business owners in payment of VAT.
- ii To examine the attitude of SME business owners towards payment of VAT.
- iii To examine the behavior of SME business owners towards payment of VAT.

1.4 Rationale of study.

The collection of the revenue over the time has proven to be the daunting task as itself it requires the expenditure over the time to collect the revenue. On the other hand, the groundbreaking reality is the resource mobilization of the government has been low so there is increasing dependency on foreign aid as well. The drawback of external financing is that the economy becomes the vulnerable to the external financier they have their vested interest for their investment but on the other hand external aid are uncertain, inconvenient and not conducive for the overall development of the economy. But from the economic perspective it may not seem to be that much harmful as everything has its advantages and disadvantages but the past few experiences seem to be had negative effects more than positive. Thus, the government should seek for the resources generation on its own for financing the regular and developmental expenditures. The government can generate revenue from taxable as well as non-taxable sources where tax is considered as the main source of revenue generation and mobilization (Gerald, 2004).

In Nepal VAT has witnessed many twists and turns from its commencement period till now both favorable and unfavorable so far. In spite of all these circumstances VAT has been proven to be the strong and reliable source of internal revenue and has already been contributing 1/3rd of government revenue. VAT has been associated with the high ratio of general government revenue, grants to GDP of nation, whereas

sometimes argued as complex and costly tax system (Inland Revenue, Annual report 2015/16).

This study will be beneficial in terms of getting the idea about current taxation scenario, will be helpful to acknowledge about how well the individuals have understood the effective and efficient implementation of VAT system identifying the loopholes and ways to mitigate them. Beside these it would be helpful:

- i To understand the VAT collection and payment system.
- ii To analyze the attitude and behavior of tax payer towards VAT.
- iii Recognition of the problems that are faced during the implementation of VAT.

1.5 Limitations of the study.

Limitations in the research are identified as the act of controlling the size or extent of something. It can be expected that the weakness of the research would be the amount of the information, documents, and reports available for the study will be limited as far as it is discovered. The data collected from survey; interviews would be the additional information retrieved regarding the research. However, the findings of the research may not be applied to other nations, principles as data collected for the investigation would be primarily focused on the Kathmandu city.

Research is a careful, systematic and objective investigation conducted to obtain valid facts, draw conclusions and established principles regarding an identifiable problem in some field of knowledge (Clarke and Clarke, 2010). Facts, conclusions whatever the information are achieved on the basis of the participant will be honest in providing the information through the survey questionnaire without any biasness.

The limitations on this study can be listed as:

- i. Among three major sides of VAT i.e., consumer, tax authorities and businesses, only interpersonal aspect from SME business owner under business side was studied on this research.
- ii. This study is limited to the factors of VAT administration i.e., awareness, attitude and behavior of business person, other interpersonal aspects are not being studied on this research.
- iii. The findings of the research were primarily focused on Kathmandu Valley.
- iv. It is also possible that subjects may modify their behavior simply because they know that they are participating in an experiment.

1.6 Chapter plan.

Preliminary part of the report comprises the title page, certificate of authorship, approval sheet, acknowledgements, table of contents, list of tables, list of figures, abbreviations and abstracts. The main body part of this report consists of five sections namely: Introduction, Literature Review, Research Design and Methodology, Data Presentation and Analysis and Results and Conclusions. The subsequent part of this report comprises references and appendices where the questionnaire of this report and the outputs from SPSS 22.0 have been included.

Chapter I: Introduction.

Introduction of the chapter would give the synopsis of the study. This chapter states the problem objectives, introduction of the subject explanations why the problem should be solved and who will be interested in the solutions. Other sub-topics such as problem statement, purpose, research objectives, definitions, limitations.

Chapter II: Literature review.

This chapter deals with reviews of previous writing, studies, which are relevant to the problem being explored within the conceptual framework. It also presents the summary of previous major researches being studied under separate heads as well as explains the reason for choosing the respective literature for the critical review and identifying the problem statement needed for the study.

Chapter III: Research methodology.

This chapter discusses about the various methods and techniques applied for conducting the research. It basically discusses about what research design was used for research, what methods were used to carry out the data collection from respondents, processing, analysis, methodology used for the study.

Chapter IV: Results and discussion.

This chapter discusses about the findings, analysis used to process data collected for research. It also identifies the degree of relationship between various variables identified as independent and dependent for the study. The main objective is to conduct the analysis of various data gathered and find out the relationship between various factors that are identified.

Chapter V: Summary and conclusion.

Finally, this chapter summarizes the whole research finding and forwards the appropriate recommendations on the basis of the research. The summary of the findings reiterates the measures that are developed, explored from the research, data gathered and analyzed. It presents the data findings in a logical, rational manner to the problem area. Limitations to the study as well as recommendations for future research are also considered.

CHAPTER II

LITERATURE REVIEW

2.1 Introduction.

Value Added Tax (VAT) is the most popular consumption tax in the world at the present scenario. It has been spread across the world within the time span of 50 years and implemented by more than 150 countries. Countries as diverse as for example Canada, Nigeria, Vietnam, China, India, Australia, Argentina, Brazil in addition to European Union (EU) from where VAT originated have a form of VAT.

Idea of VAT came up during 1920's which is credited to German Businessman Wilhelm Von Siemens. What was just an idea over the years has since been built into the system by so called the father of VAT, Maurice Laure who was the joint director of French tax authorities. VAT was implemented in France during 1954. VAT at manufacturing level were introduced shortly thereafter in Cote d Ivoire, Senegal during 1960s around that time this French colonies became independent. Brazil during 1965 with its fiscal reform introduced the traditional VAT that applied at all level of production. Until 1965 VAT was not a worldwide success its expansion was limited to less than 10 countries as most general taxes in Organization for Economic Cooperation and Development (OECD) were retail sales tax. But by 1989, 48 countries primarily western Europe, Latin American and handful of developing countries had adopted a VAT. The spread of VAT in European countries was driven the fact that it is a prerequisite for membership of European Union. Its spread has accelerated since with strong support from the International Monetary Fund (IMF) as it has now been implemented in more than 150 countries where it often accounts for the one fifth of total tax revenue. In most of the countries it has been used to accelerate the revenues of the government but in few it has enabled reductions in income taxes and excises (Pokharel & Bhandari, 2014).

VAT, General Sales Tax (GST), Sales Tax are indirect taxes on consumption that applies to most business transactions. Unlike USA sales tax, VAT is in most countries charged on supplies of both goods and services. VAT is applied to the majority of business transactions at every level of supply chain from production through to the final sale of product to the consumer. VAT is charged on the entire value of the

supply chain which is generally the production cost plus the profit element. The standard rate is applied to most supplies of goods and services. However, many countries apply zero or reduced rates to certain or specific type of product categories or transactions like exports. The standard rate for VAT ranges globally from 3%-27% (Pokharel & Bhandari, 2014).

VAT is not considered to be cost for the most of the businesses as it is generally recoverable either by offsetting the VAT incurred against the VAT due to direct refund of the amount paid. Many businesses especially export trade might even regularly receive the payments rather than making the payments to the tax authorities. VAT is generally bear by the end customer because VAT is charged and collected at every stage in supply chain failure to understand requirements or apply of correct VAT rate could lead to irrecoverable VAT costs. Irrecoverable VAT can also be caused by other legitimate reason like exemption before final consumption in financial services (Carl, 1978).

In respect of international trade VAT systems generally follow certain key principles such as destination principle (exports are exempted from tax imports are levied tax) and neutrality principle (VAT burden should not lie on a taxable business etc.)

EU the genesis of VAT reviewed its system in 2010 with the consultation businesses and member states on the ways to improve the existing system towards the general direction forward. White paper on the future of VAT contains their strategy for next decade and further based on the results of the consultation.

Some of the key aspects of VAT are discussed below though VAT implemented by countries differ from each other they can be generally divided to two VAT systems similar to EU and VAT systems other VAT systems (Agarwal, 2004).

But however, VAT systems have common key aspects:

- i Scope
- ii Taxable persons
- iii Cross border transactions place of supply
- iv VAT rates
- v Exemptions
- vi VAT recovery input VAT, deduction and refund, partial exemption

- vii Obligations-registration, filing, payment
- viii Registration threshold
- ix Special Schemes

2.2 Theoretical review.

2.2.1 Design of VAT.

The VAT raises revenue in a neutral and transparent manner. Some experts suggest that VAT is the most effective instrument for generating government revenue and that marginal cost for raising funds for public expenditure through VAT is generally lower than compare to other taxes through which funds would be raised. The VAT's neutrality has also made it preferred alternative in the context of trade liberalization (decline in revenue due to dismantling of the trade barriers). Exports are normally exempted from VAT and imports are normally subject to VAT. VAT does not affect the competitiveness of the firm (domestic) to export. Further VAT is secure from the serious fraud in the domestic market as tax relies on stage collection mechanism in which successive tax payers are entitled to deduct the input tax on purchases and have to account for output tax on sales.

In the end the tax collected by the tax authority should be equal to the tax paid by the final customer to the last vendor, it is argued that this is an efficient tax system because revenue is collected throughout the chain of production system unlike in retail sales tax the revenue is lost if their evasion in the final stage. Moreover, economists also favor the VAT tax system because it is the tax on consumption not on the income hence which encourages the savings and investments in the economy (Raghuram, 2015).

2.2.2 Origins and global rise of VAT.

From relatively inauspicious beginnings in the early 20th century, the VAT has been adopted by more than 140 countries and at present context accounts for approximately 20 percent of worldwide tax revenue. Perhaps only the income tax provides a stronger example of 20th century tax policy convergence. As Sijbren Cnossen (2011) wrote, “the nearly universal introduction of the value added tax should be considered the most important event in the evolution of tax structure in the last half of the twentieth century.” As the only developed nation without a federal VAT, the United States remains the highest-profile exception to the trend toward VAT. This exceptionalism

persists in the face of a growing belief among U.S. tax policy makers that the introduction of a VAT is either inevitable, or at least a possibility in light of burgeoning federal government debt and spending commitments (Ebrill, 2001).

The origins of the VAT have never been settled between German businessman and an American economist. Attribution is variously accredited to one of two famous sources: the German businessman Wilhelm Von Siemens in 1918, or the American economist Thomas S. Adams in his writing between 1910 and 1921. Von Siemens's VAT concept was seen as a technical innovation that brought a key improvement to the turnover tax. VAT allowed for the recovery of taxes paid on business inputs and therefore avoided the cascading problems that arise with a turnover tax. While the innovation at that period was clearly important, but it hardly meant the revolutionary overthrow of the fiscal order on the other hand Adams saw the VAT as an alternative to the business income tax. He was focused on federal tax policy, and since there was no national sales tax his concern was not with technical modification to an extant regime but with a major alteration of the existing federal income tax system. The fate of the VAT in Western Europe and the U.S. has largely reflected the different motives of the tax's innovators. Germany, along with much of Western Europe, came to embrace the VAT as a superior technical modification to sales taxes already in place, and as an adjunct to the income tax. By contrast, U.S. policymakers' ambitious and intermittent pursuit of the VAT often as a proposed substitute for the federal income tax has remained fruitless (Kandel, 2003).

In 1954 the VAT was first introduced at a national level in France. Its original coverage was limited, and France did not move to a full VAT that reached the broader retail sector until 1968. Then the first full VAT was enacted in Denmark in 1967, although the country did not join the European Economic Community (EEC) until 1973. VAT adoption progressed in two major phases. The first occurred mostly in Western Europe and Latin America during the 1960s and 1970s. The rise of the VAT in Western Europe was accelerated by a series of EEC directives requiring member states to adopt a harmonized VAT upon entry to the European Union. The second phase of VAT adoption occurred from the late 1980s with the introduction of VAT in some high-profile industrialized countries outside the EU, such as Australia, Canada, Japan, and Switzerland. This phase also witnessed the massive expansion of VAT in

transitional and developing economies, most notably in Africa and Asia. The IMF and the World Bank are identified as key influences in the rapid adoption of VAT among these countries. Less has been said about the significant role of U.S. policymakers and agencies in case of promoting VAT. This activity includes the pioneering, albeit unsuccessful efforts of the Shoup Mission to introduce VAT during the post-World War II U.S. occupation of Japan and the prominent role played by the U.S. Agency for International Development (USAID) in promoting VAT through the provision of funding and technical assistance to developing and transitional economies. Ironically, what has been seen as U.S. tax policy experts have been at the forefront of exporting a tax reform abroad but it has consistently eluded them at home (Pokharel & Bhandari, 2014).

2.2.3 Value added tax in Nepal.

Among the SAARC countries, India was the first nation to introduce MODVAT (Modified Value Added Tax) in 1986 for manufacturing products. Whereas in order to correct excise duty Pakistan, Bangladesh, and Sri-Lanka adopted Value Added Tax in 1990, 1991, and 1998 respectively (Khadka, 2001).

In Nepal after the restoration of multiparty democratic system measure for economic reform were introduced. Tax reform was the part of it and VAT emerged as the main reform program. To bring the sustainable internal resource mobilization Nepal government adopted the policy to integrate the prevailing taxes under the VAT within the period of eighth five-year plan (1992/93-1996/97).

With the formal announcement in the budget speech of fiscal year 1993/94 and intentions there after introduced to implement VAT was declared. Preparation of VAT was initiated in September 1993 when for this purpose a steering committee task force was created in the sales tax and excise department in order to make the necessary preparation for the introduction of Value Added Tax. The financial assistance was provided by United State Agency for International Development (USAID) and technical assistance was provided by Harvard Institute for International Development (HIID) Harvard University, USA. The members from task force and the consultants from the HIID carried out the preparatory work jointly such as preparatory for VAT law, launched taxpayer education program, created organizational structure, personnel system, organized training, initiated computerized process, etc. However due to

announcement of 1994 midterm elections brought the slackness in the activities. With the formation of new minority government after the election the planning to introduce was further delayed due to appointment of Tax System Review Task Force and declared the decision would be taken on the basis of report submitted by the task force. As a result, the earlier task force which operated with the assistance of USAID was dissolved. But the report submitted by the newly appointed Task Force also suggested to implement the VAT. Therefore, the new government formed decided to introduce the VAT at its earliest as possible which resulted in the resuming of the activities that was previously suspended where HIID and USAID technical, financial assistance were being experienced.

Through the budget speech of 1996/97 Government of Nepal declared all the taxpayers are to be registered under the VAAT within 90 days from April 16, 1997 and the VAT commencement would begin from the fiscal year 1997/98(July 16, 1997). But with the change in the government after April 1997 the government decided to postpone the date to November 16, 1997 and as per the notice the Sales Tax registrants having an annual turnover above the threshold were to be converted into VAT registrants and other persons who were not registered under sales tax were to be registered within the specified date.

Even though with the passage of time and law a lot of difficulties and constraints were faced during the introduction and implementation of VAT in Nepal. Like any another country Nepal also needs the revenue to fulfill the functions of any independent nation. Generating revenue means primarily collecting the taxes, the taxes could be collected using the various forms of tax systems. In Nepal when VAT was introduced it seemed to best option as it would make possible to broaden the tax base to eliminate the cascading of tax, to create the investment friendly tax system, to have a simple modern tax system that exempts basic goods and exports so from the taxation the ultimate objective is to increase the revenue.

2.2.4 Types of VAT

VAT has been classified on several bases and it can be basically classified into three categories namely consumption type of VAT, income type VAT and production type of VAT. The difference among such types of VAT depends upon the treatment of capital goods purchased from other firms and the treatment of depreciation for the

purpose of tax base (value added). That is why, discussion is concentrated within the treatment of these two items for all types of VAT (Koirala, 2010).

a) Consumption type of VAT

If all capital goods (investments) brought from other firms are excluded from the tax base (value added) in the year of purchase, but the depreciation is included in the tax base, it is known as consumption type of VAT. It can be expressed in the following equation:

$$\text{Value-added} = \text{Wages} + \text{Interest} + \text{Rents} + \text{Depreciation} + \text{Profit} - \text{Capital goods purchased from outside (in the year of purchase)}$$

The above equation clearly shows that the tax base is consumption because investments are free from taxation. Under this type of VAT, investments are encouraged because it excluded from tax base. Similarly, imports are taxed whereas exports are relieved from tax. Thus, tax base for the nation under this type is equal to the domestic consumption. Nepal has adopted it with tax credit method from very beginning (Koirala, 2010).

b) Income type of VAT.

Under the income type VAT, capital goods purchased from outside suppliers are included in the tax base in the year of purchase but depreciation is excluded from the tax base. The following equation is presented to make clear ideas about the tax base under it.

$$\text{Value added} = \text{Wages} + \text{Interests} + \text{Profits} + \text{Capital Goods purchased from outside (in the years of purchase)}$$

Or

$$\text{Value added (tax base)} = \text{Sales-Purchase (excluding purchase of capital goods from outside in the Year of the purchase)} - \text{Depreciation}$$

The above equation clearly shows that the value added is equal to the consumption plus net investment. It means the tax base for the nation is the net national income that comprises the consumption and then net investment of all firms with in the country (Koirala, 2010).

c) Production type of VAT.

The production type VAT includes capital goods purchase from other firm in the tax base in year of purchase and also includes depreciation in the tax base. It can be expressed in the following equation (Koirala 2010).

Value added=Wages + Interests +Rent + Depreciation + Profits + Capital Goods purchased from outside (in the year of purchase).

Or,

Value added (tax base) =Sales – Purchase (excluding purchase of capital goods from outside year in the purchase)

The above-mentioned equation obviously shows that the tax is imposed both on consumption and gross investment (Koirala, 2010).

This means that value added by all firms with in country constitute the gross national product (GNP). That is why; the tax base of this type of VAT is conceptually equal to the GNP. Thus, this type of VAT is also termed as gross nation product type VAT.

2.2.5 Principle of VAT.

While considering the international trade, the principles of VAT have great significance. Whenever international trade between two countries is considered, cross boarder adjustment is necessary. For the purpose of imposing VAT, principle of VAT can be divided into origin and destination principle. Choice between those two principles largely depends on the goods and the policy of nation, accession of international trade, computing methods and types of VAT (Agarwal, 2004).

a) Origin principle.

Under this principle, goods and services are taxed at the place where they are produced or rendered irrespectively, whether they are consumed or not. It implies that all exports are taxable and all imports are not-taxable. Where there is border and cross-country trade, this principle gives performance to import goods and services over domestic production (Agarwal, 2004).

Countries with international boundaries don't prefer to have this principle while taxing. But these sorts of principle may be beneficial where common trade is existed

like European Union. Otherwise rest of the countries does not prefer this principle (Agarwal, 2004).

b) Destination principle.

Under this principle, goods and services are not taxed at the place where they are produced or rendered but the place where they are consumed. Alternatively, all imports are taxed while all kind of exports are exempted from tax. The main benefit arising out of this is nondiscrimination between import and internal production (Agarwal, 2004).

This is the most popular form of principle of VAT, adopted by large number of countries. This principle supports for export and many countries are eager to be best exporter, therefore, they follow this principle. The equal treatment is provided for imports and domestic production, which fulfills the criterion of tax being neutral.

2.2.6 Methods of computation of VAT.

VAT can be computed by following three methods:

a) Addition method.

In this method, the tax base is calculated by adding the payments made by the firm to the factors of production employed in turning out the production such as wages, interest, rent, royalties and profits. This method is very close to income type of VAT that includes the reward to all the factor of production in its base because all payments made for the factors of production have to be added. It creates complexities in calculating them in practice. Virtually no country has based the additive method. However, Argentina and Israel have used it in selected economic activities, such as banking and finance, where value of inputs and outputs are difficult to measure (Due, 1976).

b) Subtraction method.

Under this method, cost of production is deducted from the base value. In other words, value added is determined as net turnover that is obtained by subtracting the cost of materials from sales proceed. It is much closed to consumption type VAT. Theoretically; it looks simple and easy but it is very difficult to compute especially where multiple rates of VAT exist. Problems like ascertaining tax value in an accounting period may also arise (Due, 1976).

Above two methods are called direct methods because value added is computed directly either by adding the payments made by the firms to the factors of production or by subtracting the cost of production from sales.

c) Tax credit method.

Tax credit method is known as indirect subtraction method or invoice method. Under this method, input tax is credited from output tax and passed into next stage up to consumption level. Tax credit method is similar, to some extent subtraction method but the major difference among two are:

- i In the earlier method, the tax base levied in the different amount of tax on sales and tax on purchase, where as in the latter method; the tax is levied on the different amount of sales value and purchase value.
- ii Earlier method requires invoices, while latter does not require. If the tax rates are same throughout the production and distribution method, all three methods, give the same result.

Among the three methods of computation of VAT, the tax credit method is widely used in the world. This is because this method has several advantages over the other two methods, which are:

- i. The tax liability in this method is attached to it. It is technically and legally far superior to other methods.
- ii. The tax calculation of value added, which is a difficult task, is not necessary.
- iii. The tax credit method creates a good audit trail making and crosschecking possible.
- iv. It provides an effective way to completely free product such as exports from tax and makes boarder tax adjustment easier and possible.

2.2.7 Structure of VAT in Nepal.

a) Coverage.

Nepal has adopted a broad-based consumption type VAT using the tax credit method. Under this system, tax is levied on all types of goods and services, both imported and domestically produced except those specifically exempted by law. It is desirable to make the commodity coverage of VAT as wide as possible. So, all goods and services should be brought into the VAT net unless there is strong justification for their exclusion. In the case of service, there are different practices, however, in developing

countries like Nepal, the service sector is rather unorganized and not many services seem to be attractive from the revenue point of view. That is why; some economist recommended a selective approach rather than an integrated approach in the cases of service (Parajuli, 2009).

b) Exemption/ no VAT.

While it is desirable to make the coverage of VAT as broad as possible, there are reasons to exempt some transactions from this tax, particularly on administrative grounds. For example, it is not desirable to waste scarce administrative resources in chasing after very small vendors who are not organized seasonal and illiterate and do not keep any record of their business. They are scattered all over the mountainous country. It will be extremely difficult to bring them in to VAT net and the revenue gain may not be substantial. So, small vendors having on annual turnover up to the level of threshold may be exempted from the VAT (Parajuli, 2009). The exempted goods and services in the context of Nepal are:

- i Basis agriculture products.
- ii Goods of basic necessity
- iii Livestock and their product.
- iv Agriculture related equipment
- v Medicine, medical treatment and other health services.
- vi Education.
- vii Books, newspaper, printed materials and publishing.
- viii Culture and craftsmanship related services etc.
- ix Professional services.
- x Land and buildings.
- xi Betting, casino and lottery.

2.2.8 Zero rating VAT.

Zero rated areas consist of certain goods and services that are taxed at the rate of zero percent. The objective behind the introduction of zero rates is to relive some goods and services completely from taxation. It means that VAT is not levied on zero rated goods or services, but they are regarded as taxable goods or services. Zero rating is definitely a better method than exemption. It is generally levied in the case of exports, which need to be free completely from internal commodity taxation. Zero rating,

however, increases the burden considerably on the part of both at payer and tax administration to the requirement of maintaining books of accounts, submitting return and refunding the tax levied on the inputs of zero-rated items. So, in Nepal, zero rating should be limited to the exports and some international services only (Silwal, 2000).

a) Rates.

VAT can be levied both with single positive rate or multiple rates. Generally, VAT with single positive rate is desirable in order to make VAT system simple, because multiple rates make tax administration more complicated under this system (Shoup, 1978). There is need to classify commodities into different groups according to their rates. Moreover, in a developing country like Nepal many small vendors, who may not be sufficiently literate, sell a number of commodities. They may not be able to apply properly the different rates of various goods they sell. Multiple rates make the tax system inefficient from the economic point of view. It gives incentive to producers to divert their resources from higher rated to lower rated industries to save on tax payment. The multiple rates create scope for tax evasion that may result in considerable revenue loss. On the other hand, single rate makes VAT less costly, easy to comply and easy to administer.

2.2.9 Operation of VAT.

a) Registration.

The provision of registration is mentioned in the section 10 Value Added Tax act, 2052. According to this section, any person already engaged in any transactions of the time of commencement which requires to the nature of Value Added Tax is required to apply for the registration within 90 days from the commencement of the act. Similarly, every person wishing to engage into transaction after the commencement of the act is leaguered to apply for registration prior to beginning to engage in such transaction. However, vendors involving in business of goods and services that are free from Value Added Tax need not register for the purpose of this tax. It means vendors having taxable goods and services are required to register their transaction to IRD. But small vendors failing below the prescribed transaction are not compulsorily required to register for Value Added Tax. For this purpose, Value Added Tax laws

have prescribed the level of registration threshold. The existing level of registration threshold is Rs.5 million of annual transactions (VAT act, 2052).

Registration means registration for the purpose of VAT. Permanent Account Number (PAN) is provided to a taxpayer for income tax purpose. But a taxpayer having registration for VAT purpose, it is mentioned on the PAN certificate that certificate would be valid for VAT also with such effect from such date. A PAN holder is also supposed to be registered with the Inland Revenue Office (IRO) under income tax act but unless it is specifically mentioned on the PAN the taxpayer not need to register under VAT (Pokharel & Bhandari, 2014).

Registration can be different types;

i Compulsory registration.

Where the specific provisions, act and rules have been mentioned to follow this type of registration (VAT act, 2052).

ii Voluntary registration.

Any person whose supply of taxable goods not more than as prescribed by the threshold during the period of last 12 months it is not compulsory for him to register for VAT. But voluntarily he may apply for the registration and tax office can provide the registration number (VAT act, 2052).

iii Forced registration.

any person who is required to get the registration under the VAT does any transaction without registering its business then the tax office may instruct such person to get it registered under the VAT. Such instruction by the tax office binding that person to get it registered is called “Forced Registration”. The onus to prove that it is not necessary to get it register under the VAT lies to the taxpayer (Shrestha, 2005).

2.2.10 Tax invoices.

VAT is invoice-based tax. VAT registrant must issue VAT bill while selling for supplying goods or services. Such bill is known as tax invoice. The tax invoice requires the name and address of the seller and the purchaser, the seller’s PAN number and invoice number, the date of transaction and description of the sale including the number of items and mention of any discounts given. The tax invoices

are a crucial document for VAT as it establishes the seller's liability for tax and the purchase entitlement to credit. It is however, not necessary to specify the format and content of the tax invoice, taxpayers may be allowed to prepare format of tax invoice according to their requirement (Shrestha, 2005).

Tax invoice must be prepared in three copies- the first copy should be clearly identified as tax invoice. The original copy is to be given to the purchaser, the second copy for audit purposes and the last copy is use by the seller while preparing record of the transaction. Tax officers may grant permission for a VAT registrant to issue abbreviated invoice for retail sales up to the value of Rs.5000. The chief difference between the two taxes invoices is that on abbreviated invoice does not require the name and address of the purchaser. The registrants have the right to request detailed tax invoice, as they will not be able to claim input tax credits with abbreviated invoices. IRD may order tax payer to issue invoices by using cash machine or computer. The procedure in such case shall be as prescribed by the General Director of IRD. It will have anytime access to the database the tax payer. Invoice are also required to claim the input tax credit in the case of local procurement and import custom clearance form and custom payment slips are also required to claim input tax credit in case of import. A registered person may keep his record in computerized system and issue invoice through it after taking the approval from the Inland Revenue department (Silwal, 1997).

2.2.11 Accounting.

Value Added Tax is levied on value added at each stage of selling and distribution activities of taxable goods or services. It is taxed on the basis of transaction of taxable goods and services. The effectiveness of VAT depends upon the record and accounting of the transition. So, the VAT registrant requires to keep clear accounts of their transactions of purchase, the registrant person has to maintain records of the following information, document and details:

- a. Information as per VAT account,
- b. Records relating to trade accounts cash receipts and payments,
- c. Tax invoices and abbreviated tax invoices issued by registrants,
- d. Tax invoices and abbreviated tax invoices received by registrants,
- e. All document relating to his imports and exports,

f. Books of purchase and sales.

The VAT account is a monthly summary showing the course of the figures of viewed in the VAT return (Silwal, 1997). All the registered taxpayers are required to maintain following accounts:

a. Purchase book.

VAT registrants are required to maintain an account of their business purchase to VAT purpose. They have to record of purchase by invoice. At the end of each accounting period, VAT registrant must total the amount of taxable purchase/ imports tax, exempt purchase/ imports and the tax paid on purchase/imports (Silwal, 1997).

b. Sales book.

Similarly, VAT registrants are required to maintain account of their sales are also to be recorded for invoice basis. At the end of each accounting periods, VAT registrants are required to total the amount of taxable and tax collect on sales. If they make both taxable and exempt purchase and sales, they are then required to calculate the proportion inputs tax, they are entitled to the tax period (Silwal, 1997).

c. VAT account.

It is a monthly summary of taxable purchase and sales and VAT paid on purchase and sales. A taxpayer needs to keep an up-to-date account of transactions of the tax period under the section 18 and such accounts wherever placed shall be made available for tax officer upon the request.

- i. The account kept by taxpayer need to include:
- ii. The date of transactions.
- iii. The value of each transaction.
- iv. If the other party of transaction is registered their registration number and other prescribed matters related to transactions.

2.2.12 Deregistration of VAT (section 11 (1)).

VAT registration may be cancelled by anyone whose total taxable sales for consecutive calendar quarters is not up to the amount prescribe by the inland revenue department and who has been registered for a full fiscal year or by persons who no longer have commercial activities. Regarding the cancellation of registration, the VAT Act has mentioned the following conditions:

- i. In case of corporate body if the body is closed down, sold, transferred or collapses.
- ii. If the business is running under proprietorship with the owner dead.
- iii. In case of sole proprietorship if the owner dies.
- iv. In case of partnership firm, if the partnership is dissolved or any of the partner dies.
- v. If the distributor or producers stops selling or producing taxable goods and services
- vi. If registered mistakenly.
- vii. In case the registered person submits zero tax return continuously for one year or it has not submitted tax return till date.

2.2.13 Return filing (sec 18).

As per VAT act 2052 VAT is based on the self-assessment tax system. Tax payer himself calculates all the taxes. Every registered taxpayer requires submitting the return to the tax officer within twenty-five days after the close of tax period. Such return all have to be submitted whether or not a taxable transaction was carried out in that tax period

- i Failure to submit return in specified time is penalized;
- ii Nil return or credit return Rs. 1000 flatly.
- iii Debit return 0.05 percent per day of due amount or Rs. 1000 whichever is higher.

2.2.14 Tax credit.

VAT is grounded on tax credit method and it is due to this reason VAT is considered as improvised version of sales tax. In the absence of tax credit implementation then the complete benefits from VAT cannot be availed. VAT is a tax that is based on value addition and since this concept is implemented in practice through the medium of tax credit, the tax payer should be entitled to deduct the entire tax paid in connection to the transaction. If this is not allowed then it ceases to be VAT and just becomes a turnover tax. Under the VAT a registered tax payer has to collect the tax from sales at a specified rate and deduct the VAT paid on purchases and imports from the tax collected on sales submit the remaining to the government. This process of

deducting the tax paid on purchases from the tax collected from sales is called Tax Credit (Zee 1995).

All the tax paid on purchase of goods and services, including assets, stationery and other expenses, related to business are allowed to credit full amount from the output tax collected on sales. There are some good, which is very difficult to ascertain whether stated in rule 41(1), tax may not be deducted in respect to the following goods and services.

- i. Beverages;
- ii. Alcohol or alcohol mixed beverages such as liquors and beers; Petrol;
- iii. Entertainment expenses.

Some goods are used for the both purposes of the business and personal use. Tax paid of the following goods may be deducted on the following proportions.

- i On all aircraft, 40 percent of purchase value;
- ii On automobiles (any motor vehicle with three or more wheels used on a road for carriage of passenger, 40 percent of purchase value);
- iii On computer, 60 percent of purchase value.

2.2.15 Refund.

Tax refund is one of the important aspects of the VAT, hence it should be simple easy and systematic. A VAT registered person can deduct excess of tax paid (input tax) over tax collected (output tax) collected from sales in any tax period can be adjusted in the following month when tax to be paid or there is a provision of refund if tax cannot be adjusted for six consecutive months with the tax office. Similarly, there is the provision for VAT refunds to the exporters, diplomats, international organizations. They are allowed to claim refund immediately. Exporter having more than fifty percent export to total sales is treated as regular exporters (VAT act 2052/53).

2.2.16 Information technology.

For tax system to be friendly and conducive to the taxpayers as well as to the tax administration it should be backed by good and effective information technology. This is meet through the scientific information system which provides highly sophisticated and standardized services to the tax payers providing them with needed and adequate information at the right time and also to the management and the

decision makers. To meet this very purpose, a separate department called “Information Technology Section (IT Section), is separately installed in the revenue office also known as Management Information System (MIS) which does the following functions:

- i. Updating the taxpayers’ individual accounts.
- ii. Entering, Processing and preservation of the central data.
- iii. Processing of tax application form and related information.
- iv. Managing of integrated information between department and field offices.
- v. Preparation of master record in database format regarding tax collection, refund, tax credit, registration, de-registration and the business closure.

Managing and preservation of data and information for a long period. The IRD posts the data in taxpayers’ account and sends the result to the related Revenue offices. The information of taxpayer is kept confidential according to VAT Act. DANIDA VAT Project has contributed a lot to systematization of the MIS in Nepal (Adhikari, 2003).

2.2.17 Appeal.

If the taxpayer is not satisfied with the decision of tax assessment made by the tax officer taxpayer has the remedy to go for administrative review and apply the Director General (DG) for it. If it is not able to be sorted out within the stipulated time period in IRD or tax payer not being satisfied with the decision made by DG the taxpayer may appeal to the Revenue Tribunal within 35 days against tax assessment for the penalty charged by a tax officer of an order by the Director General relating to the suspension of this place of transaction. Before filling the appeal, taxpayer must deposit the disputed amount of the assessed tax due and the rest of the amount of the tax due plus the whole amount shall have to be deposited or a bank guarantee of the same has to be provided. The appeal to revenue tribunal and the procedures, conditions for it shall be as per Revenue Tribunal, 2030. Provisions related to administrative review and appeal are mentioned in section 31ka and 32 of VAT act.

Administrative Review is the procedure wherein assessment made by the tax officer or department is investigated that the assessment was done as per the legal provision to void the decisions that are illegal (Pokharel & Bhandari, 2014).

2.2.18 Fines and penalties.

Every taxpayer registered with VAT supplying goods and services has to comply with the fines and penalties are attracted. The registrant is liable to fine or penalties if the registered taxpayer fails to use the registration number or does not clearly display the registration certificate, fails to file a return, does not issue invoices, fails to keep an up-to date account of transaction, obstruct the visit by tax officer, prepare false accounts and invoices or attempts to evade tax. According to VAT Act, action is taken in case of the following:

registered taxpayer fails to use the registration number or does not clearly display the registration certificate, fails to file a return, does not issue invoices, fails to keep an up-to date account of transaction, obstruct the visit by tax officer, prepare false accounts and invoices or attempts to evade tax. According to VAT Act, action is taken in case of the following:

- i. Non-registration (those falling under taxable criteria)
- ii. Non-filers or stop filers who has tax due/arrears
- iii. Who has no VAT accounts and records as prescribed by the law?

The Act also has the provision of punishment to tax officers also if the tax officer is found to have made the assessment quite negligently or maliciously, the Director General has a full authority to take action against such a culprit (Khadka, 1997).

2.2.19 Rewards.

As per the VAT Act, if a person provides information that a tax payer has evaded or attempted to evade all or some portions of tax, to the IRD with showing solid evidence the informant will be rewarded with the amount equal to 20% of the amount of tax collected on that basis of such information. The DG oneself is responsible for rewarding the informants (Pandit, 1996).

2.2.20 VAT collection mechanism.

The producers and suppliers also act as the agents for tax collection on behalf of the Inland Revenue Department or VAT administration. They are the ones who collect VAT on sales and deposit the collected amount after crediting the tax (if any amount remains) in prescribed public treasury account. Tax should be collected in selling price (cost plus transportation and distribution expenses) with profit as well. Excise

duty, custom and other tax except income taxes is also included under the selling price. But the trade discount and trade commission are not included. Any individual or firm who are not registrant are not entitled to collect tax. In the present context of Nepal, if the taxpayer fails to deposit collected tax by regular system, the tax officer may implement various methods and measures to collect the tax arrears they may be as follows:

- i Auctioning the property owned by the taxpayer.
- ii Possessing the taxpayer's fixed and current account
- iii Deducting from the bank account
- iv Deducting the tax from the refundable tax amount
- v Deducting from the amount payable to taxpayers by Government offices or Government owned enterprises.
- vi Deducting from the amount payable by the third person with the prior approval of the taxpayer.
- vii Blocking the taxpayers' export-import business. (Adhikari, 2003)

2.2.21 Evolution.

VAT is a member of sales tax family. In 1997, it replaced existing sales tax, contract tax, entertainment tax and hotel tax. Sales tax was firstly introduced in 1965 and in 1966, sales tax act was imposed at retail level in 1968, the base of sales tax was reduced up to wholesale level in 1994. This tax was converted into VAT in 1997.

Retail level sales tax (RST).

Retail Level Sales Tax was introduced in 1965. Under this system, all the retailers were required to register for sales tax purpose. They had to add the value of product by imposing it on sales by billing system was required so that each copy of bill could be verified by the tax office. Retailers had to submit monthly and annual record to the tax office.

The tax was introduced without any preparation neither the tax officials nor the taxpayers were familiar with this kind of tax as the number of retailers was very high but illiterate.

Wholesale level sales tax (WST).

Retail Level Sales Tax created many problems, so it was replaced by wholesale level sales tax in 1968. Only the manufacturers and wholesalers were required to register. The tax was levied on the sales of wholesalers to retailers and retailers to consumers. This tax, in average, is more convenient because wholesalers are more organized and the number is manageable. So that tax administration is easy.

Import/manufacture level sales tax (MST).

Due to problems in the operation of WST the tax base was further reduced in 1974 to the level of import and manufacturing. Under this system, only manufactures and importers were required to register for the tax purpose. Some manufacturers were out of the tax net if they were cottage industrialists (Due and Carrie 1988).

2.2.22 Reasons for the adoption of VAT in Nepal.

Nepal introduced VAT for several reasons which are:

a) Revenue enhancement.

The base of manufacture level sales tax (MST) was narrow. The large number of exemptions granted on socio economic grounds and weak tax administration aggregated the problem (Khadka, 2000).

Some taxes like land revenue, house tax, vehicle tax, etc. has to be transferred to the local bodies to make these bodies financially autonomous. The relative share of custom duties has been decreasing due to the reduction on import tariffs in line with the adoption of liberal economic policies and with the membership of WTO after the implementation of the SAFTA, the problem will be more acute.

Therefore, Nepal will have to become fewer dependents on international trade and small service taxes for its revenue in future.

b) Broaden the tax base.

VAT will be broadening the base of Nepalese tax both legally and administratively. Legally, VAT brings the value added at the wholesale and retail level under the tax net and makes it easier to levy tax on the service sector. VAT broadens the base administratively as well as it minimizes the problem of understatement of import due to the "catch up effect". Under the VAT any understatement of taxable value at the

manufacturing point would be corrected on subsequent sales since the credit for taxes paid on purchases would be correspondingly lower. Further there may not be an incentive for VAT registered vendors to buy goods since they will not be able to obtain input tax credits. As VAT, provides an invoice and audit trail, it makes tax evasion more difficult. Furthermore, as VAT would be levied right through the retail stage, taxpayers will think that they might be caught at a later stage if they evade tax at an earlier stage (Khadka, 1997).

c) Tax reform.

The tax reform programmes are directed by the political, economic and social condition of the country. The major objectives of tax reform programs are mainly economic in nature. The major objectives of tax reform programs are to increase revenue collection, to make the tax system efficient, to make tax system simple and transparent (Khadka, 1997).

d) Removing the problem of sales tax.

There were many problems associated with the implementation of manufacturing level sales tax. Firstly, the manufacture level tax was levied on the profit margin of the manufactures, but not the profit domestic products. Secondly, the importers favored under valuation of imported goods as there was no provision of invoice system, credit method and tax, refund mechanism, which plays a crucial role on cross checking and checking of under valuation. Moreover, the registered vendors had no compulsion to keep their account, which lowered not only sales tax but also income tax as well (Khadka, 1997).

Hence, the defective sales tax discouraged domestic production in one hand and lowered the collection of tax from sales tax along with income tax and custom duties on the other hand. Therefore, to overcome such conditions, simple tax system was necessary which was no other than VAT.

e) Administrative efficiency.

The tax system of Nepal seriously lacks administrative efficiency. The administration uses of discretionary measures and lack of transparency in day-to-day administration resulted into arbitrary tax assessments, harassment of genuine taxpayers and opportunities for corruption. Taxpayers complain that tax officials give their approval only when they raise the prices. So, the reduction on price level was not possible because the taxpayers had to pay high tax on previously determined high price even though the market price was low (Khadka, 1997).

f) Promote economic growth.

Broadening the tax base will make it possible to reduce the rate of other taxes, including income tax and import duties, thereby making the tax system economically more efficient. VAT will improve the efficiency and competitiveness of domestic product in the international market by revealing exports from internal commodity taxes. Furthermore, as VAT will be levied only on value added, imports will be relieved from taxation, meaning that double taxation will be eliminated under VAT. VAT will improve the competitiveness of the domestic products in other ways as well. It is to be noted that the existing sales tax system discriminates against domestic products. The VAT makes the equal control for domestically produced and imported goods (Khadka, 1997).

2.2.23 Problems of VAT in Nepal.

a) Structural problems.

VAT can be levied on single rate or multiple rates. The choice may depend upon economic nature of a country such as revenue requirements, equity consideration and position of foreign trade etc. VAT with a single positive rate is desirable in developing country like Nepal. Because multiple rates make tax administration more complicated since, there is need to classify commodities into different groups according to their rates. Moreover, businessman has to keep separate record and information. In a country like Nepal, many small vendors who may not be literate and able to apply properly the different rates to various goods they sell. VAT is considered as broad-based tax, but all goods and services cannot be bought within tax net, various issues play important role in determining the tax base, so timely revision

of different VAT act regarding tax base is necessary, so as to increase the revenue mobilization (Shrestha, 2005).

The exclusion of certain goods and services from tax jurisdiction is known as exemption. There are three major areas, which has brought some troubles in administration in adopting the VAT is given as.

- i The goods and services of basic need such as medical and health services, milk, not processed food stuffs, vegetable, etc. are exempted with the equity consideration, but this provision increases their demand and the relative prices and the full impact of such exception will not be felt by the poor.
- ii Some goods and services are exempted because of the administrative complexity, under this provision, the small trades, farmers and special service firms are excluded from VAT. Farmers are exempted for its difficulties of proper records and financial fragility as well as to avoid the negative effects on primary products.
- iii The exemption technique might be used for selected goods and services to encourage their production and consumption such as educational and medical services, cultural activities, public transportation, sports, etc. Zero percent tax on goods and services is given to relieve some selected goods and services completely from taxation but such items are technically supposed to be remaining within the tax net. Zero rating technique is applied for the purpose of social welfare, to make export promotion and to support economic growth.

b. Administrative problems.

Effective and efficient tax administration is necessary for the proper mobilization of revenue. The Value Added Tax is directly administrated by the Inland Revenue Administration, the Ministry of Finance, Customs Administration, and Revenue Investigation Administration. The Ministry of Finance is the apex body of the tax administration. Therefore, for effective implementation, qualified intelligent, trained manpower is necessary and on the other hand, effective monitoring is essential but there exists traditional culture of tax administration corruption, lacks of proper

training, political intervention, so there is big gap between legal system and its active operation (Shrestha, 2005).

c. Problems related with tax laws and regulation.

There is no clear provision to take legal action against the person who does transaction without PAN. So, the attitude of general public towards tax administration is negative. The tax officials have to work in co-operation, there is no possibility of runaway the defaulter next tax payer provide improper bill to customer and evade tax in a large scale (Koirala, 2010).

d. Problem related to open order and unauthorized trade.

The other important problem is unauthorized trade and open boarder. People of both countries- Nepal and India are free to enter into each other's boarder, any goods and no paying customs for personal use. Beside that unauthorized trade is very much in the broader area. There are many organized groups active in both sides of the boarder and these groups are responsible for illegal supplying of goods from India to Nepal and Nepal to India (Shrestha, 2005).

2.2.24 Prospects of VAT in Nepal.

VAT is desired to achieve the goals of neutrality, revenue productivity, fairness and transparency etc. It is modern and effective tax system, which checks the loopholes, such as under valuation, non-recording and unauthorized trade. It discourages such issues and problems existing in the sales tax system. That's why VAT is considered to be the best fiscal tool for revenue mobilization, especially in an economy with acute shortage of resources. As Nepal is a member of the WTO network, the collection of custom revenue as major sources of revenue is low. On the other hand, there is less possibility of collection of huge amounts of income tax because of low per-capita income of Nepalese people, therefore VAT is found one alternate. Because of all these factors, Nepal has already adopted broad based consumption type VAT, using tax credit method. Despite the preliminary resistance, VAT is currently well received by customers as well as the business and industrial communities. There has been made a progress in revenue mobilization (Silwal, 1997).The prospects of VAT for the revenue mobilization can be outlined as:

a) Prospects of VAT revenue mobilization at various rates.

The present rate of VAT in Nepal is low, so the revenue mobilization from VAT could not take momentum. The performance of VAT has been criticized by comparing it with sales tax because it could not fulfill the revenue requirement of the government. If multiple VAT rate is implemented with adequate preparation and study, the revenue collection trend will increase more goods and services come under VAT net (Silwal, 1997).

b) Prospects of revenue mobilization by broadening VAT base.

To meet the growing expenditure of the government, it is necessary to increase the revenue mobilization through broadening the tax base. The base of VAT can be broadening by including the value addition that takes place at all sector and level of economic activities, within the preview of tax. In the present Nepalese context, the base of VAT can be broadening by bringing all goods and services and all sectors within tax preview i.e. taxing all commodities including zero rated goods and taxing agricultural products etc. and the exemption should be limited (Silwal, 1997).

c) Reducing the threshold level.

VAT is not applicable to all transaction. An annual threshold of Rs. 5 million in transaction has been specified for this purpose. But still there is strong argument that the present threshold is high. Because of high level of threshold only limited business vendors are registered, which is providing scope for the sales of smuggled or undervalued goods. Collection of all vendors will have to bring under VAT net; this is possible at low level. Although, it seems administratively difficult and socially unacceptable, it will be one way of giving the VAT revenue momentum. If the threshold level is too high, a majority of the businessmen may not come under the VAT net and under such circumstances will not possible to implement VAT effectively. Therefore, it is common to keep threshold level as low as possible. The threshold level should be fixed based on the administrative capacity, the capacity to maintain accounts in the industry and commercial sector, the need for revenue etc. Because of fragmented, self-subsistence economic structure and unorganized business sector, it is assumed that the number of business vendor having annual transaction less than Rs.5 million is many times more than the vendors having annual transaction above than Rs. 5 million. So, it is necessary to review the present threshold level.

Behind this, there is a huge prospect of revenue mobilization through improving tax laws and regulation, improving institutional and infrastructure development. Furthermore, tax friendly environment can be created by the government provoking education; information and knowledge to the tax payers (Silwal, 1997).

2.2.25 Need for tax reform.

Nepal introduces VAT in 1997 for several reasons. One of the important reasons is to develop a stable source of revenue by broadening the tax base. Nepal has been generating bulk of its tax revenue from import duties. However, due to the opening of the Indian economy since the early 1990s there has been drastic reduction in the import tariffs quantitative restriction and licensing system in India since 1991. Further, Nepal has reduced its imports tariff inline the liberal economic policies adopted since 1992/93 and in line with the customs duties reforms taking place around the world. Consequently, import duties will be less important than they were in the past. The process has already begun as the relative position of import duties decrease from 37 percent in 1990/91 to 34 percent in 1996/97. Furthermore, Nepal will not be in position to levy import duties on trade that takes place within the SAARC region after the implantation of the SAFTA. This means that Nepal will have to become less dependent on international trade taxes for its revenue, which is also desirable from economic resource allocation point of view. The base of the domestic trade taxes has been narrowed since the share of the total economy that flows through market channels is relatively small. The potential tax base become even smaller as sales tax used to be collected at the manufacturing point. The large numbers of exemption granted on sociopolitical grounds and weak tax administration only aggravated the problem. The narrow tax base has been eroded further due to compliance weaknesses that have tolerated the understatement of import price and smuggling. Since the sales tax was not levied at the stage of manufacturing point, there was no possibility of capturing the evaded tax at a point further down the trade channels. It has also been necessary to transfer some of the national level taxes, as land revenue, house tax, land tax and vehicle tax to the local bodies, in order to make them financially more autonomous. This means that there is no choice but to introduce VAT in Nepal to generate the revenue required to improve its deterioration macro-economic performance. VAT system is needed for revenue purpose as an attentive tax system to import tariffs. At the same time, the VAT system promotes the

interchanges of information between other tax systems, particularly trade taxes, as customs information is required. It determines the validity of input tax. VAT should not only be an effective instrument to generate substantial revenue at customs points, but also helps streamline tax policy in general. VAT has a natural link with the income tax. Currently, the main basis of the income tax assessment in the case of importers is the information supplied by the customs. But only a fraction of such information reaches the tax administration. VAT will provide the information on imports, local sales and input cost that can be used to assist in the effective implementation of the income tax. Besides, it is necessary to introduce VAT for several other reasons. The manufacturing level sales tax discriminated against the domestic products viz. imports because the profit margins of the manufactures were included under the base of this tax depends upon the final price irrespective of the promotion of value added at different stages in the process of production and distribution.

Further, VAT can be applied anywhere in the economic without leading to a cascading because it employs a credit mechanism. It also relieves exports completely free from the burden of taxation through the zero-rating of exports and the refund system for excess credit. The implementation of VAT in Nepal is also expected to establish an account based modern transparent tax system. Manufacturing level sales tax is not levied on the actual selling price but on the national sales value, which included to ex-factory price import value and the amount of excises/ imports duties. This means that the determination of the sales tax base invaded the problems associated with the determination of the base of the excise of import duties. In the case of domestic product, sales tax registered manufactures were required to get their price approved by the tax officials. In the case of excisable items, manufacturing has not only to get their ex-factory prices but also dealer, wholesale and retail level prices approved by the exercise authorizes. There is a possibility of either collusion or harassment prices negotiated between tax officials and taxpayers. There is general lack of administrative capability to determine the taxable value in realistic way (Khadka, 1997).

2.2.26 Attitudes and behavior.

The mobilization of revenue is a way for government to create fiscal space, providing essential public services for the smooth operation of public activities, reducing foreign aid and single resource dependence. However, the domestic tax bases in most of the countries are undermined by widespread tax avoidance and evasion (IMF 2011). Although taxpayer non-compliance is a continual and growing global problem (McKerchar and Evans 2009), many indications suggest that developing countries are the hardest hit (Cobham 2005; Fuest and Riedel 2009). Dealing with the problem of tax evasion requires at least some understanding of the factors underlying the individual taxpayer's decision whether to pay or evade taxes. However, little is known about tax compliance behavior in developing countries (Andreoni *et al.* 1998; D'Arcy 2011; Fjeldstad and Semboja 2001).

Studying what are the factors that determine tax compliance attitude and behavior is not only of academic interest; it could be important from a policy perspective. Attempts to broaden the tax base must build on insights into how citizens, tax payers experience and perceive the tax administration and enforcement, and whether and how their tax behavior is correlated with how they perceive the state. More systematic and coherent information on taxpayer attitudes, behavior, and awareness level are therefore required for better analysis and a more informed tax policy design. Tax knowledge is also significantly correlated with tax compliant attitude.

Attitudes.

According to Mowen (1987) and Ramayah (2002), the word "attitude" comes from the Latin term, *aptus* which means "fitness" or "adaptedness". Ramayah (2002) *as noted with consistency*, Thurstone's (1931) position, Fishbein and Ajzen (1975) conceptualized attitude as the amount of affect for or against some object. In recent years, the trend is to link attitude to the concept of feelings rather than beliefs. Mowen (1987) in his book entitled *Consumer Behavior*, defined attitudes as consisting of the following:

- i. Attitudes are likes and dislikes.
- ii. The "major characteristics that distinguish attitude from other concepts are its evaluative or affective nature".

- iii. Attitudes are the core of our likes and dislikes for certain people, groups, situation, object and intangible ideas.

According to Ajzen's (1991) Theory of Planned Behavior, attitude relates to one's own personal views about a behavior. Attitude may also be defined as positive or negative views of an "attitude object"; i.e., a person, behavior or event. In relation to taxation, taxpayers' attitudes may be defined as positive or negative views of tax compliance behavior. The outcome of positive views is tax compliance and negative views are tax noncompliance.

These views may be explained by Psychology-based theories which reveal that taxpayers' attitude may be influenced by the following factors which eventually influence taxpayers' behavior.

Models of taxpayer behavior (Merima Ali, 2013), includes the decision whether or not to pay taxes, tend to reflect one of five theories that can be referred to as:

Economic deterrence.

The economic deterrence theory states that taxpayer's behavior is influenced by factors such as the tax rate determining the benefits of evasion, and the probability of detection and penalties for fraud which determine the costs (Allingham and Sandmo, 1972; Becker, 1968). This implies that if detection is likely to happen and penalties are severe, then very few people will evade taxes. In contrast, under low audit probabilities and low penalties, the expected return of evasion is high. The model then predicts substantial noncompliance. Although the model has been criticized for focusing exclusively on the coercive side of compliance, at the expense of the consensual (Sandmo, 2005), there is some evidence to support the relevance of deterrence strategies to addressing noncompliance (McKerchar and Evans, 2009). For example, the fear of getting caught, or the probability of detection, has been found in some contexts to be an effective strategy to induce truthful behavior. The theoretical principles of economic deterrence have also been widely adopted by tax administrations when developing enforcement strategies that rely principally on penalties and the fear of getting caught.

Fiscal exchange.

The fiscal exchange theory suggests that the presence of government expenditures may motivate compliance and that governments can increase compliance by providing goods that citizens prefer in a more efficient and accessible manner (Cowell and Gordon, 1988; Levi, 1988; Tilly, 1992; Moore, 2004; 1998). Alm *et al.* (1992) note that compliance increases with the availability of public goods and services. Accordingly, the main concern of taxpayers is what they get directly in return for their tax payments to the government in the form of public services (*quid pro quo*). In this perspective, taxation and the provision of public goods and services are interpreted as a contractual relationship between taxpayers and the government (Moore, 2004). Individuals may pay taxes because they value the goods provided by the government, recognizing that their payments are necessary both to help finance the goods and services and to get others to contribute (Fjeldstad and Semboja 2001). The existence of positive benefits may increase the probability that taxpayers will comply voluntarily, without direct coercion. Although most taxpayers cannot assess the exact value of what they receive from the government in return for taxes paid, it can be argued that they have general impressions and attitudes concerning their own and others' terms of trade with the government (Richupan 1987). It is then reasonable to assume that a taxpayer's behavior is affected by taxpayer satisfaction or lack of satisfaction with taxpayer in terms of trade with the government. Thus, if the system of taxes is perceived to be unjust, tax evasion may, at least partly, be considered as an attempt by the taxpayer to adjust his terms of trade with the government. The fiscal exchange theory has received much attention and is well established theoretically. Empirical evidence to support the theory is, however, ambiguous (D'Arcy, 2011).

Social influences.

In the social influence model, compliance behavior and attitudes towards the tax system is thought to be affected by the behavior and social norms of an individual's reference group (Snively, 1990). It is reasonable to assume that human behavior in the area of taxation is influenced by social interactions much in the same way as other forms of behavior (*ibid*). Compliance behavior and attitudes towards the tax system may therefore be affected by the behavior of an individual's reference group such as relatives, neighbors and friends. Therefore, if a taxpayer knows many people in groups important to him who evade taxes, his commitment to comply will be weaker.

On the other hand, social relationships may also help deter individuals from engaging in evasion in fear of the social sanctions imposed once discovered and revealed publicly. Theoretical research on herd behavior in economic situations (Banerjee, 1992; Sah, 1991) also indicates that social influences may affect compliance, in particular by affecting the perceived probability of detection. One of the most consistent findings about taxpayer attitudes and behavior in Western countries is that those who report compliance believe that their peers and friends (and taxpayers in general) comply, whereas those who report cheating believe that others cheat (Yankelovich *et al.* 1984). Evidence suggests that perceptions about the honesty of others may affect compliance behavior.

Comparative treatment.

The comparative treatment model is based on equity theory and posits that addressing inequities in the exchange relationship between government and taxpayers would result in improved compliance (McKerchar and Evans, 2009). Citizens may not consider their relationship with the state in a vacuum where both parties are the only actors. Likewise, they may not think about their fellow citizens without considering their own relationship with the state. They may also consider how the state treats them relative to their fellow citizens. This judgment is likely to affect not only their judgment of the state, but also how they view their fellow citizens (D'Arcy, 2011). If the state starts to treat certain groups preferentially nepotism and favoritism, this may affect the people's mindset and color their relationship with the state and the group receiving favors. A crucial variable is then not just what a person gets from the state, but what the person gets from the state (and how the state treats the person) relative to those who are in the person's wider national community. This social psychology model highlights the importance of equity theory in the study of compliance and taxpayer behavior (D'Arcy, 2011).

Political legitimacy.

Finally, according to the political legitimacy theory, tax compliance is influenced by the extent that citizens trust their government (Tayler 2006; Kirchler *et al.* 2008; Fauvelle Aymar, 1999).

Legitimacy could be described as belief or trust in the authorities, institutions, and social arrangements to be appropriate, proper, just and work for the common good.

Political scientists have addressed how political legitimacy and civic identification are fostered argues that countries upon independence emphasized building national over ethnic identity have been more successful than those who allowed ethnicity to become the main animus of politics (Persson, 2008).

2.3 Empirical review.

2.3.1 Review of journal articles.

Dahal (1996) analyzed the tax structure and challenges of VAT in Nepal. The study used analytical as well as descriptive research design using secondary data for the analysis. Percentage, trend line, mean, standard deviation, correlation and regression were used as statistical tools. The study found out that that VAT was the most scientific, innovative and powerful tax with built-in quality of universal application for both developed and developing economies. The biggest virtue of VAT was that it was revenue buoyant and highly instrumental for resource mobilization especially in an economy with an acute shortage of resources. The research concluded that Nepal had entered into a major global tax system with the introduction of VAT. VAT was an account-based tax that led to transparency and accountability both as the part of taxpayers and collectors. Open border, non-magnetized economy, non-issuance of invoice etc. were the major problems that would marginalize the prospects for resource mobilization in Nepal. This called for the introduction of stringent regulations to deal with the delinquency of tax, maintaining records properly and improving efficiency of VAT administration.

Chau and Leung (2009) summarized and reviewed extant literature concerning Fischer tax compliance model. The study used analytical research design using secondary data for the analysis. The study found out that Fischer tax compliance model provided a framework to understand the influence of socio-economic and psychological components on tax payers' compliance decision. The study found income level and tax rates to be negatively correlated to tax-compliance. It concluded that a taxpayer with high income and high tax rates would have higher motivation to be aggressive in tax reporting. On the contrary, a taxpayer with high income but low tax rates would have lower motivation to be aggressive in tax reporting. The study suggested a partial refinement to this model by incorporating another important environmental factor - culture and the interaction effect between noncompliance

opportunity and tax system/structure on tax compliance. Furthermore, the review synthesized this topic so that it helped researchers identify gaps and consider promising future directions for further study.

Sancak, Velloso, & Xing (2010) examined tax revenue during the business cycle which estimated the relationship between tax revenue efficiency and the output gap. The study used analytical as well as descriptive research design using secondary data for the analysis. Percentage, trend line, mean, standard deviation, correlation and regression were used as statistical tools. The study found a positive and significant relationship between the tax revenue efficiency and the output gap; results were consistent for quarterly and annual data, and across advanced and developing economies. The study also found that a worsening (improvement) in the VAT C-efficiency was driven by shifts in consumption patterns and changes in tax evasion during contractions (expansions). A key implication was that, particularly during major economic booms and downturns, policy makers ought to look beyond simple, long-run revenue elasticity's and incorporate the effects of the economic cycle on tax revenue efficiency into their analysis.

Kumar & Sarkar (2016) studied the consumers' perception towards value added tax in Uttar Pradesh. The study used analytical as well as descriptive research design using primary data for the analysis. Ratio, mean, standard deviation and correlation were used as statistical tools and Uttar Pradesh was selected purposively as the study area with a sample size of 600 respondents following random sampling method. For the purpose of analysis and interpretation mean, standard deviation, correlation and ANOVA test were used as statistical tools. The study found out that the majority of the consumers paid tax but, they were not much aware of the VAT. Due to the high tendency of VAT, the consumers tried to avoid the payment of tax in U.P. The paper concluded that most of the consumers had poor knowledge of VAT in Uttar Pradesh irrespective of their level of literacy. There were some lacunas in the VAT management system like consumers tried to avoid payments of VAT when they got some benefit, dealers also refused to give cash voucher and consumers usually agreed to it, consumers felt as if they were betrayed by shopkeeper in the name of collection of tax and that was more harmful for the state's overall growth and development.

Botonka, Karunakaran, and Huka (2017) assessed the practices and challenges of VAT in Yirgalem town. Both primary and secondary data were used for the study purpose. Yirgalem Town was selected purposively as the study area. 83 tax payers were selected as sample respondents on the basis of simple random sampling technique. Structured questionnaire were prepared to collect primary data from the tax payers. Simple statistical tools such as frequency table and percentages were used for data analysis and interpretation. The study found out that majority of the respondents were not aware about the intricacies of VAT administration and thus had poor knowledge. However, more than 70 percent of the respondents perceived that VAT had helped them on issues related to sales, turnover, price reduction, governmental revenue and ease of accountability. Most of the respondents perceived that there was an improvement in VAT collection and their profession. Nonetheless, majority of the respondents disagreed on the service delivery mechanism of Yirgalem Revenue and Customs Branch Office. The study concluded that most of the tax payers had poor awareness and knowledge about VAT and its different dimensions in Yirgalem Town irrespective of their level of literacy. There was a gap of communication between the clients and RCA officers. It was recommended that the RCA office needed to use community radios with local languages to reach the vicinity clients with adequate information, short term training programs to be organized, periodical supervision and inspection needed to be undertaken by checking the transactions of the business.

Gnawali (2018) examined the taxpayers' knowledge towards value added tax in Nepal. The study used descriptive survey research design. Data were collected through questionnaires. Mean and percentage were used as statistical tools. The study found that more than 88 percent of respondents were aware enough to ask tax invoice after they purchased goods or services. Most of them asked for tax invoice to get the authenticity of sellers. VAT was successful and this largely depended upon the public awareness, honesty, faith and morality of tax officials and the business community. There was a need for willpower and action. It also found that taxpayers' awareness programme and tax education played a prime role to increase the VAT revenue in Nepal. The study concluded that VAT had broadened the tax base, eliminated tax cascading, created an investment friendly tax system, created a simple and modern tax system that exempted export and basic goods from taxation and finally increased revenue.

Dangal (2014) examined the value added tax in Nepalese context. This study used descriptive and comparative methods based on secondary data for the analysis. The study found that sales tax had been replaced by VAT since 1997 in Nepal. Department of VAT and its field offices were responsible for administering VAT functions that was not yet attractive and efficient. However, data showed that collecting VAT was in increasing order. In Fiscal Year 2014/15 it was NRs. 11516 crore which was 5.42 percent of GDP, 29.60 percent of total revenue and 48.14 percent of indirect tax revenue. And the contribution of VAT as percent of GDP remained at average of 4.04 percent during the study period (2002/2003 to 2014/2015). The study concluded that the value added tax was imposed on the value that business firm added to the goods and services that it purchased from other firms and on processing or handling those purchased goods with its own labour force or machinery, building or other firms. However, value added tax belonged to the family of sales tax. A general sales tax was a tax on sales transactions but it had been applied at only one stage of the business activities. Discussing the incidence of VAT in an open economy if demand was not inelastic, there remained the possibilities of exporting some of tax to non-resident factor owner.

Dahal (2020) assessed the contribution of Value Added Tax (VAT) in Nepal. This study was based on secondary data, which were incorporated from the Ministry of Finance and other related government as well as non-government organizations. Both analytical and descriptive statistics were applied as methods in this study. Statistical tools like regression, correlation, etc. were used to analyze data. The study found out that VAT had significant percentage in total revenue and total tax revenue in Nepal. There were more than 99 variations due to VAT in total revenue, total tax revenue and indirect tax revenue. All these relationships were significant as $r > 6$ PE everywhere. Thus, VAT had a significant contribution in government revenue of Nepal. The study concluded that the VAT was the effective system for the revenue collection of the country. However it was necessary to improve some policy of VAT system and increase awareness for the taxpayers about VAT system. It was recommended that the system of VAT needed to be improved to increase its effectiveness through the government policy level and increase awareness tax payers about baling system of VAT.

2.3.2 Review of previous thesis.

Ghimire (1998) assessed key issues on successful implementation of VAT in Nepal. The study used descriptive research design using both primary and secondary data for the analysis. Mean, standard deviation, correlation and regression were used as statistical tools and Kathmandu valley was selected as the study area with a sample size of 150 respondents following purposive sampling method. The study found that level of VAT evasion, VAT knowledge of taxpayers and VAT complexities had a significant impact on successful implementation of VAT. The study concluded that existence of open boarder and large amount of unauthorized trade from India to Nepal posed a great threat to the success of VAT in Nepal. Illegal imports helped form a channel which resulted in large scale of tax evasion. The study recommended that strong administration education program to relevant persons, training program to VAT personals, technical data base system, combination of various revenue teams, co-ordination of VAT department with other departments, close co-operation between government and private sector needed to be carried out.

Wagle (2010) investigated the contemporary issues on VAT system of Nepal. The study used descriptive research design using both primary and secondary data for analysis. Ratio, mean, standard deviation and correlation were used as statistical tools and Kathmandu valley was selected purposively as the study area with a sample size of 134 respondents following random sampling method. The study found that VAT knowledge had a significant impact on VAT administration, and VAT policy determined the ability of taxpayers in complying VAT, but awareness level of the general customers regarding the provisions of law of the country was found very poor. The research concluded that the major source of VAT collection was from the imports but was insignificant from small businesses as they felt it a matter of useless things and they were not getting knowledge from the competent authority on such issues. The main problem from the side of revenue administration was they were not friendly with tax payers and cooperation and help from the government official was very low for those who were willing to pay tax. Under invoicing by businessmen and corruption from the government officials were the main causes for VAT not being collected at an optimum level. The study recommended that awareness at consumer's level was very important so they felt their duty and responsibility to pay tax and contributed something towards the nation. The research further suggested that

taxpayers and customers who ignored the VAT system should be given proper knowledge about the VAT and its benefits and that knowledge of the people associated with VAT system should be developed well and they should be able to get all the facility given to them by Value Added Tax Act of Nepal.

Karn (2011) studied VAT administration and its effectiveness in Nepal. The study used analytical as well as descriptive survey research design. Both primary and secondary data were used for the analysis with a sample size of 180 respondents following convenience sampling method. Ratio, trend, mean, standard deviation, correlation and regression were used as statistical tools, and Kathmandu valley was selected purposively as the study area. The research found that VAT awareness, VAT knowledge, and penalties and service of tax authorities had a significant impact on VAT administration and its effectiveness. The study concluded that Nepal had different kinds of problem, constraints and challenges in all the sectors of VAT implementation such as administrative, political, geographical, social and economic, and others as VAT influenced the level of economic activities and other variables like price, wages, foreign trade directly or indirectly. The study recommended that officials needed to be motivated for the effective implementation of VAT. It was also recommended that the concerned bodies needed to have clear concept about the VAT and VAT bills be issued and taken. It was also recommended that the government needed to set up an effective and easy mechanism to pay and refund VAT, consumer to be awarded and that government needed a strong action plan.

Koirala (2011) analyzed the VAT implementation and its effectiveness in Nepalese economy. The study used descriptive research design with a sample size of 150 respondents following convenience sampling method. Mean and standard deviation were used as the statistical tools and Kathmandu valley was selected purposively as the study area. The study found that the level of awareness of the accountant and business persons paying VAT was at low level. Some provisions of VAT act and revenue administration had various issues. Implementation of VAT in Nepal was poor and those issues had a significant impact on VAT performance. The research concluded that there were many problems on VAT performance i.e., level of awareness of the accountant and businessperson was poor regarding VAT Act, their knowledge was very important so that proper use and implementation of VAT system

can be ensured. Likewise, revenue administration had some issues that could be improved with good attitude of people. The ineffective implementations of VAT in Nepal were due to the reasons of poor planning, unaccountable staffs, weak and corrupt bureaucracy, etc. It was recommended that different education programs, seminars etc. should be organized for taxpayers as well as general public in all over the country with the objectives to aware them about VAT which helped to bring more and more tax payers in the tax circumference. The research suggested that the VAT system could be developed by adopting automatic billing system. In order to make VAT effective, it was essential to create such an environment in which invoices were issued properly, accounts were maintained accurately, tax was based on transactions, and fair competition among industrialists and businessmen was established with respect to tax.

Tamrakar (2013) highlighted the legal provisions, practices, and contribution of value added tax to government revenue. The study followed analytical as well as descriptive research design and focused on secondary data. Ratio, percentage and trend lines were used as statistical tools. The research found out an increment in the collection trend of VAT; both internal and imports. Similarly, contribution of VAT to GDP and revenue collection also increased. The average contribution of VAT in total tax revenue, indirect tax revenue and GDP were 37.57 %, 47.99%, 7.5% respectively in FY 2011/12. The research also found out that the average numbers of VAT payers were increasing each year. The study concluded that double entry book keeping practices were prevalent in Nepal among businessmen for VAT evasion. VAT evasion by way of under invoicing, misclassification of commodities, omission of self-deliveries, tax collected but not remitted and concealment of stock position were major issues related to VAT evasion in Nepal. It was recommended that business houses needed to practice proper accounting standards and rules and proper books of accounts to be maintained, tax authorities to become strict in their rules and regulations and their proper implementation and the public to be more honest and true.

Neupane (2014) identified the effectiveness of value added tax in Nepal. The study used analytical as well as descriptive research design. Both primary and secondary data were deployed for the study purpose with sample size of 150 respondents which followed quota sampling. Kathmandu valley was selected purposively as the study

area. Ratio, percentage, mean, correlation and regression were used for statistical analysis. The study found that VAT had become one of the major sources of government revenue; VAT contributed 35% on the total tax revenue of the government in over past 10 years. Major contribution of VAT revenue come through VAT on import levied at the custom point. Out of domestic collection of VAT, major contribution was from production sector. The level of awareness of VAT system in Nepal was very low among small business and consumers. 50% of consumers had no knowledge about the VAT system of Nepal. Similarly, 13% businessmen did not know about the VAT system of Nepal. The research concluded that the habit of asking for VAT bill among consumers was low. Consumer's choice remained unaffected by registration status of seller. Businessmen found various difficulties to deal with prevailing legislation of VAT. Improper VAT charging, unreasonable demands of tax authority, stringent refund procedures were the major problems faced by businessmen. There were various loopholes in current VAT legislation. Under invoicing, import smuggling, difficulty in differentiating personal and business use and lower monitoring activities were regarded as major loopholes of current VAT practices in Nepal. Various corrective actions were available for sophistication of current legislation on VAT in order to control revenue leakage. It was recommended that corruption needed to be discouraged, the rules regarding issuance of VAT bill needed to be strengthened, and surprise visits at business premises and awareness on VAT needed to be increased.

Adhikari (2016) examined the effective implementation of VAT in Nepal. The study applied analytical as well as descriptive research design with the application of secondary data. Statistical tools used in the research were ratio, percentage, trend line, correlation etc. The study found out that the main issue was administrative incapability. It was concluded that although the government had tried many reforms in the field of taxation, no alternatives were effective because it lacked proper planning which led to administrative failure as there was a wide spread corruption and red-tapism. Also, proper records were not maintained. It was recommended that tax officials and business people needed to be honest and faithful and that every section of the economy needed to be accountable and responsible.

Haluwai (2019) analyzed the practical aspects of the implementation of VAT in Lalitpur district in context of Nepal. The study adopted quota sampling and included 90 tax payers, 30 tax administrators and 30 tax experts as sample respondents. Structured questionnaire had been prepared to collect primary data from the tax payers. According to the findings, in Nepalese context the revenue collection from VAT was in increasing trend, in an aggregate 2/3 of tax was collected from VAT. Internal VAT revenue was lower than external VAT revenue and tax administration was weak. The study concluded that the narrow tax base of previous sales tax failed to generate the minimum required amount of revenue because it included only imports and manufacturing units. Similarly, most of the goods and services were exempted from VAT. The income tax was decreasing slowly. The culture of doing business without maintaining proper books of accounts or maintaining multiple sets of books of accounts has made implementation of VAT difficult. The problem further intensified due to lack of culture of issuing and receiving bills at the point of sales and purchase, negative behavior of tax officials, and lack of sense of accountability in the government and political parties. It was recommended that proper billing for Vat purpose was needed, businessmen and tax administrators to be ethical and audit and investigation systems needed to be improved and effective, and those who did not follow the rules needed to be punished.

Poudel (2019) examined the tax payer's education regarding VAT collection in Nepal on 50 sole proprietors, 50 partnerships and 100 customers of Kathmandu Metropolitan City, deploying both analytical and descriptive research design. Percentage, trend analysis, mean, standard deviation and correlation were used as statistical tools. Knowledge about VAT, provision about VAT, policy of government regarding VAT and VAT paying system were the independent variables and awareness of VAT was a single dependent variable. The research found that contribution of VAT to government revenue was in increasing trend while revenue structure of Nepal and tax revenue of Nepal slightly fluctuated each year. Study also found that the majority of the tax payers had good knowledge on income tax and VAT. The study concluded that the implementation of VAT and its contribution was low in comparison with other headings and it was recommended that tax related education program to general people and training program to employees to aware them needed to be carried out.

2.3.3 Review of research report and other related literature.

Gerard and Naritomi (2018) examined Value Added Tax in developing countries: Lessons from recent research found out that VAT aided revenue mobilization, as they created incentives for firms to report accurate information in B2B transactions. But they still presented opportunities for evasion, production inefficiencies, and administrative difficulties. This paper also concluded that retailers often failed to report sales to final consumers. This non-compliance could be transmitted upstream along the supply chain which hampered revenue mobilization and that several countries had introduced policies incentivizing consumers to ask for receipts to improve compliance. They also concluded that electronic filing and receipts provided new enforcement opportunities to strengthen VAT systems.

EU (2019) report prepared for the European Commission, DG TAXUD under contract TAXUD/2017/DE/329 contained new estimates of the Value Added Tax (VAT) Gap for 2017, as well as updated estimates for 2013-2016. This study also reported the results of the econometric analysis of VAT Gap determinants initiated and initially reported in the 2018 Report (Poniatowski et al., 2018). It also scrutinized the Policy Gap in 2017 as well as the contribution that reduced rates and exemptions made to the theoretical VAT revenue losses. In 2017, growth in the European Union (EU) continued to accelerate with a combined real GDP growth of 2.5 percent, providing a sound environment for an increase in VAT collections. As a result, VAT revenue increased in all Member States. Increase in compliance contributed to an approximate 1.1% increase in VAT revenue. The VAT Gap share of the VAT total tax liability (VTTL) dropped to 11.2 percent in 2017 and is the lowest value in the analyzed period of 2013-2017. Of the EU-28, the VAT Gap as percentage of the VTTL decreased in 25 countries and increased in three. Overall, half of EU-28 MS recorded a Gap above 10.1 percent. The Policy Gaps and its components remained stable. The average Policy Gap level was 44.5 percent, out of which 9.6 percentage points are due to the application of various reduced and super-reduced rates instead of standard rates (the Rate Gap). The econometric analysis repeated after the 2017 study observed that the dispersion of tax rates and unemployment rate had a positive impact on the VAT Gap. Regarding the variables in hands of the administration, on the extended times series compared to the previous year, the results suggested that the nature of the expenditure of the administration, in particular IT expenditure, is more important that

the amount of the overall resources. Estimations made suggested that the downward trend would continue and that VAT Gap would likely fall below EUR 130 billion in 2018.

2.3.4 Summary of articles and thesis

Table 2.1

Summary of articles and thesis

S.N.	Author/ Year/ Country	Independent variables	Dependent variables	Sample size /method	Findings
1	Ghimire, (1998)	Vat evasion; Willingness of tax payer; VAT knowledge; VAT complexities.	Successful implementation of VAT.	Survey (n=150)	Level of VAT evasion, VAT knowledge on taxpayers and VAT complexities has a significant impact on successful implementation of VAT.
2	Chau and Leung (2009)		Critical review of Fischer tax compliance model		Income level and tax rates are found to be negatively correlated to tax-compliance further, these 2 variables may jointly have a negative interaction effect i.e., two variables considered together, which is over and above that of their individual impact, on tax compliance
3	Wagle, (2010)	VAT knowledge; VAT gap; VAT fairness; Consumers' willingness; behavior of tax authorities; VAT Policies	VAT administration	Survey (n=150)	VAT knowledge has a significant impact on VAT administration. Taxpayer's knowledge towards the VAT policy determines the ability of taxpayer's in complying VAT.
4	Parajuli,	VAT collection;	VAT Revenue.		The key issues on

	(2010)	Revenue Mobilization			collection of VAT revenue are administrative capability and situation, Nepalese businessmen are generally found not issuing the VAT bill and public are also not well educated in this matter.
5	Karn, (2011)	Taxpayer awareness, Knowledge, Tax penalties, Tax authorities service	VAT administration; VAT Effectiveness	Survey (n=180)	Taxpayers awareness, VAT knowledge, Penalties and service of tax authorities has a significant impact on VAT administration and its effectiveness.
6	Koirala, (2011)	VAT awareness; Attitude; VAT Education; VAT system	VAT performance	Survey (n=200)	Level of awareness of the accountant and businessperson paying VAT was at low level on some provision of VAT Act. Revenue administration has various issues that can be improved with good attitude of people. The implementations of VAT in Nepal have poor results than expectation. And those issues has significant impact on VAT performance which seems at a moderate level.
7	Tamrakar, (2013)	Legal provision; VAT practice; VAT contribution to government revenue	Successful implementation of VAT		Collection trend of VAT both internal and imports both are in increasing trend every year. Contribution of VAT to GDP and revenue

					collection is also increasing. The average contribution of VAT in total tax revenue, indirect tax revenue and GDP were 37.57 %, 47.99%, 7.5% respectively in FY 2011/12.
8	Neupane, (2014)	VAT awareness	Effectiveness of VAT	Survey (n=150)	The level of awareness of VAT system in Nepal is very low among small business and consumers. 50% of consumers do not know about the VAT system of Nepal. Similarly, 13% businessmen do not know about the VAT system of Nepal. The habit for asking for VAT bill among consumers is very low. Beside that VAT has become one of the major sources of government revenue; VAT has contributed 35% on the total tax revenue of the government in over past 10 years.
9	Adhikari, (2016)	Administrative capability; VAT gap;	Effective implementation of VAT in Nepal.		Administrative capability and situation has a significant impact on effective implementation of VAT, which led to a significant VAT gap.
10	Botonka, Karunakaran,	Awareness of taxpayers;	VAT Administration	Survey (n=83)	Majority of the respondents were not

	and Huka, (2017)	knowledge of tax payers; perception of tax payers			aware about the intricacies of VAT administration and thus having poor knowledge. Most of the respondents perceived that there was an improvement in VAT collection and their profession. Nonetheless, majority of the respondents disagreed on the service delivery mechanism of Revenue and Customs Branch Office.
11	Gerard and Naritomi, (2018)	VAT evasion; VAT revenue mobilization; VAT knowledge; VAT gap	VAT in Development countries		VAT had aided revenue mobilization, as they created incentives for firms to report accurate information in B2B transactions. Existence of opportunities for evasion, production inefficiencies, and administrative difficulties was still higher.
12	Gnawali (2018)	Tax Payers' Knowledge Towards VAT	Value Added Tax in Nepal	Survey (n=120)	The study found that more than 88 percent of respondents were aware enough to ask tax invoice after purchasing goods or services. Most of them ask for tax invoice to get the authenticity of sellers. VAT must be successful and this largely depends upon the public awareness, honesty, faith

					and morality of tax officials and the business community
13	Dangal (2074)	Historical development of VAT; Administrative capacity. VAT on Nepalese GDP	Value added tax in Nepalese context		Collection of VAT is in increasing order. In Fiscal Year 2014/15 it came to NRs. 11516 crore which was 5.42 percent of GDP, 29.60 percent of total revenue and 48.14 percent of indirect tax revenue. And the contribution of VAT as percent of GDP remained at average of 4.04 percent during the study period (2002/2003 to 2014/2015).
14	EU, 28-member state report, (2019)		VAT gap		Growth in the European Union (EU) continued to accelerate with a combined real GDP growth of 2.5 percent, providing a sound environment for an increase in VAT collections. As a result, VAT revenue increased in all Member States. Increase in compliance contributed to an approximate 1.1% increase in VAT revenue. The VAT Gap share of the VAT total tax liability (VTTL) dropped to 11.2 percent in 2017 and is the lowest value in the analyzed period of 2013-2017. Of

					the EU-28, the VAT Gap as percentage of the VTTL decreased in 25 countries and increased in three. Overall, half of EU-28 MS recorded a Gap above 10.1 percent. The Policy Gaps and its components remained stable.
15	Haluwai, (2019)	Structure of government revenue; Structure of VAT; VAT collection;	Implementation of VAT	Survey (n=150)	In Nepalese context the revenue collection from VAT is in increasing trend, in an aggregate 2/3 of tax collects from VAT. The culture of doing business without maintaining proper books of accounts or maintaining multiple sets of books of accounts has made implementation of VAT difficult. The problem is further intensified due to lack of culture of issuing and receiving bills at the point of sale and purchase, negative behavior of tax officials, and lack of sense of accountability in the government officials.
16	Poudel, (2019)	VAT and government revenue; Scenario of VAT; VAT awareness; Problems on collection and	Awareness regarding VAT collection in Nepal.	Survey, (n=200)	Contribution of VAT to government revenue was in increasing trend while revenue structure of Nepal and tax revenue of Nepal was slightly fluctuating each year.

		reporting of VAT			Also, the majority of the tax payers had good knowledge about income tax and VAT. Results showed that the implementation of VAT and its contribution was low in comparison with other headings.
17	Dahal, (2020)	Contribution of VAT; Trend of VAT; Correlation between VAT and total revenue.	Role of VAT in total revenue collection in Nepal.		VAT has significant percentage in total revenue and total tax revenue in Nepal. There were more than 99 present variations due to VAT in total revenue, total tax revenue and indirect tax revenue. All these relationships were significant as $r > 0.6$ PE everywhere. Thus, VAT had a significant contribution in government revenue of Nepal

2.4 Research gap.

The review of relevant literature has contributed to enhance the fundamental understanding and knowledge, which is required to make this study meaningful and purposeful. The main focus of this study is on individual taxpayer's VAT awareness, attitude and behavior towards VAT and how these factors lead to VAT administration. Review of different literatures revealed the different researches conducted in different period relating VAT and its administration, VAT gap and the things that led the VAT gap, both nationally and internationally in different approaches.

In the context of Nepal, very few efforts have been made to assess the issues regarding interpersonal aspect of individual and small business owning taxpayers.

Research of VAT knowledge, complexities, opinion regarding VAT system and rate on its administration and how these variables lead to compliance behavior have not been studied. Nepalese researchers have studied various aspects of VAT policy in Nepal but study of interpersonal aspect of taxpayers and its status has not been studied. It certainly stimulates the curiosity to know the level of VAT knowledge, attitude and behavior towards VAT. Are people aware about the VAT administration? Is taxpayer's attitude found to be in favor of VAT administration? And are people's behavior inclined towards VAT payment? Some of the major issues of the present study include, what people feel about the current rate of VAT and the level of people currently evading VAT.

Notwithstanding the importance of taxpayer's interpersonal aspects on compliance behavior, not much has been written on this issue in the Nepalese setting, except for few studies on general VAT application issues. Thus, this paper has tried to address this gap.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction.

The methodologies undertaken for the research paradigm is sampling process, data collection and analysis techniques to study the VAT administration in Nepal: Study of Awareness, Attitude and Behavior of SME tax payers. This chapter also explains about the data collection procedure and methodology used for the analyzing the data. Questionnaire development, method and procedure used for collecting data and analysis has been explained.

3.2 Research design.

This research lies into descriptive survey research. The data has been collected through formulating a set of questionnaires which was distributed among the respondents (Taxpayers). The questionnaire was self-administered. The findings have been derived from the data and facts provided by the respondent. The study was based on the statistical test such as mean, standard deviation and etc. The software called Statistical Package for Social Science (SPSS), Microsoft Excel were used to analyze and interpret the data. This software is widely used in the business setting with its easy-to-use user interface and easily available. The reliability scales test was carried out using Cronbach's Alpha test which is the best measure for multiple scale items and most popular for inter item consistency reliability.

3.3 Population and sample.

The population for the study comprises of all individual taxpayers doing business in Kathmandu. Here the population is too large to be investigated hence the small and carefully chosen sample of respondent is used to represent the population.

The sample of 130 individual from the commercial areas of the Kathmandu such as Thamel, New Road, Putalisadak and adjacent areas were chosen for the purpose of the study. The set of questionnaires were distributed to total of 150 respondents out of which 130 taxpayer's respondents responded. Convenience sampling was used for the study as it is one of the non-probability sampling methods.

3.4 Sources of data.

Primary source of data has been used to collect the data from the respondents. Under this study, a structured questionnaire was prepared and distributed to individual taxpayers and then these filled questionnaires were collected from the respondents. Respondents were selected carefully so that they have understanding of the subject matter to avoid random results. The preference for a questionnaire was based on the fact that respondents are able to complete it without help, anonymously, and it is cheaper and quicker than other methods while reaching out to larger sample (Bryman, 2008; Cohen et al., 2007).

3.5 Data collection procedure.

The questionnaire was used for the process of data collection. The respondents filled the questionnaire following the instruction given in the questions and then responses were collected from the respondent. The questionnaire was distributed on the basis of the convenience of the demographic factor.

The questionnaire was divided into three parts. The first section was the sociodemographic questions that aimed to know the basic information of those respondents, such as their gender, age, education, yearly sales.

The second section of the questionnaire focused on understanding the respondent's knowledge or level of awareness regarding VAT. The example questions like from when did VAT law came to affect.

The third section of questions was used to measure the relationships among the variances in research. Those questions were presented by a 5-point Likert scale, 1 being from strongly agree to 5 being strongly disagree. The main measurements included the awareness, attitude and behavior of SME business person regarding VAT.

3.6 Instrumentation of data collection.

The research was based on the primary data which was collected through the questionnaire and distributed to the respondents. The major tool used as instrumentation for primary data collection was questionnaire set using the conceptual framework and other secondary data such as journals, papers, graduate research project, reports, newspapers, websites, etc. But the major tool considered

was questionnaire. Altogether there are 23 questions including the multiple-choice questions. These questionnaires were distributed among the small, medium enterprise owners. The questionnaire had multiple response questions, 5-point Likert scale questions. Likert question is named after its developer Rensis Likert which was a widely rating scale question that required the respondent to indicate the degree of agreement or disagreement with each of series of statement. Each scale item of responses categorizes ranging from the “strongly agree” to “strongly disagree”.

3.7 Data analysis tools and techniques

After the completion of the data collection the information that were gathered, edited, coded, categorized and properly recorded in the SPSS, Microsoft Excel. Data were processed in a manner so that they were accurate and consistent with the intent information obtained.

For the analysis of the data several statistical tools were used to analyze the research responses. SPSS, Microsoft Excel were used to analyze interpret the data. For presentation of data several tools like table, diagrams, were used. Moreover, tools like mean, standard deviation were carried out to draw the inferences from the collected responses. The data were presented in depth interpretation as of questionnaire for the possible results and conclusions.

3.8 Validity and reliability

Validity of research design and plan was checked by the discussion with the experts along with the use of comprehensive research instrument to test before starting the real investigation. The questionnaire was developed after discussing with the supervisor. The items were carefully designed considering the questionnaire. The main purpose of validity and reliability analysis of data was to determine whether the is trustworthy or not.

Validity refers to how well the measurement truly represents characteristics that exist in the phenomenon being investigated. For the assurance of external validity measure were taken to collect the sample that was representative as far as possible.

The value range taken was 3. Generally, it was thought that value 3 is positive response. The values were less than 3 is considered positive and more than 3

considered negative as degree of acceptability ranged from 1 strongly agree to 5 strongly disagree.

After collecting data from the respondents Cronbach's Alpha coefficient was calculated to identify the reliability of the instrument used. This study adopted Cronbach's Alpha value as a tool for reliability examination. Based on the suggestion proposed by Guieford, (1965), the higher the Cronbach's Alpha value, the higher the internal consistency is. Cronbach's Alpha test is best used for multipoint scale items and it is also the most popular test for inter item consistency reliability.

Table 3.1

Reliability Statistics

Variables	Number of items	Cronbach's Alpha
Attitude	16	0.803
Behavior	14	0.836

Source: SPSS 22.0 calculations based on Field Survey 2020.

Reliability statistics was typically associated with internal consistency and its value range from 0 to 1. Sekaran, (2002) stated that Cronbach's Alpha coefficient less than 0.6 are considered poor, greater than 0.6 and less than 0.8 is considered acceptable and greater than 0.8 is considered good. Table 3.1 shows that Cronbach's Alpha of the research questionnaire asked to the respondent is above 0.8 that indicates the reliability of the instrument used in the survey was good. Similarly, for establishing the validity, the questionnaire was prepared under the guidance of a supervisor who oversaw the question making process and helps the researcher to come up with the standard set of question.

3.9 Data analysis.

The data has been statistically analyzed using software such as the Statistical Package Social Science Software (SPSS) and Microsoft excel were used. The responses were categorized, tabulated, processed and analyzed using different methods. Frequency distribution means, standard deviation was calculated.

The total responses collected from the respondent were coded tabulated into SPSS worksheet depending upon the nature of the question such as Likert Scale, multiple choice questions coding was as per the rule.

For reliability Cronbach's alpha was calculated. After finding the reliability data were analyzed using different tools. Mainly statistical tools such as frequencies, descriptive analysis was done for the purpose of finding. The conclusion recommendations were based on the findings.

CHAPTER IV

RESULTS AND DISCUSSION

This chapter contains the analysis, discussion, and interpretation part of the results based in data collected. The data collected were mainly through the questionnaire which were distributed to the respondents to be filled. The data were analyzed with the help of SPSS the data that were ascertained were presented with the tables, diagrams to make it convenient to interpret. The mean and standard deviation has been done to examine the significant relationship between the variables. To analyze the data tables, figures were extensively used.

For the convenience to understand this section has further been divided into different subsections. The first part deals with the demographic presentation which provides the detail about the respondent's gender, age, education, yearly sales, and marital status. Followed by the analysis, interpretation of the data collected through descriptive analysis and the final part with the discussion of the results obtained through analysis.

4.1 Results

4.1.1 Demographic presentation of survey.

This section deals with the demographic analysis and interpretation of the primary data that were collected through the distribution of the questionnaire to the respondents. This part helps to get the insight into the demographic characteristics of the respondents considered for the study. The questionnaire that was developed for the small and medium firm enterprise owners. The respondents profile includes gender, age, education level, yearly sales, and marital status. Total of 150 questionnaires were distributed to the respondents out of which 130 respondents responded to the questionnaire which shows the response rate to be 86.66 percent. The tax payers' respondents were the business person owner of the small and medium firm like shops, showrooms, small cottage industries, etc. of the Kathmandu city.

a) Gender of respondents.

For the purpose of survey, the questionnaire was distributed to the respondents especially the owners of small and medium size enterprises among which out of 130 respondents 86 were male respondents and remaining 44 were female respondents expressed in percentage represents male 65.4 % and female 34.6 % respectively.

Table 4.1***Gender of Respondents.***

Gender	Frequency	Percent
Male	86	66.2
Female	44	33.8

Source: Field Survey 2020

Results: From the table 4.1 it showed that 66.2% of respondents were male whereas 33.8 % of respondents were female among who responded the questionnaire.

Figure 4.1***Gender of respondents.***

1. Gender

130 responses

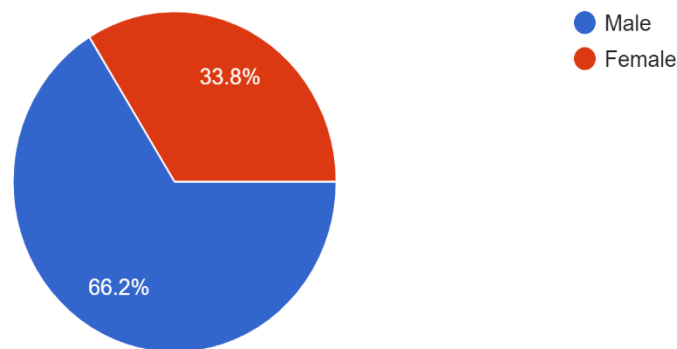


Figure 4.1 is the pictorial representation of the above table 4.1 where 66.2 % were male respondents and 33.8% were the female respondents. Study showed that SME enterprises are mostly owned by male compare to female.

b) Age of respondents.

For the purpose of survey as questionnaire were distributed among the respondents of different age group of SME business owners. The table 4.2 shows the age group and the percentage of the respondents.

Table 4.2***Age of Respondents.***

Age	Frequency	Percent
Below 35	63	48.5
35-45	60	46.2
45-55	6	4.6
Above 55	1	0.8
Total	130	100

Source: Field Survey 2020.

Table 4.2 shows the age group of respondents who were business persons where majority of are from age group of below 35 years representing 48.5 % of respondents, similarly the age of 35-45 years was 46.2 %, 45-55 years 4.6 %, and above 55 years 0.8%.

c) Education level.

The education level of respondents was different as per the respondent. The respondents have the minimum education qualification as Plus Two, Bachelor, and Masters and above.

Table 4.3***Educational Level.***

Educational Level	Frequency	Percent
Plus Two	25	19.2
Bachelor	71	54.6
Masters and Above	34	26.2
Total	130	100

Source: Field Survey 2020.

Table 4.3 shows the education level of different respondents. Among all respondents Bachelor level respondents were of highest number with 71 (54.6%), followed by Masters and above 34(26.2%) and Plus Two 25 (19.2%). From the above table it shows that Bachelor level qualified business person were the highest respondent for the Value Added Tax (VAT) survey who are interested to know more about VAT.

c) Respondents yearly sales.

From the table it shows the yearly sales of the respondents. As per the new VAT directive the threshold for the VAT registration is yearly sales of 5 million. Here the highest rate of respondent for the VAT survey is in the range of below 5 million with 73 respondents (56.2%) followed by sales range 5-10 million with 48 (36.9%) respondents and above 10 million with 9 (6.9%) respondents.

Table 4.4

Yearly Sales.

Sales	Frequency	Percent
Below 5 million	73	56.2
5-10 million	48	36.9
Above 10 million	9	6.9
Total	130	100

Source: Field Survey 2020.

Result: From the Table 4.4 it shows the yearly sales of the taxpayers' respondents. The amount of yearly sales were given the multiple choices for the respondent convenience. The yearly sales were given the alternatives of Below 5million, 5-10 million, above 10 million among which 56.2 % of respondents had below 5 million yearly sales, 36.9% had 5-10 million yearly sales, and 6.9 % had above 10 million yearly sales.

Figure 4.2

Yearly Sales.

4. Yearly Sales
130 responses

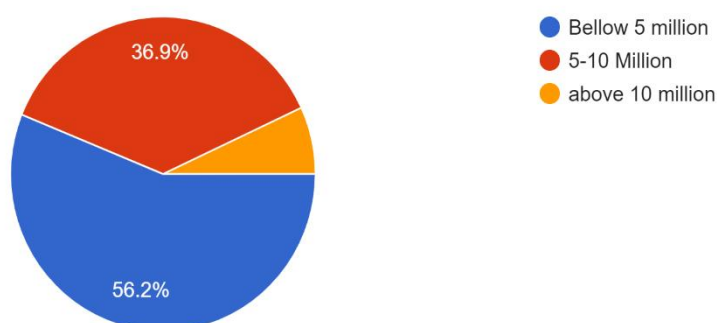


Figure 4.2 showed the yearly sales in the pie chart for better understanding of the respondent's yearly turnover sales.

d) Marital status.

Out of total 130 respondents 98 (75.4 %) were married whereas remaining 32(24.6 %) respondents were unmarried respondents. From the shown below it shows that married couples were more involved in the business rather than unmarried couples.

Table 4.5

Marital Status.

Status	Frequency	Percent
Married	98	75.4
Unmarried	32	24.6
Total	130	100

Source: Field Survey 2020

Result: From the table 4.5 it shows that 75.4 % of respondents were married and remaining 24.6% respondents were not married. It also can be ascertained that mostly small, medium enterprise taxpayers are married.

Figure 4.3

Marital status.

5. Marital Status

130 responses

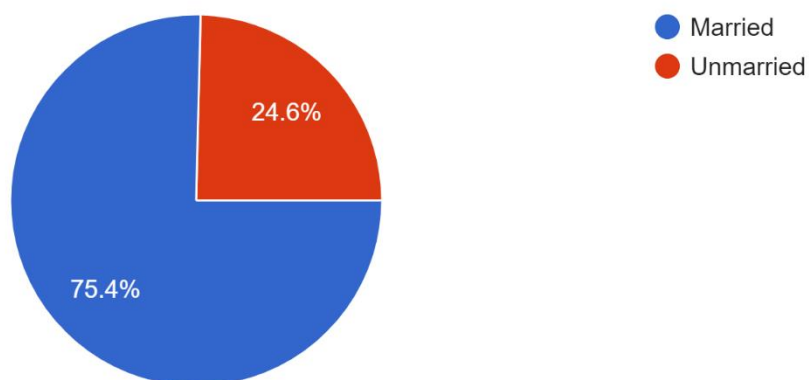


Figure 4.3 shows the pictorial representation of the marital status of the respondents with 75.4% respondents being married and remaining 24.6% with very few respondents being unmarried.

4.1.2 Descriptive analysis.

This section deals with the descriptive analysis of data collected through the questionnaire which were distributed among the respondents for the survey. Descriptive statistics is the discipline of quantitatively describing the main features of the data collected. Descriptive statistics simply summarizes about the sample observations the study at have been collected. In this research study there were many sub variables too within the business performance variable and other variables. The descriptive statistics helps to simplify the large amounts of data associated with these variables in a sensible way. For this purpose, the “Five Point Likert Scale” questions were asked to the respondents which scaled from Strongly Agree, Agree, Neutral, Disagree, and Strongly Disagree which is ranked from 1,2,3,4 and 5 respectively. Besides aforementioned remarks were provided accordingly 0-1 Strongly Agree, 1-2 Agree, 2-3 Neutral, 3-4 Disagree, 4-5 Strongly Disagree.

a) Awareness of business person (SME) towards VAT.

Questions relating to the VAT were asked in order to know the awareness of business person, taxpayers regarding the VAT. From the respondents answers it is known that business person was aware and conscious regarding the tax payment its genesis etc. As it is come to be known that the business person was aware about their duties, obligations but in return of the anticipation to ascertain something for the tax payment has led some discouragement but with respect to their duties towards the tax payment they seem to be very aware.

Table 4.6

Awareness of business person (SME) towards VAT.

Statements	Frequency	Percent
1. From when VAT law came to effect	73	56.2
2. Knowledge of yearly sales turnover (million) for a firm to register for VAT (goods trading)	124	95.4
3. VAT rate being implemented at the present context.	129	99.2

4. The true payers of VAT	125	96.2
5. What kind of tax is VAT	116	89.2
6. Last date for filing VAT	122	93.8
7. Following VAT updates	112	86.2
8. Aware about the impact of VAT to the industry.	109	89.9
9. Knowledge about the verification system of purchase and sales book for VAT.	96	73.8

Source: SPSS 22.0 calculations based on Field Survey 2020.

From the table 4.6 showed the awareness of business person (SME) regarding the VAT. With the knowledge of VAT rate mean being 99.2 percent of statement 3 it shows that people are very much aware of what they pay. With the lowest percent being 56.2% of statement first about the VAT law came to effect in Nepal, which shows people are not caring much about from when Nepal implemented the vat system. The second lowest percentage being 73.8% of the statement 9 about the knowledge of verification system of the purchase and sales book for VAT, which shows majority of people owning SME are not aware about the purchase and sales book verification system for VAT but 26.2 % of people that is around one-fourth of respondents are aware about the purchase and sales book verification system for VAT. Other than these all the statements are on range of near and more than 90% which reflects most of the SME are aware about the VAT.

Awareness regarding the commodities in the society that were affected by VAT were asked among the respondents to know about their perception regarding VAT and its influence on the price of the commodities. The people's perception is shown in the table below:

Table 4.7

Perception of business person (SME) regarding VAT effects on different types of commodities.

Goods	Frequency	Percent %
Luxury Goods	72	55.4
Infrastructure Goods	22	16.9
Necessity Goods	27	20.8

Utilities	9	6.9
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020.

The table 4.7 shows that business person (SME) has the perception of VAT being highly influential on the Luxury Goods followed by Necessity Goods, Infrastructure Goods, and Utilities respectively. Though VAT has been levied on all the aforementioned goods as per the VAT act of the country with respect to awareness of VAT among the people they consider it highly affects the luxury goods more. Question regarding the VAT refund system were asked among the respondents to know whether they have knowledge regarding VAT refund system. The data about the knowledge of people is shown in the table below:

Table 4.8

Knowledge of business person (SME) regarding VAT refund system in Nepal.

Statements	Frequency	Percent %
Having Knowledge	92	70.8
Little Bit	34	26.2
No Idea	4	3.1
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020.

The table 4.8 it shows that business person (SME) has the knowledge of VAT refund is being 70.8% that shows the majority of taxpayer are aware about the VAT refund system. Followed by having little bit knowledge being 26.2% and having no idea is being 3.1% that shows most of the SME's are aware about the VAT refund system in Nepal.

Question to know whether they have taken any VAT awareness workshop/seminar/meeting were asked among the respondents to know about their level of awareness the data about the awareness workshop of people is shown in the table 4.9:

Table 4.9***Responds of business person (SME) on VAT awareness workshops/ seminar.***

Response	Frequency	Percent %
Taken workshops before	52	40
Simple consultation	51	39.2
Not taken any workshops	27	20.8
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020

The table 4.9 shows that business person (SME) who had taken the VAT awareness workshop/seminar/meeting before are being 40% and of people taken some consultations are being 39.2% those are almost of same level of people; some had taken workshops and some had gone through consultation as per their need. The remaining percentage of people being 20.8% had not taken neither workshops nor any consultation. If we divide them by direct categories, we simply can say 40% of people are aware, 39.9% people are moderately aware and 20.8% of people are unaware about VAT awareness.

Question to know whether they have taken any VAT preparedness workshop/seminar/meeting were asked among the respondents to know about their level of awareness. The data about the preparedness workshop of people is shown in the table below:

Table 4.10***Responds of business person (SME) on VAT preparedness workshops/ seminar.***

Responses	Frequency	Percent %
Taken workshops before	51	39.2
Simple consultation	59	45.4
Not taken any workshops	20	15.4
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020

The table 4.10 shows that business person (SME) who had taken the VAT preparedness workshop/seminar/meeting before are being 39.2% and of people taken

some consultations are being 45.4% which is higher than those taken workshops for VAT preparedness that shows people are less aware about VAT preparedness though they are taking consultation as per their need. The remaining percentage of people being 15.4% had not taken neither workshops nor any consultation about VAT preparedness. If we divide them by direct categories, we simply can say 39.2% of people are aware, 45.4% people are moderately aware and 20.8% of people are unaware about VAT preparedness.

b) Attitude of business person (SME) towards VAT payment.

While going through the respondent's questionnaire overall attitude towards their responsibility regarding tax payment had been found to be positive. The attitude of the business person was measured through mean, standard deviation which is shown in the table below:

Table 4.11

Attitude of business person (SME) towards VAT with mean reference.

Statements	Minimum	Maximum	Mean	SD
1. I always issue VAT invoice to my customers.	1	5	2.02	.797
2. I acknowledge my responsibility towards my tax payment.	1	4	1.56	.647
3. I and my customers feel VAT as a regular cost.	1	5	1.89	.750
4. My business clients prefer to carry out the business through issuing VAT invoice.	1	5	1.75	.740
5. I have the tendency to show the true financial report to tax administration.	1	5	1.50	.707
6. I prefer the tax audit to be carried with strict rules and regulations.	1	5	1.55	.648
7. I prefer for every import and export trading VAT registration is must irrespective of goods and service nature.	1	4	2.04	.884
8. I perceive tax offices provide prompt, quick and reliable service.	1	5	2.52	1.143
9. In case of fraud and manipulation cases, I prefer tax offences and penalties should be high.	1	3	1.49	.517
10. I find it difficult to accept any change of a rule or tax system.	1	4	1.58	.633
11. I pay tax dues for the privilege of membership in an organized society.	1	4	1.85	.759

12. I would stop paying tax if I had the opportunity of not being discovered.	2	5	4.43	.767
13. I think VAT is the appropriate tax system for traders of Nepal.	1	5	1.73	.691
14. I think people need to be trained for vat preparedness.	1	3	1.72	.584
15. I think vat planning is essence for any business houses.	1	4	1.68	.638
16. My current accounting system have the interface that is updated with vat parameters.	1	5	2.01	.665

Source: SPSS 22.0 calculations based on Field Survey 2020.

The table 4.11 shows the statement 5, 6 and 9 are very close to strongly agree parameter where the business person (SME) tend to acknowledge and abide by their tax paying obligation. Overall the attitude pattern towards the VAT payment of taxpayers seem to be positive as the lowest mean value tend to be 4.43 where the payers were asked whether they will stop paying tax if they had the opportunity of not being discovered, this shows the positive attitude towards the VAT administration, the second lowest mean vale is 2.04 which is of the statement 7 where they were asked whether they prefer for every import and export trading VAT registration is must irrespective of goods and service nature. Which is also a positive response towards the VAT administration as 2.04 is so near from the parameter 'Agree' about the statement.

c) Behavior of business person (SME) towards VAT payment.

After the attitude another variable behavior of tax payer towards VAT was evaluated through the distribution of the questionnaire.

Table 4.12

Behavior of business person (SME) towards VAT payment with mean reference.

Statements	Minimum	Maximum	Mean	SD
1. I pay my taxes on time to avoid payment of unnecessary fines and penalty.	1	5	1.68	.574
2. I have the sense of responsibility and maintain transparent VAT accounts.	1	4	1.49	.600
3. I maintain my purchase and sales book properly.	1	3	1.38	.519
4. I seek assistance from experts for knowledge about VAT.	1	4	2.12	.705
5. I have managed my office accounting system to fit with vat readiness.	1	4	1.79	.566

6. I as businessman read and study about how vat impacts my company.	1	4	1.60	.666
7. I as a businessman initiates to provide vat preparedness training for staff of a company.	1	4	2.05	.547
8. I as businessman initiate dialogues with tax authorities through our business association for formulation of better policies benefitting both business community and government.	1	5	2.55	.748
9. I as businessman prefer the threshold amount for VAT registration should be revised at definite interval of time for its effective implementation.	1	3	1.79	.667
10. I anticipate the rate of VAT should be different as per the nature of business activity.	1	5	3.45	1.23 3
11. I as business person prefer the standard rate of VAT to be maintained for its successful implementation.	1	4	1.90	.608
12. I as a business person cooperate and made an assessment if any difficulties occur on vat system.	1	5	2.12	.678
13. I consider the payment of tax debt as a priority.	1	4	1.97	.871
14. I would stop paying tax if I had the opportunity of not being discovered.	2	5	4.38	.847

Source: SPSS 22.0 calculations based on Field Survey 2020.

The table 4.12 of behavior of business person (SME) towards VAT has been identified. From the above the statement 2, 3, and 6 they are inclined towards the 1 the strongly agree parameter with the statement 14 being the least parameter with mean value 4.38 which close to the disagree parameter for not paying tax even having the opportunity of not being discovered which shows the positive behavior towards VAT administration. Statement 3 represents about the maintaining of purchase and sales book properly for VAT. followed by the statements such as sense of responsibility of VAT to maintain transparent VAT account and a business person they read and study about how vat impacts their company.

Hence, overall, the behavior of business person (SME) seems to be positive towards the VAT payment from the findings above.

d) Opinion Test.

Last two questions were asked regarding the opinion test to see business person (SME) prefer the present 13% VAT rate or not and VAT appropriate for the Nepali traders.

Table 4.13***Preferred VAT rate.***

VAT rate (%)	Frequency	Percent (%)
13	5	3.9
10	123	94.6
10-15	2	1.5
15-20	0	0
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020.

Result: The table 4.13 found that most of the respondents favored 10% to be the VAT rate over 13%. Whereas other VAT rate options were not considered by the respondents. It may be due to easy to calculate and not perceived to be very high.

Table 4.14***Taxpayers perception of Nepali people evading VAT.***

Statement	Frequency	Percent (%)
Less than 10%	79	60.8
10-30%	40	30.8
30-50%	9	6.9
More than 50%	2	1.5
Total	130	100

Source: SPSS 22.0 calculations based on Field Survey 2020.

Result: The table 4.14 it shows the majority of people thinking that less than 10% of Nepali people are evading tax. Which is a positive sign through the tax payer's perspective that they feel most of the people pays their VAT and very few of them may evading.

4.1.3 Findings.

- i All 130 respondents are the business person (SME) from the commercial area of Kathmandu such as Thamel, New Road and Putalisadak.
- ii The data showed that out of 130 respondents 86(66.2%) were male while 44 (33.8%) were female.

- iii The data showed that the majority of the respondents are from the age group of below 35 years contributing 63(48.5%) out of 130 respondents. That was followed by those aged from 35 to 45 years which is contributed to 60 (46.2%) out of 130. That was followed by those aged from 45 to 55 years which is contributed to 6 (4.6%) out of 130. Followed by only 1 (0.8%) who was 55 years and above.
- iv Analysis of 130 respondents showed that the majority of the respondents were bachelor's degree holder who accounted for 71 (54.6%). Then here were 34(26.2%) master's and above degree holders and 25(19.2%) had qualifications of plus two level.
- v The analysis showed that 73 (56.2%) out of 130 had the approximate yearly sales range of below 5 million. Followed by 48(36.9%) out of 130 with the range of 5 to 10 million yearly sales and 9(6.9%) with more than 10 million yearly sales.
- vi Among the 130 respondent's majority of people representing 98(75.4%) were married and remaining 32(24.6) were the unmarried ones.
- vii The analysis regarding the awareness of SME business person showed that with the knowledge of VAT rate mean being 99.2 percent of statement 3 clears that people are much aware about what they pay. Followed by the lowest percentage being 56.2% of statement first about the VAT law came to effect in Nepal, which showed people are not much caring about from when Nepal implemented the VAT system.
- viii The data regarding the perception of vat effects on different commodities showed that VAT being highly influential on the luxury goods (55.4%) followed by necessity goods (20.8%), infrastructure goods (16.9%) and utilities (6.9%) respectively.
- ix The study on knowledge regarding VAT refund showed that out of 130 respondents 98(70.8%) were found aware about VAT. Followed by 34(26.2%) moderately aware and 4(3.1%) were found unaware about the vat administration.
- x The survey on business person (SME) who had taken VAT awareness workshop before showed 52(40%) out of 130 respondents are those who had taken the VAT awareness workshops before. Followed by 51(39.2%)

who had taken some simple consultation and 27(20.8%) are those who had not taken any workshop or even a consultation for VAT awareness.

- xi The survey on business person (SME) who had taken VAT preparedness workshop before showed 59(45.4%) out of 130 respondents are those who had taken some simple consultation regarding VAT preparedness workshop before. Followed by 51(39.2%) who had taken VAT preparedness workshop before and 20(15.4%) are those who had not taken any workshop or even a consultation for VAT preparedness.
- xii The mean value of the respondent's attitude towards stops paying tax if they had the opportunity of not being discovered was 4.43 which came under the strongly disagree parameter which showed that the attitude of taxpayer towards VAT administration was positive.
- xiii The mean value of the respondent's behavior towards maintaining purchase and sales book properly was 1.38 which came under the strongly agree parameter which showed that the behavior of business person (SME) towards VAT administration was positive.
- xiv The analysis of opinion test for the preferred VAT rate found that most of the respondents favored 10% over 13%. Whereas other VAT rate options were not considered by the respondents.
- xv The analysis of perception towards the approximate level of Nepali people evading VAT showed that the majority of people 79(60.8%) out of 130 respondents thinking that just less than 10% Nepali people are may be evading VAT. Which is a positive sign through the mentality of the business person (SME) that they feel most of the people pays their VAT.

4.2 Discussion.

The major objective of the study was to determine the awareness, attitude and behavior of the business person (SME) towards the VAT administration. The study focused on different administration components of the VAT among the SME. Data for these variables were collected through questionnaires sample size of 130.

In the research the respondents were the small, medium enterprise owners of Kathmandu city. Respondents were of different age group, educational level and from

different business backgrounds. Descriptive statistical analysis is very useful for answering the research questions objectives.

The current study has successfully answered the research objectives and research questions. The result generated from SPSS is adequately applied to provide the knowledge about the status of SME taxpayer's administration of VAT.

This research was in line with Gnawali (2018) which indicated that VAT must be successful and this largely depends upon the public awareness, honesty, faith and morality of tax officials and the business community.

This study is also in congruence with Walsh (2012) which showed, a less well-developed area is the potential for behavioral research to contribute to better tax administration. Better understanding of the motives of taxpayers and their attitudes and behavior towards taxation can improve both voluntary compliance and the efficiency of the tax administration.

This study is also in congruence with Seidl and Traub (2002), the paper investigated taxpayers' attitudes, behavior, and perception of fairness with respect to taxation using data drawn from a survey among German employees. It is shown that there is a large gulf between subjects' attitudes towards taxation and their behavior.

This report is in agreement with that of Loo, McKerracher and Hansford (2009), which supported statements of Canada Revenue Authority (2009) as their findings reveal that gaining tax knowledge has a significant impact on Malaysian's compliance level when the self-assessment system had been introduced.

CHAPTER V

SUMMARY AND CONCLUSION

The research was carried out to understand the Small, Medium Enterprises owner's awareness, attitude, behavior towards VAT administration. Additionally, this research perhaps can be helpful to gain insight from the perspective of taxpayers regarding VAT administration and identify the pitfalls in the tax administration and develop the appropriate ways to tap into the making the process better understanding for the business persons.

The previous chapter data analysis been carried out accordingly to assist in finding of the study. This part contains the brief overview of the introduction, review of related methodology, findings of the study which assists in drawing the inferences from the findings that will lead to certain conclusions and generalizations.

5.1 Summary.

This research work entitled, "VAT Administration in Nepal: A Study of Awareness, Attitude and Behavior of business person (SME)", has been carried out to ponder into the theoretical knowledge of VAT and to examine the administration system of VAT especially in the Kathmandu valley, to assess the post-administration period of VAT as compared to the period before the in connection with generating revenue, to examine whether VAT is accepted by the business person compare to Sales Tax. To achieve those objectives descriptive statistical analysis has been done with the help of questionnaire developed by the researcher. It also illustrated previous studies in relation to VAT administration and VAT gap. For this, various books, journal articles, articles in periodicals, conference proceedings, reports, cases, websites and other literary articles were studied and the main limitation of this study was the lack of sufficient literature review regarding this topic in the context of Nepal.

Descriptive research design has been used in this study. The population for this study comprised all SME business persons in Kathmandu Valley and a suitable sample size was chosen on the basis of personal contacts. The source of data was primary in nature. Data was collected through Likert based questionnaire survey and multiple-choice question. Descriptive statistical test was used for the analysis of data in the study. Validity and reliability tests were also carried out.

The identified factors for VAT administration i.e., Awareness, Attitude and behavior of respondents can be used as the measures for getting the insights about the VAT in the perspective of business person (SME) significantly. The study confirmed the underlying fact in the literature by providing that all the identified variables were essential for the VAT insights with respect to the SME business owners.

The study begins with the description of the respondent's profile, the variables considered for the testing of the study their outcomes, Likert scale and multiple choice questions response findings, mean, standard deviation outcomes are ascertained. Their findings and discussion were presented.

The sample survey of 130 SME business person were considered as respondents. About 23 questions were asked them about the various issues relating to administration of VAT in Nepal. The study also discusses the trend of registration, Non-filers. Tax rate, revenue sales per for VAT registration. Their attitude and behavior regarding the VAT payment were tested. After all these studies were made, the study came up with results.

The questionnaire was first started with the information on the respondents' demographic profile. Regarding the demographic profile the study focused on gender, age, educational level, marital status, yearly sales. Out of total 130 respondents in this survey 66.2 % were male and 33.8 % were female. 48.5% were below 35years, 46.2% were 35-45 years, 4.6% were 45-55 years and 0.8 % were above 55 years. Educational level of respondents was 19.2% Plus Two, 54.6% Bachelor level, 26.2% Masters and above. The yearly sales of respondents 56.2% below 5 million, 36.9% 5-10 million, 6.9% above 10 million. Married respondents were 75.4 % and remaining 24.6% were unmarried.

With respect to awareness among the SME business person it shows that minimum of 56.2% respondents were aware about when the VAT law come to effect, with 99.2% aware about rate of VAT being implemented at present context.

There was a significant positive attitude towards VAT administration as the highest mean (1.49) on the statement 'In case of fraud and manipulation cases, Businessperson prefer tax offences and penalties should be high.'

There seems to be a good and positive behavior towards VAT administration as the highest mean (1.38) on the statement where respondents were asked about the businessperson maintaining their purchase and sales book properly for the VAT purposes.

Overall, the study could be concluded that the business persons' response towards VAT is positive. Also being the highest mean being 1.38 closet to the strongly agree (1) defined parameter shows that business person is aware and willing to pay their taxes on time.

5.2 Conclusion.

To identify the level of awareness of SME business person, four sets of study has been carried out i.e., awareness test through multiple choice questions, perception testing regarding VAT effects on different types of commodities, knowledge of SME business owners regarding VAT refund system, and responses of business owners regarding VAT awareness and preparedness.

Business persons were aware about what and how much they paid for value added tax as it was showed from the statement about the VAT rate implemented currently in Nepal and from when vat law came to effect in Nepal. It showed a good level of awareness on business persons regarding VAT. On the perception testing regarding VAT effects on different types of commodities with respect to awareness of VAT among the people, they considered it highly affected the luxury goods more though VAT was levied on all the mentioned goods as per the VAT act of the country. Most of the respondents were found to have good knowledge on the VAT refund system in Nepal. By summarizing all four sets of study it can be concluded that business persons were much aware about the VAT and its practices.

This study found a positive attitude towards value added tax as most of the responses were found inclined to the disagree parameter for the statement of not paying tax if they had an opportunity of not being discovered, followed by the statement which is inclined towards the agree parameter on if they preferred for every import and export trading VAT registration is must irrespective of goods or service nature. From the findings of the research the attitude of business person can be considered positive.

The behavior of business person can also be considered as a positive behavior towards the value added tax from the responses with a mean value that is inclined to the strongly agree parameter on the statement of maintaining proper purchase and sales book for VAT, followed by the mean value inclined to the agree parameter for the statement of having responsibility of maintaining transparent VAT account.

The business person's awareness, attitude and behavior tend to show positive through the result as SME business person at present context are much aware about their responsibilities towards the VAT and the respondents also responded positively to the questionnaire.

5.3 Implications.

Based on the results and findings, this study has the following implications.

5.3.1 Implications for VAT authorities.

On the basis of research, the following are the implications for better administration of VAT system in Nepal.

- i Nonetheless the level of awareness of SME business persons on VAT was good on an overall basis; but the facts where the research found a weak point could not be ignored. The research found out that more than half of business persons were had not taken VAT awareness and preparedness workshop, which is definitely not a good sign for proper VAT administration. Therefore, Ministry of Finance and IRD should coordinate and organize workshops and seminars on VAT preparedness and awareness.
- ii Even though the study found an overall positive attitude of SME business persons towards VAT, the study also cannot ignore minor deficiencies that need to be addressed. The general response towards the statement that the tax officials provided quick and prompt services was at an unsatisfactory level. Hence, the tax authority should work on the problems of their officials and motivate them.
- iii The study found out that the behavior of SME business persons towards VAT was at a satisfactory level but it still had some shortcomings. SME business persons hesitated to communicate with the tax officials. Hence, orientation programs should be conducted to bridge this gap.

5.3.2 Recommendations for future researchers.

On the basis of the findings and conclusions the following implications for future researchers emerge.

- i The research model developed in this study has been shown to offer a good explanation of business persons' Awareness, attitude and behavior towards VAT and its administration in Nepal. Thus, replication of this model to other parts of the world is important so as to be able to generalize the findings in this study.
- ii As indicated earlier, this study is limited to SME business persons in Nepal. Extending this study to other groups of taxpayers to tax professionals would also be interesting.
- iii Researchers can also use the quantitative data in this thesis to examine on the same objective since this study employs only qualitative data to come up with the results or study could be done by using both type of data.

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APPENDICES

A. Questionnaire

Dear valued respondent,

You have been chosen at random as one of a large number of respondents to this study of “VAT Administration in Nepal: A study of Awareness, Attitude and Behavior of SME Tax Payers” as a part of my dissertation for the completion of my Master’s degree in Accounting at the Central Department of Management, Tribhuvan University.

The purpose of this survey is to identify and evaluate the factors that effect on the VAT administration from the perspective of businessmen and taxpayers.

Your participation is voluntary and you do not have to answer all the questions asked if you do not want to but it would be greatly appreciated if you could answer all questions honestly and answer as many as you can so that my research is as complete as possible. Your response will be treated confidentially at all times so you can be entirely open in your responses.

Completing the survey should not take more than 15 minutes at most. The instructions are included in each part of the survey.

Thank you for your cooperation!

Yours sincerely,

Ashish Adhikari,

Central Department of Management,

Tribhuvan University.

Part I: Respondent Profile

Q1. Gender: (1) Male [] (2) Female []

Q2. Age (Years): (1) Below 35 [] (2) 35-45 [] (3) 45-55 [] (4) Above 55 []

Q3. Education Level : (1) Plus Two [] (2) Bachelor [] (3) Master and Above []

Q4. Yearly Sales: (1) Below 5 million [] (2) 5- 10 million [] (3) Above 10 million []

Q5. Marital Status (1) Married [] (2) Unmarried []

Part II: Questionnaire on Awareness of VAT

Please put a tick mark (✓) in the box in an appropriate option for each of the following.

Q6. Do you know that from when VAT law came to effect?

(1) 1997 [] (2) 1998 [] (3) 1999 [] (4) 2000 []

Q7. Do you know the yearly sales turnover (million) for a firm to register for VAT (goods trading) ? (1) 4m [] (2) 5m [] (3) 7m (4) Above 8m

Q8. Which of the following VAT rate being implemented at the present context? (1) 10% [] (2) 13% [] (3) 15% [] (4) 18% []

Q9. What commodities in the society are greatly affected by VAT implementation?

(1) Luxury Goods [] (2) Infrastructure Goods [] (3) Necessity Goods (4) Utilities []

Q10. Who are the true payers of VAT?

(1) Producers [] (2) Wholesalers [] (3) Retailers [] (4) Ultimate customers []

Q11. What kind of tax is VAT?

(1) Direct Tax [] (2) Indirect Tax [] (3) Do not have idea []

Q12. Do you know about VAT refund?

(1) Yes [] (2) Little Bit [] (3) No Idea []

Q13. Do you know the last date to file the vat of a certain month ?

(1) 30th of same month []

(2) End of next month []

(3) 25th of next month []

(4) No idea. []

Q14. Have you taken any vat awareness workshop/seminar/meetings before ?

(1) Yes [] (2) Simple consulting only [] (3) No []

Q15. Have you taken any vat preparedness workshops/seminar/meetings before?

(1) Yes [] (2) Simple consulting only [] (3) No []

Q16. Do you follow vat updates ?

(1) Yes [] (2) No [] (3) Not sure []

Q17. Are you aware of the impacts of vat to your industry?

(1) Yes [] (2) No [] (3) Not sure []

Q18. Do you have Vat-exempt suppliers?

(1) Yes [] (2) No [] (3) Not sure []

Q19. Do you know the verification system of your purchase and sales book for vat?

(1) Yes [] (2) Little Bit [] (3) No Idea []

Part III: Questionnaire on Attitude of VAT among the respondents

Q20. Indicate the level of agreement with the following sentence from 1(Strongly Agree) to 5 (Strongly Disagree):

Statements	1	2	3	4	5
1. I always issue VAT invoice to my customers.					
2. I acknowledge my responsibility towards my tax payment.					
3. I and my customers feel VAT as a regular cost.					
4. My business clients prefer to carry out the business through issuing VAT invoice.					
5. I have the tendency to show the true financial report to tax administration.					
6. I prefer the tax audit to be carried with strict rules and regulations.					
7. I prefer for every import and export trading VAT registration is must irrespective of goods and service nature.					
8. I perceive tax offices provide prompt, quick and reliable service.					
9. In case of fraud and manipulation cases, I prefer tax offences and penalties should be high.					
10. I find it difficult to accept any change of a rule or tax system.					
11. I pay tax dues for the privilege of membership in an organized society.					
12. I would stop paying tax if I had the opportunity of not being discovered.					
13. I think VAT is the appropriate tax system for traders of Nepal.					
14. I think people need to be trained for vat preparedness.					
15. I think vat planning is essence for any business houses.					
16. My current accounting system have the interface that is updated with vat parameters.					

Questionnaire on Behavior of VAT among Taxpayers

Q21. Indicate the level of agreement with the following sentence from 1(Strongly Agree) to 5 (Strongly Disagree):

Statements	1	2	3	4	5
1. I pay my taxes on time to avoid payment of unnecessary fines and penalty.					
2. I have the sense of responsibility and maintain transparent VAT accounts.					
3. I maintain my purchase and sales book properly.					
4. I seek assistance from experts for knowledge about VAT.					
5. I have managed my office accounting system to fit with vat readiness.					
6. I as businessman read and study about how vat impacts my company.					
7. I as a businessman initiates to provide vat preparedness training for staff of a company.					
8. I as businessman initiate dialogues with tax authorities through our business association for formulation of better policies benefitting both business community and government.					
9. I as businessman prefer the threshold amount for VAT registration should be revised at definite interval of time for its effective implementation.					
10. I anticipate the rate of VAT should be different as per the nature of business activity.					
11. I as business person prefer the standard rate of VAT to be maintained for its successful implementation.					
12. I as a taxpayer cooperate and made an assessment if any difficulties occur on vat system.					
13. I consider the payment of tax debt as a priority.					
14. I would stop paying tax if I had the opportunity of not being discovered.					

Q.22. Which of the following option you prefer to be as the appropriate rate for VAT?

- (1)13% [] (2)10% [] (3) (10-15) % [] (4) (15-20) % [] (5) Not more than 20% []

Q. 23. What do you think how many of Nepali people are evading VAT?

- (1) Less than 10% []
 (2) 10-30% []
 (3) 30-50% [] (4) More than 50% []

B. SPSS Output**Gender**

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Female	44	33.8	33.8	33.8
	Male	86	66.2	66.2	100.0
	Total	130	100.0	100.0	

Age

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	35-45	60	46.2	46.2	46.2
	45-55	6	4.6	4.6	50.8
	Above 55	1	.8	.8	51.5
	Below 35	63	48.5	48.5	100.0
	Total	130	100.0	100.0	

Education level

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Bachelor	71	54.6	54.6	54.6
	Masters and Above	34	26.2	26.2	80.8
	Plus Two	25	19.2	19.2	100.0
	Total	130	100.0	100.0	

Yearly sales

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	5-10 Million	48	36.9	36.9	36.9
	above 10 million	9	6.9	6.9	43.8
	Bellow 5 million	73	56.2	56.2	100.0
	Total	130	100.0	100.0	

Marital status

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Married	98	75.4	75.4	75.4
	Unmarried	32	24.6	24.6	100.0
	Total	130	100.0	100.0	

Do you know that from when VAT law came to effect?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 1997	73	56.2	56.2	56.2
1998	47	36.2	36.2	92.3
1999	10	7.7	7.7	100.0
Total	130	100.0	100.0	

Do you know the yearly sales turnover (million) for a firm to register for VAT (goods trading) ?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 4M	5	3.8	3.8	3.8
5M	124	95.4	95.4	99.2
Above 8M	1	.8	.8	100.0
Total	130	100.0	100.0	

Which of the following VAT rate being implemented at the present context?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 10%	1	.8	.8	.8
13%	129	99.2	99.2	100.0
Total	130	100.0	100.0	

What commodities in the society are greatly affected by VAT implementation?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Infrastructure Goods	22	16.9	16.9	16.9
Luxury Goods	72	55.4	55.4	72.3
Necessity Goods	27	20.8	20.8	93.1
Utilities	9	6.9	6.9	100.0
Total	130	100.0	100.0	

Who are the true payers of VAT?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Producers	2	1.5	1.5	1.5
Retailers	2	1.5	1.5	3.1
Ultimate Customers	125	96.2	96.2	99.2
Wholesalers	1	.8	.8	100.0
Total	130	100.0	100.0	

What kind of tax is VAT?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Direct Tax	6	4.6	4.6	4.6
Valid Indirect Tax	116	89.2	89.2	93.8
Valid No Idea	8	6.2	6.2	100.0
Valid Total	130	100.0	100.0	

Do you know about VAT refund?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Little Bit	34	26.2	26.2	26.2
Valid No Idea	4	3.1	3.1	29.2
Valid Yes	92	70.8	70.8	100.0
Valid Total	130	100.0	100.0	

Do you know the last date to file the vat of a certain month ?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 25th of next month	122	93.8	93.8	93.8
Valid End of next month	5	3.8	3.8	97.7
Valid No idea	3	2.3	2.3	100.0
Valid Total	130	100.0	100.0	

Have you taken any vat awareness workshop/seminar/meetings before ?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid No	27	20.8	20.8	20.8
Valid Simple Consulting only	51	39.2	39.2	60.0
Valid Yes	52	40.0	40.0	100.0
Valid Total	130	100.0	100.0	

Have you taken any vat preparedness workshops/seminar/meetings before?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	20	15.4	15.4	15.4
	Simple consulting only	59	45.4	45.4	60.8
	Yes	51	39.2	39.2	100.0
	Total	130	100.0	100.0	

Do you follow vat updates ?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	2	1.5	1.5	1.5
	Not sure	16	12.3	12.3	13.8
	Yes	112	86.2	86.2	100.0
	Total	130	100.0	100.0	

Are you aware of the impacts of vat to your industry?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	3	2.3	2.3	2.3
	Not sure	18	13.8	13.8	16.2
	Yes	109	83.8	83.8	100.0
	Total	130	100.0	100.0	

Do you have Vat-exempt suppliers?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	No	75	57.7	57.7	57.7
	Not Sure	47	36.2	36.2	93.8
	Yes	8	6.2	6.2	100.0
	Total	130	100.0	100.0	

Do you know the verification system of your purchase and sales book for vat?

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Little Bit	29	22.3	22.3	22.3
	No Idea	5	3.8	3.8	26.2
	Yes	96	73.8	73.8	100.0
	Total	130	100.0	100.0	

Which of the following option you prefer to be as the appropriate rate for VAT?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 10-15%	2	1.5	1.5	1.5
Valid 10%	123	94.6	94.6	96.2
Valid 13%	5	3.8	3.8	100.0
Total	130	100.0	100.0	

What do you think how many of Nepali people are evading VAT?

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid 10-30%	79	60.8	60.8	60.8
Valid 30-50%	9	6.9	6.9	67.7
Valid Less than 10%	40	30.8	30.8	98.5
Valid More than 50%	2	1.5	1.5	100.0
Total	130	100.0	100.0	

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
I always issue VAT invoice to my customers.	130	1	5	2.02	.797
I acknowledge my responsibility towards my tax payment.	130	1	4	1.56	.647
I and my customers feel VAT as a regular cost.	130	1	5	1.89	.750
My business clients prefer to carry out the business through issuing VAT invoice.	130	1	5	1.75	.740
I have the tendency to show the true financial report to tax administration.	130	1	5	1.50	.707
I prefer the tax audit to be carried with strict rules and regulations.	130	1	5	1.55	.648
I prefer for every import and export trading VAT registration is must irrespective of goods and service nature.	130	1	4	2.04	.884
I perceive tax offices provide prompt, quick and reliable service.	130	1	5	2.52	1.143
In case of fraud and manipulation cases, I prefer tax offences and penalties should be high.	130	1	3	1.49	.517
I find it difficult to accept any change of a rule or tax system.	130	1	4	1.58	.633
I pay tax dues for the privilege of membership in an organized society.	130	1	4	1.85	.759
I would stop paying tax if I had the opportunity of not being discovered.	130	2	5	4.43	.767
I think VAT is the appropriate tax system for traders of Nepal.	130	1	5	1.73	.691
I think people need to be trained for vat preparedness.	130	1	3	1.72	.584
I think vat planning is essence for any business houses.	130	1	4	1.68	.638
My current accounting system have the interface that is updated with vat parameters.	130	1	5	2.01	.665
Valid N (listwise)	130				

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
I pay my taxes on time to avoid payment of unnecessary fines and penalty.	130	1	5	1.68	.574
I have the sense of responsibility and maintain transparent VAT accounts.	130	1	4	1.49	.600
I maintain my purchase and sales book properly.	130	1	3	1.38	.519
I seek assistance from experts for knowledge about VAT.	130	1	4	2.12	.705
I have managed my office accounting system to fit with vat readiness.	130	1	4	1.79	.566
I as businessman read and study about how vat impacts my company.	130	1	4	1.60	.666
I as a businessman initiates to provide vat preparedness training for staff of a company.	130	1	4	2.05	.547
I as businessman initiate dialogues with tax authorities through our business association for formulation of better policies benefitting both business community and government.	130	1	5	2.55	.748
I as businessman prefer the threshold amount for VAT registration should be revised at definite interval of time for its effective implementation.	130	1	3	1.79	.667
I anticipate the rate of VAT should be different as per the nature of business activity.	130	1	5	3.45	1.233
I as business person prefer the standard rate of VAT to be maintained for its successful implementation.	130	1	4	1.90	.608
I as a taxpayer cooperate and made an assessment if any difficulties occur on vat system.	130	1	5	2.12	.678
I consider the payment of tax debt as a priority.	130	1	4	1.97	.871
I would stop paying tax if I had the opportunity of not being discovered.	130	2	5	4.38	.847
Valid N (listwise)	130				

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Attitude of VAT among the respondents	130	1.31	3.81	1.9572	.35201
Behavior of VAT among Taxpayers	130	1.36	3.07	2.1621	.31805
Valid N (listwise)	130				

Attitude of VAT among the respondents

Case Processing Summary

		N	%
Cases	Valid	130	100.0
	Excluded ^a	0	.0
	Total	130	100.0

a. Listwise deletion based on all variables in the procedure.

Reliability Statistics

Cronbach's Alpha	N of Items
.803	16

Behavior of VAT among Taxpayers**Case Processing Summary**

		N	%
Cases	Valid	130	100.0
	Excluded ^a	0	.0
	Total	130	100.0

a. Listwise deletion based on all variables in the procedure.

Reliability Statistics

Cronbach's Alpha	N of Items
.836	14

Scale: ALL VARIABLES**Case Processing Summary**

		N	%
Cases	Valid	130	100.0
	Excluded ^a	0	.0
	Total	130	100.0

a. Listwise deletion based on all variables in the procedure.

Reliability Statistics

Cronbach's Alpha	N of Items
.798	2