

A Study On
INCOME TAX ADMINISTRATION IN NEPAL

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RECOMMENDATION

This is to certify that the thesis

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INCOME TAX ADMINISTRATION IN NEPAL

has been prepared as approved by the Department in the prescribed format of office of the Dean, Faculty of Management, Tribhuvan, this thesis is forward for examination.

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VIVA-VOCE SHEET

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and found the thesis to be the original work of the student and written according to prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirements of Master's Degree in Business Studies (M.B.S.)

Research Committee

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DECLARATION

I, hereby, declare that my research work reported in this thesis entitled “*A Study on Income Tax Administration in Nepal*” has been submitted to New Horizon College, Faculty of Management, Tribhuvan University is my original work done in the form of partial fulfillment of the requirement for the Master’s Degree in Business Study (M.B.S.) under the supervision of Mr. Lalit Man Shrestha of New Horizon College.

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Madhav Nepal

Researcher

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ABBREVIATION

DDG	Deputy Director General
DG	Director General
F/Y	Fiscal Year
GDP	Gross Domestic Product
GON	Government of Nepal
Govt	Government
HR	Human Resource
ICAN	Institute of Chartered Accountants of Nepal
INGOs	Institutional of Non Government Organizational
IRD	Inland Revenue Department
IRO	Inland Revenue Office
ITA	Income Tax Act
LTO	Large Taxpayer Office
MIS	Management Information System
NGOs	Non-Government Organization
NRB	Nepal Rastra Bank
S.N.	Serial Number
TP	Tax Payer
TR	Total Revenue
VAT	Value Added Tax

CHAPTER I

INTRODUCTION

1.1 Background of the Study

Tax is an important factor in economic planning and development of a nation. It is a compulsory levy imposed on the payer by a legal authority or recipient public authority. 'Income Tax' mean 'Income Estimate,' which helps the government to know the actual economic strength of a person. It is also a way to set up an economic standard for general people. It helps the Government to know the distribution of money among country's people.

Income Tax is a direct tax in that the burden and incidence are on the same person who pays the tax. It is imposed on income and plays a vital role in the economic growth & stability of our country. Income tax is levied on net income of individuals and corporations. Income tax is annual tax levied and collected by the Central Government on an individual's or corporation's net profit. Income tax was first introduced in England in 1799. The history of tax in Nepal is not very long. The idea of introducing income tax in Nepal started in late fifties. Income tax was first introduced in 2016 B.S. by first elected government which was levied only on business profits and remuneration income.

Income Tax Act in Nepal was first introduced only in the year 2019 B.S. In 2031 B.S. another income tax was introduced. In 2058 B.S. the modern and scientific tax system was brought to avoid various defects of Income Tax Act, 2031. The Parliament of Nepal enacted Income Tax Act, 2058, which is still in force. According to this Act income means a person's income from any employment, business or investment and the total of that income as calculated in accordance with this act.

Income Tax is administered by the tax administration. This administration was set up as the Tax Directorate in 1959, Inland Revenue Department in 1961/62 and Department of taxation in 1963/64. In order to collect tax revenue tax offices were created under this department. Inland Revenue Department is responsible for the implementation and administration of Act. The Ministry of Finance is at the apex body of tax administration. Government of Nepal is the highest authority of the tax administration. Income Tax Act, 2058 has empowered the Government of Nepal as regards to the implementation of the tax laws.

Income Tax plays a leading role for the economic development of a country. It is one of the internal sources which fulfill the financial needs. It is assumed as a best weapon to achieve social justice, balanced regional development and distributive motive. Income tax is the main source of financing economic expenditure in most developing economics. It is the vital sources of government revenue.

Income Taxes are used in most countries around the world. They vary greatly. Comparison of tax rates around the world is difficult. Income tax is computed and paid as prescribed in the law and is levied on the income of individuals or businesses (corporations or other legal entities).

An efficient resource mobilization is indispensable for the economic development of a country. With an effective tax administration system, developed economies are able to significantly generate revenues needed for meeting their governmental expenditures. However, in developing economies like Nepal, poor tax administration system has marred the much-needed resource mobilization for infrastructural development and creation of public goods. In fact, Nepal has one of the lowest taxes to GDP ratios in South Asia. And this is a testimony to its inefficient tax policy.

The country is enmeshed in a slow-paced economic growth rate. The growth rate has hovered around 3 to 4 percent for the past several years. In order to achieve the targeted economic growth rate, Nepal needs to prioritize its infrastructural development and enhance the existing foundations of basic amenities like health, education and drinking water, among others. Being one of the least developed countries in the world, Nepal significantly relies on foreign aid and loans for meeting its expenditures. This reliance must be gradually phased out by improving its trade balance and reforming its tax policy. Although resource mobilization has increased over the years, this improvement needs to be further enhanced via improved tax administration system.

In a nutshell, Nepal needs an efficient and fairer tax policy. The country's main sources of tax revenue are income tax, VAT, customs and excise duties. While the contribution of customs duties and import-related revenues is approximately 50 percent of the total tax revenues, the contribution of direct tax revenues is just 20 percent of the total tax revenues. While some tax regulations are good for the economy, others may not be that fitting when considered in the long run. For example, the Government of Nepal gives incentives to investors to start businesses/industries in under-developed and remote areas of Nepal. For this, the government provides tax rebates ranging from 25 to 50 percent of the applicable tax. This initiation is good as it tends to promote economic development of under-developed regions of the country by providing local employment and utilizing locally available raw materials and resources. Similarly, the government provides an exemption of excise duty to industries producing products using locally available raw materials, chemicals and other resources. This initiation promotes the use of locally available resources and limits the import of raw materials from other countries. And more importantly, the government reimburses any customs and excise duties on raw materials used during product manufacture on the basis of export quantities. All these initiatives are great as they tend to promote export-oriented

industries in a country that has been subdued by huge trade deficits with other countries.

Tax administrations in many low-income countries are weak, corrupt, and nontransparent. This inefficiency reflects both the mix of taxes and the faulty design in their structure and in their operational systems. The tax administration is also affected by policies relating to the salary, the attitude, and the reward and punishment system of personnel. The tax administration in low-income countries is driven by detailed revenue targets and not by the tax laws and accounting records.

A well-designed set of tax policies cannot be implemented properly by a weak administration. The Nepalese tax administration fails to deliver professional services. It has been able to implement the tax laws and regulations properly, resulting in a huge gap between what the legal provisions say and their actual implementation. Although there has been considerable reform in the tax policies in recent years, dissatisfaction with the tax system has been increasing rather than decreasing. Knowing the limitations of the tax administration, many taxpayers try to take full advantage of the situation. The government must not continue relying on foreign aid and loans for meeting its developmental expenditures. This reliance is not a sustainable solution for the economic advancement of a country.

1.2 Statement of the Problem

The Nepalese economy is basically an agro based developing economy. The agriculture sector occupies one third space in countries GDP and provides employment opportunities to two third of its populate. Despite this fact, agricultural production could not be increased as expected. In each year, imports exceed exports. The balance of payment is not favorable. Every year, Nepal has been preparing deficit budget. The economic growth rate of the country, a major indicator of economic development has not been encouraging.

Various challenges are emerging in the economy. The gap between expenditure and revenue called resource gap is increasing each year. So it has been a serious obstruction in the process of economic development of developing countries like Nepal. Therefore to decrease the sources gap, it is necessary to raise government revenue. It is possible only after raising the sources of revenue.

Tax revenue is the most important source of government revenue among the various revenues. Income tax as one of the internal sources has minimized the dependency on foreign loans and aids. Internal source has no obligation towards the third party and less risky as compared to external funds. Due to rapid increase in government expenditure as compare to revenue, the developing countries like Nepal are facing a serious problem of inconsistency between resource mobilization and expenditure policies of their government. They need adequate financial resources to meet the expenditure of the country. It is well known fact that there are numerous problems inherent in the Nepalese Income Tax System. With the present economy, a lot of problem originated from the assessment, collection and management of income tax. Income tax is a source of revenue to the government and, therefore, must be saved from the setbacks.

Since we are not in an ideal world, the problems associated with income tax may not be removed completely but can be reduced to a manageable extent. It is intension of this work, therefore, to find some of the hindrances which strongly influencing against the tax system and to find possible remedies. Income taxation enjoys widespread support because income is considered a good indicator of an individual's ability to pay. However, income taxes are hard to administer because measuring income is often difficult. For example, some people receive part of their income "in-kind"—in the form of goods and services rather than in cash. Farmers provide field hands with food, and corporations may give employees access to company cars and free parking

spaces. If governments tax cash income but not in-kind compensation, then people can avoid taxation by taking a higher proportion of their income as in-kind compensation.

People avoid to pay taxes. They feel trouble and they become dishonest to show their all sources of income. Tax avoidance and evasion are on the increase. Income tax evasion is a serious problem in Nepal. The contribution of income tax is very low because of its low contribution of income and wealth. The officials responsible for tax collection administration are just ignorant of the importance of their task. Tax administration has not been able to convince taxpayers as to why they need to pay tax. The means and methods of working in tax offices of Nepal are very conventional. Poor taxpaying habit of Nepalese people and poor recording system of tax office are also the problem of economic development of Nepal. Considering the importance of income tax in national economy and the role of tax office in administering such tax, the following research questions have been raised for the study;

- a. What section of the total revenue of the government is collected through income tax?
- b. Under income tax, what types of taxes and from whom the taxes are collected?
- c. How the income tax is administered by the tax offices and the Inland Revenue Department?
- d. How the performance in income tax administration could be improvised?

1.3 Objective of the Study

The main objective of the study is to analyze the Income Tax administration in Nepal. The other objectives of the study are as follows:

- a. To analyze the contribution of income tax to total revenue.
- b. To examine the composition of income tax.
- c. To analyze the income tax administration in Nepal.

- d. To judge the opinions of taxpayers and others for the enhancement of income tax administration.

1.4 Significance of the Study

More and more financial resources are needed to meet the increasing expenditure for growing development activities. The government requires sufficient funds to fulfill current expenses, developmental works and repayment of loans. There are various sources to meet such needs but emphasis has been given to the fulfillment of financial needs from internal sources specially income tax because income tax is the easy, permanent and effective instrument to increase revenue. The study is significant for various stakeholders as the study gives idea and make familiar with income tax act prevailing in Nepal. Moreover, the contribution of income tax to government revenue can be known from this study. The study is also useful for all interested persons about administration, composition and legal provision of income tax in Nepal. And finally, this study makes other researcher easy to conduct further research on income tax in Nepal.

1.5 Limitation of the Study

Every study has suffered from the limitation. This study is not an exception. The following are the limitation of the study.

- a. This study is concentrated only on the Income Tax Administration in Nepal.
- b. The study is limited up to the availability of data and sufficient literature.
- c. This study has been conducted on the basis of data of 10 fiscal years. (Fiscal year 2002/03 to fiscal year 2011/12).
- d. The reliability of the primary data depends absolutely on the opinions of the selected respondents, and the validity of the secondary data depends on the annual reports published by Inland Revenue Department.

- e. The interpretation presented on primary data analysis is inductive in nature as completely deductive reasoning is somewhat not ease.

1.6 Organization of the Study

This study has been organized into five chapters.

Chapter-I: Introduction

It deals with introduction. This includes general background, statement of the problem, objectives of the study, significance and limitation of the study.

Chapter -II: Conceptual Framework and Review of Literature

It deals with the review of available relevant studies. It includes conceptual/theoretical review of the related studies book, journals and the published and unpublished research work as well as thesis.

Chapter- III: Research Methodology

It explains the methodology used in the study which includes research design, population and sample, sources of data, data collection technique and limitations of the methodology.

Chapter- IV: Presentation and Analysis of Data

It deals with the presentation and analysis of all the relevant collected data. Similarly this chapter also includes the major findings of the study and this is the heart of the study.

Chapter-V: Summary, Conclusion and Recommendation

This chapter deals the summary of the study, the main findings, conclusion, recommendation and suggestion on the basis of the study.

Bibliography and appendix are included at the end.

CHAPTER II

REVIEW OF LITERATURE

In this section of the study, the concept of tax, tax administration, types of tax and tax related subjects are reviewed. Besides these, the past journals and articles, and thesis are also reviewed.

2.1 Conceptual Framework

2.1.1 Tax

Tax is compulsory contribution from people to government to undertake work of public good. Many tax experts have given the definition of tax in their own words. They have focused the different aspect of tax according to their own view.

A tax may be defined as a "Pecuniary burden laid upon individuals or property owners to support the government a payment exacted by legislative authority." A tax "is not a voluntary payment or donation, but an enforced contribution, exacted pursuant to legislative authority" and is "any contribution imposed by government whether under the name of toll, tribute, tillage, gable, impost, duty, custom, excise, subsidy, aid, supply, or other name."

According to Prof. Seligman "Tax is compulsory contribution from a person to the government to destroy the expenses incurred in the common interest of all without reference to special benefit conferred".

2.1.2 Tax and Efficiency

A tax except in the form of a lump sum levy reduces the consumer's welfare in two ways: directly through a transfer of resources from him to the government and indirectly through a rise in the consumer prices of taxed commodities relative to those of non-taxed ones. The farmer produces an income effect

while the latter gives rise to both an income effect and a substitution effect in the standard manner following a relative price change (Bartelsman and Beetsma; 2003: 228).

The efficiency loss of a tax refers to the excess of the reduction in the consumer's welfare above and beyond that which can be accounted for by income loss due to payment of the tax. For this reason, the efficiency loss is usually referred to as the excess burden of the tax.

2.1.3 Tax and Equity

Equity is one of the main issues in taxation. Equity means distribution of income, wealth and or other variables of interest equally. A possible way to give concreteness to the meaning of equity is to interpret it only in the context of redistribution. Equity issues in taxation are generally examined under the two complementary rubrics of horizontal equity and vertical equity (Auerbach and Reishus; 1988: 141). The former calls for the equal tax treatment of equal individuals, while the latter calls for the unequal tax treatment of unequal individuals.

2.1.4 Types of Tax

Tax may be of various types. The rate and nature of tax may be different as economists have classified the tax from different angles. They have given a very long list of the types of tax. But on the basis of impact and incidence the tax may be classified into two types.

- Direct tax
- Indirect tax

A direct tax is really paid by the person on whom it is legally imposed. Direct taxes are levied on the income and property. The direct taxes have been used to bridge the gap of income and wealth inequality in the society. An indirect tax is imposed on one person but paid partly or wholly by another. Indirect taxes are

generally imposed on consumption of goods and services. The taxes on such goods and services are integrated with their price. Selling those goods and services on higher price, the taxpayers easily transfer the burden on general consumers (Kandel; 2003: 88).

2.1.5 Income Tax

Income tax is a direct tax that is imposed on the earning of individual and corporation. Actually, tax levied on the taxable income is known as the income tax. It is charged by the government on the income of the previous year at the rate prescribed each year by the finance act. From very earlier, income tax has always been regarded as a tax based on the canon of ability. The tax could be adjusted as to exempt the lowest income groups from operation of tax and make the richer groups bear the burden of tax according to their income. Tax economists have a view that an income tax is a levy imposed upon the income of an individual after the exemption limit (Desai and Dharmapala; 2006: 159). All incomes about the tax exemption level are subjected to income tax that is based on the income tax act of the concerned country.

2.1.6 Administration

Certain established practices and techniques in society are recognized as constituting the field of administration. Those administrative practices and managerial techniques enable the various organizations of a society, its governments and business enterprises, its social clubs and labor unions to fulfill their responsibilities and to execute their programs. The majority of authors agree that administration plays an important role in society. But while they agree on the importance of administration, they assign to the subject different degrees of significance.

Henry Fayol believes that the administrative process is universal, that its existence is percentage wise the most element in particularly all vocations and professions. So, there is widespread need for the scientific study of

administration. While Paul Pigars feels that the main purpose of administration is to preserve the status quo in society. Brooks Adam regards administration as a more important, indeed as the most important human facility because its function is to facilitate social change and to cushion the stock of social revolution. James Burnham contends that the administrators or managers of society have appropriated so much power that the decisive revolution has already arrived, neither fascistic nor communistic revolution but managerial. Charles E. Marrion regards administration as the evolution of another human technology leading to man's adaption to his complex environment. Charles A. Beard believes that administration is the key science of contemporary civilization.

2.1.7 Tax Administration

Tax administration is regarded as a tool for including some responsibilities for determining the policies and the programs of government related to tax. Especially it is the planning, organizing, directing, coordinating and controlling of government organization related to taxation. The shape of tax system in practice is determined to a great extent by the way it is administered (Li and Weber; 2009: 662).

The main objectives of tax administration should be the efficient assessment, collection and enforcement of taxes legally due, without undue cost and harassment to the government or taxpayer in terms of money, time inconvenience and mental worry. More specifically the objectives of tax administration may be stated as follows:

1. To assess and collect taxes in order to meet the revenue requirements of the country.
2. To facilitate and encourage voluntary compliance by taxpayers.
3. To detect and conduct tax evasion and avoidance.
4. To maintain public confidence in the fairness and integrity of the system.
5. To administer tax legislation fairly, uniformly, impartially with firmness.

6. To keep high the morale and motivation of tax officials.
7. To work efficiently in order to make the tax system effective.

2.1.8 Significance of Tax Administration

Tax evasion and tax avoidance, whether at the national or international level, violate the principle of fiscal equity and undermine the concept of voluntary tax compliance, that is, the timely filing and reporting of required tax information, correct self-assessment of taxes due and their timely payment without resource enforcement action (Yetman; 2008: 302).

Tax evasion is normally considered to occur when non compliance is the result of a willful and conscious failure to notify the taxing authorities of taxable assets or income activities giving rise to taxable income, a deliberate failure to pay taxes legally owed or use of fraud to conceal the existence of taxable income and or obtain allowances or the repayment of taxes. Tax avoidance on the other hand, a less precise concept, is generally in such a way as to take advantage of weaknesses or ambiguities in the tax law to reduce the tax payable below. What it could otherwise be, without actually breaking the law (Ghimire 2005: 39).

Tax avoidance techniques, although legal that is, in conformity with the letter of the law- nevertheless achieve the reduction or elimination of tax liability in circumstances where it is the underlying intention of the law, that tax should be charged. Although tax avoidance may be regarded as immoral, the techniques employed are legal and tax conduct involved is not fraudulent. It has shown that there are multiple motives for both compliance and non-compliance with the tax laws. With regard to compliance; it gives the meaning of self-motivate to pay tax. Taxpayers who obey may be motivated by a sense of civic responsibility or social justice or by a fear of sanctions that some cases by fear of the less of social acceptance if their delinquency should ever become public knowledge.

With regard to non-compliance, a number of reasons for failure to abide by the tax laws are as follows:

- High tax rates.
- Lack of trained staff to examine or audit accounts.
- Weakness in the tax laws and administration.
- Lack of coordination between tax departments and other government departments.
- Weakness in the tax laws and administration.
- Lack of coordination between tax departments and other governments departments, such as custom.
- Absence of international conventions on income tax for exchange of information (Beard; 1994: 236).

Tax evasion and avoidance are two forms of non-compliance. Significantly reduce the amount of collected taxes that is the amount of compulsory unrequited payments to government that enable to perform the tasks constitutionally and legally entrust to them and increase their dependence on non tax resources.

Tax evasion and avoidance also increase the desire for taxpayer to ignore the tax laws or seek artificial ways around them. In order to offset the revenue losses this occurs, government may have to levy new taxes: increase tax rates and eliminate exemptions, there by imposing an unfair burden on honest taxpayers. The impact of this is perceived to be high taxes, which are not return with services or other identifiable benefits (Ivkovich, Poterba and Weisbenner; 2005: 1608). They are accompanied by criticism of the size and inefficiency of government.

In the circumstances described above, the ability of tax administrations to enforce compliance and thus minimizes the disparity between taxable capacity and tax effort levels becomes a matter of honest priority.

The challenge facing by many developing countries is thus to overhaul their tax administrators so as to enhance their overall performance. A tax administration of high quality can help not only to meet or achieve revenue requirements but can also constitute a means of achieving greater financial self-reliance, since external financial assistance, even when forthcoming can be no more than an adjunct to domestic financial resources (Wolfe; 2006: 611). Moreover, any existing or new foreign borrowing will have to be serviced within the limits of two degrees, the ability of developing countries to attain sustainable administration with great integrity capable of collecting revenue as specified in the tax legislation and at the same time of providing tax payers with better service.

A tax administration that operates with maximum efficiency and effectiveness helps to mobilize more revenue, thereby enabling governments to achieve greater financial reliance and facilitating the pursuit of growth-oriented structural adjustment programs, the provision of requisite infrastructure for economic and social development and the creation of a more hospitable environment for private foreign investment.

In addition to forecasting a more attractive environment for foreign investment, a smoothly functioning tax administration yields other benefits including the following:

- It enhances the ability of government to efficiently enforce tax with potentially high revenue yields (such as income tax and excess profit tax) which requires precise and sophisticated applications.
- It obviates the need to broaden the tax base, i.e. to levy new taxes and or raise tax rates and may make it possible to eliminate or reduce burdensome taxes, grant more tax exemptions and enlarge income tax brackets without reducing tax revenue, and

- It may take it possible to successfully tax the agricultural sector, which in many countries remains largely untaxed despite its inherent potential as a significant source of revenue (Scholes & Wolfson; 1992: 186).

In a broader context, an efficient and effective tax administration will help developing countries to take advantages of economic recovery elsewhere in the world by including their determination to undertake necessary reforms. Thus, bolstering their ability to attract a greater share of foreign direct investment, bring back home resources lost to capital flight and come to grips with their external debt servicing burden through negotiations with their creditors. It might even help these countries to qualify for more official development assistance for the financing of needed infrastructure (Ghimire, 2005: 66).

2.1.9 Tax Administration and Fiscal Policy

Tax administration interacts with fiscal policy in various ways:

For example:

- Higher taxes on certain activities or sectors, although an administratively convenient way of increasing revenue or reducing a deficit, may in fact act as a distinctive to production and efficient revenue utilization; these taxes also have a contractive effect on consumption, since they reduce the tax payer's purchasing power.
- If it is considered politically unacceptable to increase taxes as a means of reducing budget deficits, the tax administration may be called upon to help achieve this goal by operating more efficiently and effectively. If successful, this approach reduces the budget's contribution to growth in the money supply and this help to curb inflation and decrease dependence on non-bank financing.
- A budget- balancing determination would make the government more conscious of its spending behavior and give the tax administration an additional incentive to combat tax evasion and avoidance and

- A larger budgeted deficit resulting from weaknesses in tax administration may lead to a larger public debt and higher interest and tax rates as well as to lower capital accumulation and employment growth rate. Financing large deficits through money creation fuels inflation and discourages private investment. Higher tax rates and or new taxes may then become the only viable means of generating the domestic savings needed for capital-formulation projects (Graham and Tucker; 2006: 568).

2.1.10 Tax Administration and Tax Policy

With regard to tax policy, experience has shown that even in countries where tax policy reforms have been implemented their economic impacts has often been compromised by poor tax administration and revenue yields have not been up to the mark. Efficient and effective tax administration gives the makers of tax policy a wider range of options and is in fact, the key to effective tax policy, for no policy can be constructive or even feasible unless properly implemented by the tax administration.

2.1.11 Tax Administration and Tax Structure

The effectiveness and efficiency of the tax administration also affects the tax structure. The tax structure can be modified, but unless the tax administration is capable of enforcing both new and existing taxes, the modifications may have no significant impact on tax collection. The importance of tax administration performance in relation to the tax structure has described by the Director of the Fiscal Affairs Department of the IMF (2006) in the following terms:

In arriving at the desirable tax structure that they will recommend, fund missions take into account:

- The government's priorities.
- The country's macro-economic situation.
- The strength and honesty of the country's tax administration.
- The existing statutory taxes structure.

- The structure of the economy, and
- A variety of other factors such as constitutional or legal limitations, prevailing customs and attitudes, the incidence of the existing tax system and so forth.

The factors mentioned above construction the number of feasible options and to some extent, influence the final tax structure. The weakness of tax administration may rule out all but the simplest options the maximum that ‘old taxes are good taxes’ would argue against a major overhaul of the tax system. There is only so much change that a tax administration can absorb at any one time.

2.1.12 Essential Functions of the Tax Administration

The tax laws impose on taxpayers certain obligations with which they are required to comply. Generally speaking, they must be registered on the tax rules, file returns, provide full and accurate information and pay the taxes due on time. A tax administration ‘carries out the ordered of tax policy’ its basic mission is to ensure compliance with the tax laws and regulations as they stand or are interpreted by the courts. It must help taxpayers to fulfill their tax obligations and when necessary induce or compel them to do so.

In order to execute its basic mission, a tax administration performs certain fundamental functions tax payer registration and identification, assessment, collection and audit. These functions have been classified as ‘essential’ whereas personnel management planning and control and taxpayer information and assistance have been described as ‘auxiliary’ or ‘support’ functions. The essential functions have also been labeled ‘operational’, since they involve the actual collection of taxes and entail close relations with taxpayers while the ‘auxiliary’ or ‘support’ functions have been designated as ‘normative’ meaning that they involve in interpretation and application the preparation and issuance of guides and standards and the establishment of working methods and procedures.

In the performance of its essential functions, a tax administration usually faces serious constraints and difficulties in developing countries, where many taxpayers, unlike taxpayer in industrialized countries, are not enmeshed in a set of interlocking recorded transactions. In industrialized countries, a major part of the tax base is linked to the activities and assets of large organizations, whereas, in developing countries, the potential base would normally be linked to the activities and assets of self- employed business persons, farmer and professionals, who constitute the 'hand-to- tax'. Consequently for reasons of administrative convenience and feasibility, developing countries tend to rely on a handful of easy to administer indirect taxes such as export duties, import duties and excise duties, other taxes on imported goods (Barber and Odean; 2004: 425).

In fact, in many developing countries the tax laws can to a large extent be enforced fully only in the formal sector for frequently only corporations have the capacity to maintain proper accounts. First, developing countries often have a large informal sector, consisting of black markets, capital flight and so on , which are virtually beyond the reach of level of illiteracy not only creates ignorance of the tax laws and regulating but provides an excuse for it . The alleged inability of tax payers to furnish the documentation needed for a realistic assessment prevents the income, net worth, gift and land-whose incidence is generally assumed to rest with those who pay them offer greater incentives and more opportunities for tax dodging. In addition, incomes, imports, sales, real estate and like may have objective or true values completely different from those on the basis of which the relevant taxes are calculated. This is not necessarily due to a deliberate intent to evade or avoid taxes, but any is the result of poor record-keeping and accounting standards, other things being equal, the lower the compliance cost, and the better tax administrations performance. Optimum compliance is the result of improved tax payer registration and identification assessment, collection and audit.

Until recently, Nepal collected all its major taxes, including customs duties, excise/countervailing duties, sales tax, and advance income tax at either the point of import or at the manufacturing stage. These taxes used to generate the bulk of the tax revenue. Since all the major taxes were collected at either the point of import or manufacturing, there was a tendency among the importer either to smuggle in order to evade tax or to declare lower values for their imports in order to reduce their tax liability. There was also a tendency for the manufacturers to create an artificial sales depot, sell it at the lower price, pay a low tax, inflate the selling price of the artificial sales depot, and then reap large profits. Dealers, wholesalers, and retailers were not required to register for any types of commodity taxes. While they were supposed to register for income tax, most of the traders had not been maintaining proper accounts for the purpose of this tax either. In response to this, a very nontransparent bureaucratic process was set up to administer all major taxes.

Until recently, in theory, at least, import duties were levied on the invoice price or the price in the customs valuation book, whichever was higher. In practice, importer were to submit invoices indicating prices equivalent to values mention in the valuation book, irrespective of their real values, meaning that the import duties were levied on or around prices mentioned in the valuation book. This required the presentation of some false documents. It is believed that administrative smuggling is rampant. To ensure the smooth processing of import shipments, there are more or less standard fees. Traders say that physical inspections and clearance delays can be kept to a minimum if customs inspectors are given facilitation fees. The local tax administration is inefficient as well. The octroi was levied on goods brought into a given local area for commercial, professional, or industrial use in commercial quantities. Vehicles are stopped at several points for the purpose of collecting the octroi. This created not only inconvenience for the importers and passengers, but wasted time and energy and increased the costs of production and trade.

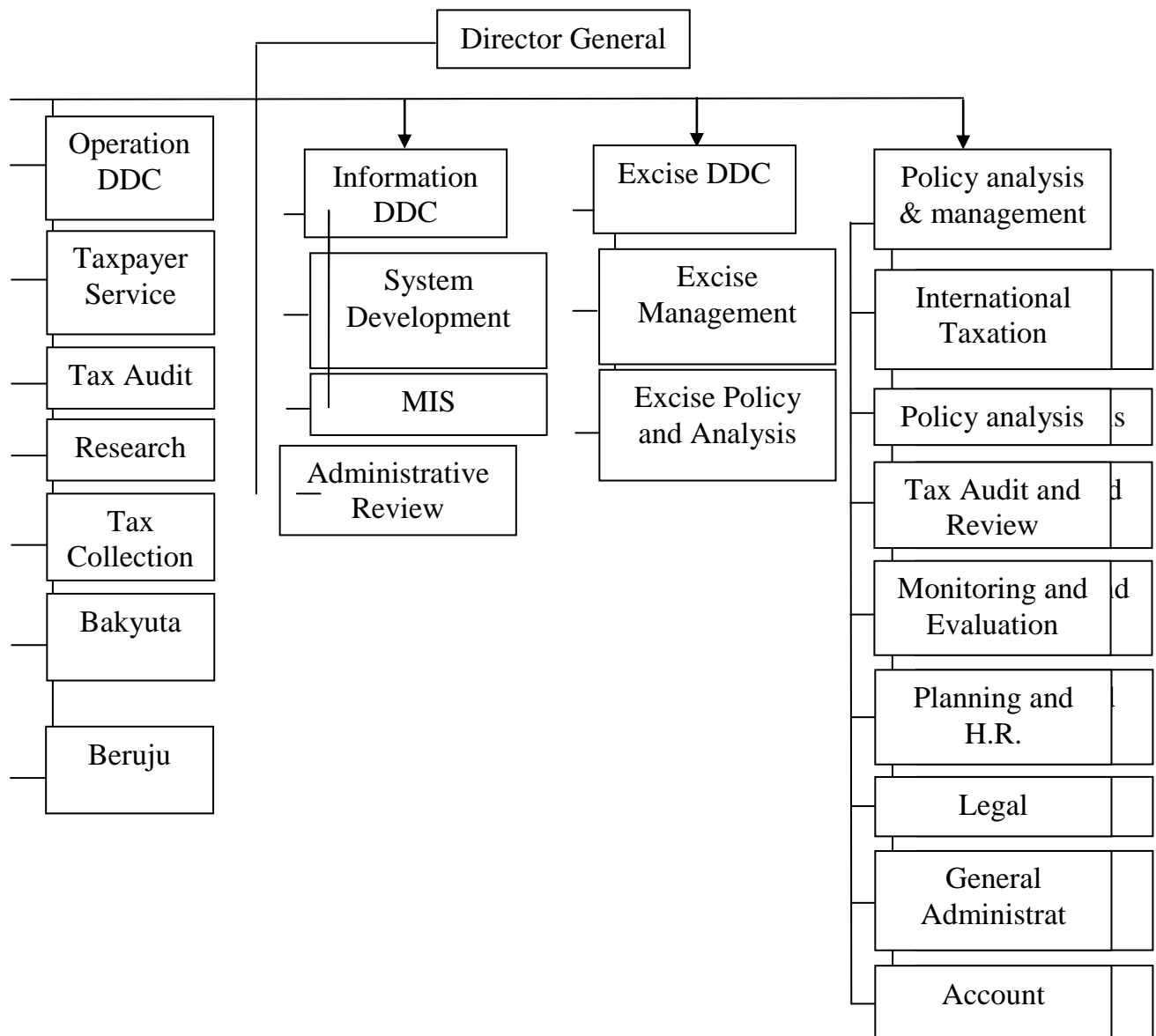
This tax system and these procedures actively and strongly discourage the development of an account-based transparent system in Nepal. Inconsistency and lack of transparency in the tax procedures have had various implications for revenue, fairness, and efficiency of resource allocation. They have also undermined confidence in and respect for the government's fiscal apparatus. The bargaining system, together with an inadequate legal framework related to taxpayers' rights and personnel compensation, and the lack of an effective appeal system, have caused considerable uncertainty and imposed unnecessary and unforeseen costs on taxpayers.

2.1.12.1 Development of Income Tax Administration

Income tax is administered by the tax administration. This administration was set up as the Tax Directorate in 1959, Internal Revenue Department in 1961/62 and department of taxation in 1963/64. The number of tax offices increased gradually. These offices were classified as Zonal Office and Branch Offices over the years. Before the merger of the income tax and VAT administration in mid – April in 2001, the total number of tax offices was 40. Of them, the number of tax offices, area offices and unit offices was 32, 7 and 2, respectively. These offices were situated in major urban areas. The government through gazette notification had specified their geographical area of working. One office covered more than one district.

The Department of Taxation and the Department of Value Added Tax were merged into one organization in the mid –April 2001, while field offices under these two departments were merged in the middle of July 2001. The merged Department was called the Inland Revenue Department and field offices are known as Inland Revenue Offices. There are twenty two Inland Revenue Office and one, Big Taxpayers Offices all over the country. Organizational Structure of Inland revenue Department is structured on a functional line.

Figure 2.1
Organizational Structure of Inland Revenue Department



2.1.12.2 Personnel System

Inland Revenue department is headed by the Director – General (gazette level second class officer) who is assisted by Deputy Director Generals, who are also assisted by 18 Director (gazette level second class offices), 42 Section officer (gazette level third class officer). Thus the total strength of personnel on the Inland Revenue Department is 154. Details may be seen from the following chart.

Table 2.1**Position Created in the Inland Revenue Department**

S.N	Position	Grade	No of Staff
1	DG	GI	1
2	DDG	GI	4
3	Director	GII	18
4	Deputy Attorney	GII	1
5	Director (information)	GII	1
6	Deputy Attorney	GII	1
7	Chemist	GIII	1
8	Computer Officer	GIII	2
9	Computer engineer	GIII	2
10	Information officer	GIII	6
11	Section Officer	GIII	32
12	District Attorney	GIII	1
13	Account Officer	GIII	4
14	District Attorney	GIII	1
15	Nayab Subba	NG-I	22
16	Computer operator	NG-I	15
17	Accountant	NG-I	5
18	Sub – computer Operator	NG-I	5
19	Driver		10
20	Peon		19
21	Sweeper		3

Sources; Annual Report of IRD 2011/12

Of the 22 field offices, 4 are headed by Chief Tax Administrator (Gazette Level Class I) and the rest are headed by Chief Tax Officer (Gazette Level class II). The total strength cadres on the Inland Revenue Offices and the number of window offices under each office under each officer may be seen from the following table.

Table 2.2**Position Created in the Inland Revenue Offices**

S.N	Position	Grade	Total No. of position
1	IRO,Kathmandu No. 1	A++	72
2	IRO, Kathmandu No. 2	A++	68
3	IRO,Kathmandu No. 3	A+	69
4	Big Taxpayers office	A++	58
5	IRO, Biratnagar	A	44
6	IRO, Simara	A	38
7	IRO, Lalitpur	A+	46
8	IRO, Birgunj	C	48
9	IRO, Bharatpur	A+	45
10	IRO, Bhairahawa	A+	41
11	IRO, Pokhara	A++	42
12	IRO, Nepalginj	A++	41
13	IRO, Bhadrapur	A+	28
14	IRO, Dharan	A++	36
15	IRO, Lahan	C	25
16	IRO, Janakpur	D	31
17	IRO, Heatuda	A	26
18	IRO, Krishnagar	A++	16
19	IRO, Dang	A++	18
20	IRO, Dhangadhi	A++	22
21	IRO, Mahendranagar	A+	17
22	IRO, Bhaktapur	C	18
	Total		849

Source: Annual Report of Department of Inland Revenue 2011/12

2.1.13 Taxpayer Registration and Identification

A tax administration needs to take all feasible steps to ensure that all natural and legal persons liable to taxation are registered. However, given the limited resources of many tax administrations, efforts to register new taxpayers have to concentrate on areas which seem likely to yield significant revenue. Upon

registration, each taxpayer is immediately been issued an identification number to ensure that documents and records in master files can easily be traced to a specific taxpayer (Allingham and Sandmo; 1972: 326). Once, issued the identification number has not be duplicated, reissued or cancelled in the event of the tax payers death or cessation of operation.

2.1.14 Assessment

For assessment, it has been followed where feasible and appropriate, what is called the conventional approach to assessment, which emphasis voluntary compliance through self assessment- backed by random but rigorous auditing and stringent penalties and the provision to taxpayers of outreach services, including technical advice on tax assessment obligations (Cloyd, Limberg and Robinson; 1997: 263). In that connection, taxpayers have been authorized to file and play in ways that minimize compliance cost. On the other hand when prevailing condition make it necessary to rely primarily on administrative or official- assessment of all returns, the tax administration has to carry out economic or statistical studies where finding helps tax official to make ‘best judgment assessment’, when the information supplied by tax payers is deemed to be incomplete or inaccurate.

2.1.15 Collection

In the developing countries-as well as in industrialized countries-the tax collation function is guided by the need to maximize revenue. Collection at source and other current payment arrangements for direct taxes (personal income tax, taxes based on accounts and records) has been strengthened and even extended. To that end, the tax administration is to be designed and implemented a monitoring system comparable to the credit control system used in private business. In developing countries, where must tax payer either do not keep reliable records on making not reveal them the scarcity of administrative resource makes it highly desirable to use withholding as extensively as possible: third parties engaged in transaction with potential and actual tax payers is required to withhold appropriate amounts from payments (Goolsbee;

2000: 274). The amounts thus withheld by third parties on behalf of the tax administration is transmitted to official on accounts as promptly as possible and credited against the tax liabilities of the appropriate taxpayers. A person is to be imposed if the taxpayer underestimates by more than a given Percentage (e.g. 25 of 30 percent) his or her liability, as opposed to the actual assessment made by the tax administration or if the tax payer fails to pays a tax installment within specified time period.

2.1.16 Audit

Auditing is accurately focused and carried out with a high degree of supervision in order to ensure its effectiveness and integrity. Auditing is to be based on appropriate selection criteria; over- extensive auditing is impractical since any additional revenue raised is offset by increased administrative costs. A good information system, using computers where feasible and appropriate is to be facilitated rapid detection of non- filers, stop filers. Taxpayers must be categorized according to type of tax, type of business, geographical location and potential contribution to revenue (IMF; Annual Report of 2009).

2.1.17 Tax Administration Transformation Process

The tax administration transformation process has its major components: its tasks, its people, the formal organizational arrangements and the informal organizational arrangements. The real challenge of tax administration design is to select from the range of alternatives the most appropriate way to configure the tax administration components to create the output required by the strategy. In order to do this, it is essential to understand each tax administration component and its relationship to the others. The following sections discuss these tax administration components.

2.1.17.1 The Formal Organizational Arrangements

According to Wyman, the formal organization is made up of the structures, systems and processes. Each organization creates to group people and the work they do and to co-ordinate their activity in ways designed to achieve strategic

objectives. It is proposed that an important aspect of formal organizational arrangement is the strategic planning system. A strategic plan is essential for a tax administration. With a well-conceived strategic plan, tax managers will be more forward thinking in their approach in an era of uncertainty (Hall and Jorgenson; 1967: 396). A strategic plan is an important document to guide any tax department on the way forward. Adequate planning will help management to find the best way of achieving a particular objective.

2.1.17.2 The Informal Organizational Arrangements

Organizational culture has been defined as a complex set of values, beliefs, assumptions and symbols that define the way in which an organization conducts its business. Flamholtz suggested that an organization's culture is the set of values, beliefs and social norms which tend to be shared by its members and, in turn, tend to influence their thoughts and actions. The relationship between organizational culture and organizational performance has had sporadic but growing interest from a range of disciplines. In fact, general connections between an organization's culture and its performance have been made since the early stages of management and organization theory. One of the major reasons for the widespread popularity and interest in organizational culture stems from the argument that certain organizational cultures lead to superior organizational performance.

2.1.17.3 Tasks

Task is the defining activity of any organization; that is, the basic and inherent tasks to be performed by the organization and its parts. The performance of this task is one of the primary reasons for the organization's existence and any analysis from a design perspective has to start with an understanding of the nature of tasks to be performed, anticipated work flow patterns, and an assessment of the more complex characteristics of the work. Gill listed the main tasks of a tax administration that require analysis when assessing if a tax administration needs to be reformed. The tasks consist of organization, management and operational tasks.

Table 2.3

Main Tasks of Revenue Administration Requiring Analysis

Organization and management tasks	Operational tasks
Strategy and policy formulation	Registration of taxpayers
Planning, budgeting, resource allocation	Taxpayer services: <ul style="list-style-type: none"> • Taxpayer education • Taxpayer assistance • Facilitation of voluntary compliance
Monitoring and evaluation	Processing of declarations and payments
Co-ordination	Monitoring of tax withholders and collecting agents
Financial management	Collection of information about taxable transactions <ul style="list-style-type: none"> • Collection of information from third parties • Intelligence operations • Search and seizure and survey operations to obtain incriminating evidence
Personnel management	Risk analysis and selection of cases for audit and investigation
Information Technology management	Audit and investigation
Asset Management	Recovery of tax arrears
Internal Control	Legal and judicial matters: <ul style="list-style-type: none"> • Legislation • Appeals • Prosecution
Anti-corruption	Code of ethics, disciplinary rules, vigilance and co-operation with external anti-corruption agencies
External Relations	Effective interaction with important environmental factors to promote the tax administration objectives, meet external challenges and exploit emerging opportunities offered by the environment

(Source: Gill; 2004: 741)

Concerning the issue of tax administration tasks, Silvani and Baer suggested that, in order for a tax administration to be efficient, the general strategy of the tax authority should have an integrated approach to the tax collection process as a guiding principle, where each element in the tax collection process is essential to the tax administration

strategy. Silvani and Baer also stated that to achieve a significant improvement in the overall performance of a tax administration, each element in the tax collection process needs to be improved. They elaborated that tax collection process involves: (1) taxpayer registration; (2) tax returns and payments processing; (3) computer operations; (4) detection of stop filers and collection of arrears; (5) delinquent taxpayers; (6) audit; (7) the sanctions and penalty system; (8) taxpayer services and publicity; (9) management and organisation; and (10) personnel.

2.1.17.4 People

Basically, a revenue collection system is an interactive structure of people, equipment, methods and controls, designed to create information flows and records that support the repetitive work routines of the revenue collection departments. It is important to identify the salient characteristics of the people responsible for the range of tasks involved in the core work of an organization. These characteristics include the knowledge and skills they bring to their work; their needs and preferences, in terms of the personal and financial rewards they expect to flow from their work; their perceptions and expectations about their relationship with the organization; their demographics and how these factors relate to their work. The people who perform the core tasks are indeed an important element in tax administration. In the context of a tax administration, if the tax employees' attitude towards the tax administration is positive, it could have favorable effects on taxpayer satisfaction and the overall tax authority performance.

2.1.18 Tax Authority of Nepal

The Inland Revenue Department (IRD) is currently responsible for the enforcement of Tax Laws and administration of the following taxes: Income Tax, Value Added Tax, Excise Duty, Vehicle Tax and certain fee and duties like Entertainment fee (Film Development Fee), Special fee, etc. Likewise, the Department is also responsible for monitoring the non-tax revenue such as dividends, royalties etc. of the Government.

IRD carries out the following functions:

- a. Tax Administration (Income Tax and VAT)
- b. Tax Policy

- c. Tax Payer Services
- d. Registration, Revenue Collection
- e. Tax audit
- f. Tax Enforcement and investigation
- g. Review & Appeal
- h. Tax Refund
- i. Advance Ruling
- j. Tax Treaty and International Taxation
- k. Excises and Liquor Administration
- l. Monitoring of non-tax

IRD is centrally located in Kathmandu. There are 36 field offices throughout Nepal including 1 Large Taxpayers Office, 22 Inland Revenue Offices and 13 Taxpayer Service Offices. The previous Department of Taxation was established in 1960. IRD and its district offices are totally running on functional line. Major functions include Taxpayer's Service, Audit and Collection.

2.1.18.1 Taxpayers Rights and Assurances

In addition to the specific rights and assurances provided in the concerned Acts, taxpayers in general are assured of the following rights. These assurances will be strictly adhered to. The Taxpayers rights, among others, include: Each taxpayer is treated with due respect and honor.

- a. Each taxpayer will get an immediate receipt of return submission whilst a receipt of other correspondences is to be provided in ONE hour.
- b. Each taxpayer willing to seek an advance ruling may apply either in the Department or through concerned Inland Revenue Office. There is a legal provision that a decision should be made within 45 days after the request is made.
- c. Each taxpayer can represent or make any correspondence by an authorized person including legal assistants and the accounts specialist or auditors just in case if he/she is unable to represent or make any correspondence.

- d. Each taxpayer is to get copies of the documents related with him/her or submitted to the IRO or documents or decisions affecting her/him generally in TWENTY FOUR hours of his/her request in the concerned IRO.
- e. Each taxpayer is to get refund of his excess input tax (VAT) and other taxes. The exporter will get refund generally within 15 days in IROs and 30 days in IRD upon receiving application for refund.
- f. Each taxpayer is to get certificate/renewal of Excise/Liquor business generally within TWENTY FOUR hour after the request is made.
- g. Each taxpayer is to get sales and purchase books certified by the Tax Officer generally within TWENTY FOUR hours after the request is made.
- h. Each taxpayer is to get initials of the Tax Officer on stock transfer or sales to the non-registrants generally within TWENTY FOUR hours after the request is made.
- i. Each taxpayer is to get Permanent Accounts Number (PAN) or the Certificate generally within 3 days after the request is made, and
- j. Each taxpayer is to get Tax Clearance Certificate generally within TWENTY FOUR hours after the request is made.

2.2 Review of Previous Study

2.2.1 Journal and Articles

Dahal (2011) in his article, *“Taxation in Nepal: Structure, Issues and Reforms”*, stated that in developing economies, resource gap is critical and widening resulting to huge fiscal and budgetary deficits. The growing resource gap is frequently of by mobilizing internal and external borrowings and consequently shifting the burden of debt to posterity. Therefore, revenue mobilization is challenging proposition in an economy like Nepal where a majority of the people live in abject poverty and the people engaged in economic activities have extremely limited taxable capacity. In addition, legal base of taxation is compressed with unlimited tax shelters and tax administration lacks innovative mechanism to identify new taxpayers and bring

them into tax net. In Nepal's tax structure revenues are buoyant but inadequate to supplement development activities. Interestingly, there was no adverse impact of conflict on internal revenues and, subsequently, the tax system suffers from structural constraints with tremendous administrative and procedural complexities envisaged in the existing Income Tax Act, which lacks simplicity and transparency. The major problems of taxation in Nepal include: (1) marginally high tax rates (2) limited tax base (3) low tax elasticity (4) poor voluntary compliance (5) leakages in tax collection (6) rigid Income Tax Act, 20(K) (7) inefficient, indifferent and corrupt tax administration, and (8) no consolidated record of property (land and building) with the Internal Revenue Department. The tax system in Nepal calls for periodic reforms to ensure growth, equity and stability. The studies and reports on taxation exhibit that several reforms have had been undertaken by the government in the past to simplify and modernize the tax system. These reforms were confined to improving tax structure by designing appropriate policy instruments. The reforms in taxation in Nepal consist of three types: (1) reforms in tax laws and regulations (2) reforms in environment, and (3) reforms in tax administration.

Timilsina (2012), in her article, "*Tax Elasticity and Buoyancy in Nepal: A Revisit*", stated that a time series analysis of tax elasticity and buoyancy reveals an inelastic tax structure in Nepal. Taxes are not responsive to changes in income with most elasticity coefficients reporting below unity. The tax system is not progressive adequately also in the case of proxy bases. A progressive tax system needs to have at least greater than unitary value of the coefficient of elasticity. And a higher degree of progressivity in the tax structure would result in elasticity greater than 2. The low built-in flexibility (elasticity) observed in Nepalese tax system is explained through a variety of factors such as exemptions, tax incentives, duty waivers, low compliance and the large sectors of the economy which are not subject to taxation. Therefore, the automatic response of tax to income is low. The targeted average revenue growth mentioned in the Second Interim Plan could be achieved only with the rigorous

efforts of the fiscal authorities to improve the overall tax system as well as revenue administration.

Article I.

Article II. Gurung (2012), in his article, *“Tax Administration Fails to be Assertive”*, stated that over the past few years, the success of the tax administration has been measured in terms of revenue collection figures which will have an adverse impact in Nepal’s economic sector, according to experts. The tax administration has failed to intervene in a meaningful manner after the completion of the multi-billion Value Added Tax (VAT) fraud committed by certain businesses by producing fake invoices, adding that the Inland Revenue Department (IRD) has been more focused on its target despite the provision of self-compliance in the country’s tax regime.

Article III.

The existing policy has envisaged the role of the tax administration as a facilitator in revenue mobilization rather than as a collector. However, the tax administration has merely been playing the role of a collector. He said that the tax administration has failed to intervene in areas of revenue leakages significantly. Private business firms have started evading their tax liabilities using highly intelligent approaches. But the revenue administration has failed to empower its officials in a competent manner. Moreover, the virtual account system of businesses is another problem which the tax administration has failed to bring under its scanner. The trend of keeping account details in a foreign country has thrived in the country. The revenue administration has failed to control it.

Article IV. Khadka (2013), in his article, *“Present Tax Administration: A Case for Reforms”*, stated that an efficient resource mobilization is indispensable for the economic development of a country. With an effective tax administration system, developed economies are able to

significantly generate revenues needed for meeting their governmental expenditures. However, in developing economies like Nepal, poor tax administration system has marred the much-needed resource mobilization for infrastructural development and creation of public goods. In fact, Nepal has one of the lowest taxes to GDP ratios in South Asia. And this is a testimony to its inefficient tax policy.

Article V.

The country is enmeshed in a slow-paced economic growth rate. The growth rate has hovered around 3 to 4 percent for the past several years. In order to achieve the targeted economic growth rate, Nepal needs to prioritize its infrastructural development and enhance the existing foundations of basic amenities like health, education and drinking water, among others.

In a nutshell, Nepal needs an efficient and fairer tax policy. The country's main sources of tax revenue are income tax, VAT, customs and excise duties. While the contribution of customs duties and import-related revenues is approximately is much high. This mode of revenue generation is not a sustainable one. This is mainly because Nepalese import has surged up with an increased consumption over the years, and the growth in consumerism has been fuelled primarily by increased remittances. But with growing financial instabilities in developed economies, there will be a crunch in remittance inflows to Nepal. Moreover, with increased trade liberalization, import-based revenues tend to decline. While some tax regulations are good for the economy, others may not be that fitting when considered in the long run. For example, the Government of Nepal gives incentives to investors to start businesses/industries in under-developed and remote areas of Nepal. The government must not continue relying on foreign aid and loans for meeting its developmental expenditures. This reliance is not a sustainable solution for the economic advancement of a country.

2.2.2 Review of Thesis

Lama (2009), in his study, "*A Study on Effectiveness of Implementation Aspect of Tax Planning in Nepal*" has the main objective to make on Tax planning regarding its effective implementation. The specific objectives of the study are to study the concept of tax planning, to examine the use of tax planning in Nepalese organization, to examine the implementation of Tax planning and to provide suggestion to Nepalese organization to use tax planning.

The study finds that the provision of best judgment assessment should be put to use in its true spirit. In addition to other financial and non-financial assistance, including incentives, other assistance need to be provided by government and financial institution for the revival of sick industrial units.

Pradhan (2010), in his study, "*Tax Administration and Income Tax System in Nepal*", has the main objective to analyze the effectiveness of income tax administration and system of Nepal. The specific objectives of the study are to examine the administrative aspects and system of income tax in Nepal, to examine the tax system in Nepal, to identify major problems related to tax administration in Nepal and to provide appropriate suggestions and recommendations.

The study finds that the Nepalese total revenue is composed of both Tax revenue and Non-tax revenue. The average contribution of Tax revenue and Non-tax revenue was 79.64% and 20.36% respectively. Moreover, there is a dominant role of indirect tax revenue in Nepalese tax structure. The average contribution of direct tax and indirect tax to total tax revenue was 26% and 74% respectively. Although the total amount of both taxes is increasing, there is not satisfactory growth in collection of both taxes. Also, the average contribution of custom duties, value added tax and excise duty on indirect tax revenue were 38%, 46% and 16% respectively.

Shrestha (2011), in her study, "*A Comparative Study on Contribution of Direct*

and Indirect Tax to National Revenue of Nepal”, has the main objective to analyze the contribution of direct tax and indirect tax to national revenue of Nepal. The specific objectives of the study are to find the contribution of direct tax and indirect tax to national revenue in Nepal, to analyze the structure of direct and indirect tax, to analyze the contribution of corporate tax to national revenue of Nepal, and to find out the most important factors for effectiveness of income tax in Nepal.

The study finds that the contribution of tax revenue was 86.86% and that of non tax was 13.14% in FY 2009/10. It shows that tax is major source of government revenue. Also, the contribution of direct tax and indirect tax to total tax revenue was 26.71% and 73.29% respectively in 2009/10. It reveals that tax structure of Nepal is not a justifiable on equity ground and progressiveness because indirect tax is considered regressive in nature. The contribution of custom duty, excise duty, VAT on indirect tax were 43.73%, 13.14%, 43.13% respectively in FY 2000/01 and contribution each taxes were reached 30.83%, 21.22% and 47.90% respectively in FY 2009/10. It shows that custom duty was in decreased trend and excise duty and vat were in increasing trend. Finally, the contribution of income tax, house and land registration tax revenue and vehicle tax in FY 2000/01 were 89.71%, 6.03%, 4.26% respectively which reached to 81.01%, 13.20%, 5.79% respectively in FY 2009/10.

Agrawal (2012), in her study, *“Attitude of Businessmen Toward Income Tax Act 2058”*, has the main objective to judge the opinion of the Taxpayers regarding the Act. The specific objectives of the study are to analyze the impact and effectiveness of income tax on revenue generation of Nepal and to give appropriate suggestion to improve the tax system so that the government can collect more revenue and use it in the economic development of the country.

The study finds that the collection of Income Tax has faced various problems like tax evasion, poor tax administration, unsound income tax policy, lack of

consciousness of people and etc. Moreover, the success and effectiveness of income system entirely depends upon provision of income tax system, sound and effective tax administration, trained employees as well as positive response and willingness of taxpayer to implement the provisions. Also, the Income tax act 2058 is modern and effective than the previous income tax Act but some of the problems still exist. The act is insufficient in rebates and facilities provisions; increasing corruption, ineffective service to the taxpayer by tax administration and etc.

2.3 Research Gap

After reviewing the various books, dissertations reports, articles and research, simply in tax administration topics found that income tax is administered directly by the Inland Revenue Department. It is responsible for the implementation and administration of the Act. Government of Nepal is the highest authority of the tax administration. Most of literatures are concentrated on administrative, legal and assessment procedure of income tax. Since, all of them have identified the main problem in this sector as poor performance of tax administration. Although very few studies was concerned on focusing tax administration covering all sources of taxes in separate way. Thus, this study mainly concentrates on covering all aspects of tax and focusing particularly income tax in more specific way.

CHAPTER III

RESEARCH METHODOLOGY

Research methodology sets the sketch of the study. It defines what activity is to be done, how it would be done, and what data will be followed. A researcher can get data from both primary and secondary sources. The secondary sources are the ones that have been already available or published, for instance the annual reports, brochures, magazines, journals and others. However, the primary sources demand the collection of the data by the researcher himself. A questionnaire can be a good source of primary data.

3.1 Research Design

Research design is a plan structure and strategy of investigation conceived so as to obtain answer to research questions and to control variances. The study aims to portray on the income tax administration of Nepal. The research design followed for this study is basically a historical, empirical and descriptive-cum-analytical.

3.2 Sources of Data

This study is conducted on the basis of both the secondary data and primary data relating to income tax administration. The secondary data have been extracted mainly through the annual reports Inland Revenue Department and Economic Surveys. Besides these, the annual report of Nepal Rastra Bank has also been equally reviewed. Similarly, various data and information are collected from the periodicals, economic journals, managerial magazine and other published and unpublished reports and documents from various sources. For the primary data collection, a set of questionnaire has been prepared and requested to the taxpayers, tax experts; auditors, and tax employees to provide their best answers.

3.3 Sample Size

This research study has included the sample size of 75 respondents representing 25 taxpayers, 25 auditors and 25 tax employees.

3.4 Data Collection Procedure

Various numerical data and information were collected as per objectives of the study and research questions. Firstly, law, rules, regulation and policies related to income tax were studied. Secondly, different libraries such as Chamber of Commerce and NRB were also visited. Thirdly, numerical were collected from different year budget speeches, economic surveys, annual reports of IRD, publications of TU. Lastly various journals and national newspapers were also studied.

3.5 Data Presentation and Analysis Procedure

The collected data were classified and tabulated for the presentation of data various tables and diagrams were presented for data analysis and presentation. Correlation and hypothesis testes were also applied.

CHAPTER IV

DATA PRESENTATION AND ANALYSIS

4.1 Secondary Data Analysis

This section of the study analyzes the data obtained from the Inland Revenue Department that are related to the income tax collection and its administration.

4.1.1 Structure of Government Revenue

The government collects its revenues from various sources. These sources can be broadly classified in two main sections, first the tax revenue and second the non-tax revenue.

Table 4.1
Structure of Government Revenue (Rs. in Crore)

Fiscal Year	Unit	Custom	Excise Duty	Vehicle Tax	VAT	Income Tax	Property Tax	Others	Tax Revenue	Non-Tax Revenue	Total Revenue
2002/03	Rs.	1278.32	377.12	42.96	1345.97	967.64	60.07	16.58	4089.60	1364.29	5453.89
	% of TR	23.44	6.91	0.79	24.68	17.74	1.10	0.32	74.99	25.01	100
2003/04	Rs.	1555.48	622.67	70.06	1447.89	924.59	169.75	26.86	4817.30	1415.80	6233.1
	% of TR	24.96	9.99	1.12	23.23	14.83	2.72	0.43	77.29	22.71	100
2004/05	Rs.	1570.16	644.59	80.65	1888.54	1015.94	179.92	30.67	5410.47	1601.80	7012.27
	% of TR	22.39	9.19	1.15	26.93	14.49	2.57	0.44	77.16	22.84	100
2005/06	Rs.	1534.40	650.76	84.76	2161.07	1037.37	218.11	56.57	5743.04	1485.15	7228.19
	% of TR	21.23	9.00	1.17	29.90	14.35	3.02	0.78	79.45	20.55	100
2006/07	Rs.	1670.76	934.32	99.50	2609.56	1503.40	225.35	69.78	7112.67	1658.54	8771.21
	% of TR	19.05	10.65	1.13	29.75	17.14	2.57	0.80	81.09	18.91	100
2007/08	Rs.	2106.24	1118.96	106.92	2981.57	1731.12	294.07	176.66	8515.56	2246.70	10762.25
	% of TR	19.57	10.40	0.99	27.70	16.09	2.73	1.64	79.12	20.88	100
2008/09	Rs.	2679.29	1622.09	185.00	3970.09	2514.24	522.33	212.15	11705.19	2642.26	14347.45
	% of	18.67	11.31	1.29	27.67	17.52	3.64	1.48	81.58	18.42	100

	TR										
2009/10	Rs.	3515.08	2430.61	241.79	5492.09	3128.56	551.11	270.25	15629.49	2365.09	17994.58
	% of TR	19.53	13.51	1.34	30.52	17.39	3.06	1.50	86.86	13.14	100
2010/11	Rs.	3571.16	2654.29	302.26	6166.36	3886.85	357.25	339.59	17277.76	2704.11	19981.87
	% of TR	17.87	13.28	1.51	30.86	19.45	1.79	1.70	86.47	13.53	100
2011/12	Rs.	4354.92	2935.36	288.72	7218.10	5245.15	312.78	95.95	20451.28	3609.05	24060.33
	% of TR	18.10	12.20	1.20	30.00	21.80	1.30	0.40	85.00	15.00	100

(Source: Economic Survey 2011/12 & Annual Reports 2011/12, IRD)

Note: TR here means Total Revenue

If compared with the non-tax revenue of the government, the tax revenue has greater preponderance in total revenue. In most of the observed periods, the tax revenue reflected more than four-fifth of the total revenue while in the remaining periods as well, the tax revenue is at least three-fourth of the total revenue. Hence, the tax revenue is categorically the main source of revenue for the government. The tax revenue to total revenue has ranged from 74.99% in the fiscal year 2002/03 to 86.86% in the fiscal year 2009/10, while in amount the tax revenue has increased from Rs. 4089.60 crore in the fiscal year 2002/03 to Rs. 20451.28 crore in the fiscal year 2011/12. In contrast, the collection of revenue from non-tax source has ranged from Rs. 1364.29 crore in the fiscal year 2002/03 to Rs. 3609.05 crore in the fiscal year 2011/12. Though the weight of non-tax revenue on total revenue is comparatively small, the role of non-tax revenue should not be minimized.

If the contribution of each component of tax-revenue on total revenue is analyzed, it can be said that VAT is the most important component. However, in the fiscal year 2002/03, the custom duty has been the most contributing source of tax-revenue. In fact, the custom duty is the second most reliable revenue of tax-revenue. Although the income tax has remained the third reliable source from the tax-revenue to contribute to total revenue in most of the cases, it has proved to be the second contributing source from the fiscal year 2011/12 onward. Likewise, the excise duty, property tax, vehicle tax and

other taxable source are equally important in that order. Proportionally, the ratio of VAT to total revenue has ranged from 23.23% to 30.86%, custom duty to total revenue has ranged from 17.87% to 24.96%, income tax to total revenue has ranged from 14.35% to 21.80%, excise duty to total revenue has ranged from 6.91% to 13.51%, property tax to total revenue has ranged from 1.10% to 3.64%, vehicle tax to total revenue has ranged from 0.79% to 1.51%, and other tax to total revenue has ranged from 0.32% to 1.64% in the observed decade. Finally it can be said that although VAT is the major source from tax-revenue to total revenue, the other components of tax-revenue along with the income tax, which is emerging as the second most import tax-revenue source, and the other non-taxable sources are equally important to accentuate the government revenue.

4.1.2 Composition of Income Tax

Structure of income tax consist income from business, investment and employment. This section analyzes the composition of collected income tax.

Table 4.2
Composition of Income Tax (Rs. in Crore)

Fiscal Year	Public Enterprises	Corporate	Individual	Remuneration	Interest & Others	Total
2002/03	292.80	192.43	336.22	59.73	86.40	967.64
2003/04	205.66	153.13	353.34	139.12	73.34	924.59
2004/05	133.24	246.78	392.63	167.59	75.70	1015.94
2005/06	19.57	340.43	423.47	176.41	77.49	1037.37
2006/07	101.97	571.71	523.44	200.79	105.49	1503.40
2007/08	20.46	718.65	638.12	245.10	108.79	1731.12
2008/09	95.91	942.51	987.75	319.56	168.51	2514.24
2009/10	113.18	1223.44	1103.99	441.31	246.64	3128.56
2010/11	128.18	1396.55	1362.74	586.33	413.05	3886.85
2011/12	223.97	1964.35	1644.31	853.29	559.23	5245.15

(Source: Economic Survey 2011/12 & Annual Reports 2011/12, IRD)

The contribution of the corporate body in income tax has been observed to be highest in all the examined years. Thus, it can be said that the corporate bodies are the highest tax paying bodies from the perspective of income tax. Next to

this body, the individual firms, which are small scaled firms but tremendous in numbers, are the largest income tax paying entities. After that, the remuneration tax, which is the tax paid by the professional and employees from various sectors, are the important income tax source. In later periods, the interest earned tax by the individual or other entities has become greater contributing income tax source than the public enterprises.

Quantitatively, the income tax paid by the corporate bodies, which is in increasing trend in most of the years, has ranged from Rs. 153.13 crore in the fiscal year 2003/04 to 1964.35 crore in the fiscal year 2011/12, the income tax paid by the individual firms has gradually increased from Rs. 336.22 crore in the fiscal year 2002/03 to Rs. 1644.31 crore in the fiscal year 2011/12, and the tax levied on remuneration has also persistently increased and thus is raised to Rs. 853.29 crore in the fiscal year 2011/12 from Rs. 59.73 crore in the fiscal year 2002/03. Similarly, the interest and other tax has ranged from Rs. 73.34 crore in the fiscal year 2003/04 to Rs. 559.23 crore in the fiscal year 2011/12 and the tax paid by the public enterprises has ranged from Rs. 19.57 crore in the fiscal year 2005/06 to Rs. 223.97 crore in the fiscal year 2011/12. Analyzing the data, it can eventually be said that the tax levied on the corporate bodies is the major component of the income tax.

4.1.3 Administration of Income Tax

Collecting the income tax is one of the challenge for IRD, and on the other facet, the administration of income tax is equally challenging. The IRD adopts various strategies to administer the income tax effective.

4.1.3.1 Registration in Income Tax

For the operation of the business, an entity needs to be registered in Income Tax, otherwise such the property of such unregistered could be seized by the tax administration whenever it desires and the entity may also liable to punishment in the form of fines and penalties and others, depending upon the nature of business. The number of registration in Income Tax Office during the ten fiscal years have been tabulated and interpreted in this section.

Table 4.3
Registration in Income Tax

FY	No.	%
2002/03	22454	6.06
2003/04	24149	6.51
2004/05	27188	7.33
2005/06	25441	6.86
2006/07	28325	7.64
2007/08	33422	9.01
2008/09	31325	8.45
2009/10	46156	12.45
2010/11	55122	14.86
2011/12	77239	20.83
Total	370821	100

(Source: Annual Reports of IRD)

In most of the fiscal years, except in the fiscal year 2005/06 and 2008/09, it has been observed that the number of entities registering in income tax is in increasing trend this shows that the administration of Income Tax by IRD is quite praiseworthy. However, it is dubious to say that whether the performance of such department is optimal, as infinite entities in suburban, remote and even small numbers in urban areas are running their business without registering and these entities are escaping from Income Tax Act. Nevertheless, it can be expected that these would be forced to register, if the IRD took strict steps. Quantitatively, the number of registrants in Income Tax in each year has been increased from 11618 to 77239 in the observed decade. In such decade, a total

of 370821 entities, which is 68.52% of total 541180 registrants, registered in Income Tax. The performance of IRD in this decade, from the sense of high preponderance of registrants, is thus progressive. The growth of registrants is highest, 20.83%, in the fiscal year 2011/12 and is lowest, -8.45%, in the fiscal year 2008/09.

4.1.3.2 Registration in Income Tax till the FY 2068/69

Under this section of the study, the registration made by different entities; individual, private limited, public corporation and others, in single fiscal year, 2068/69, are numerated and analyzed.

Table 4.4
Registration in Income Tax till the FY 2068/69

Detail	No.	%
Individual	414487	76.59
Private Limited	69686	12.88
Public Corporation	833	0.15
Other Corporation	28388	5.25
Cooperative	12074	2.23
Partnership	10455	1.93
Others	5257	0.97
Total	541180	100

(Source: Annual Reports of IRD)

Up to the fiscal year 2068/89, 541180 entities have been registered in income tax. However, the proportion of each type of income tax registrants on total registrant has differed. It is the individual entity who has preponderance on such registration. The firm that has been run by the individual numbers 414487, representing 76.59% of the total registrants. After that the Private Limited Company is on front, which is 69686 in number, representing 12.88%. In addition, the public corporation represented 0.15% and other corporation represented 5.25%. Similarly, there are 12074 registered cooperatives, 10455

partnership firms, and 5257 other firms. Although the transactions of the individual's firms is apparently small, and resulting the profit earned and ultimately the taxable income to be small, the contribution of their cumulative income in nation building could not be minimized.

4.1.3.3 Assessment Against Non-filer in Income Tax

Despite the initiation of the tax offices, still some individuals do their business without registering in Income Tax, and in each year, the income tax office targets to assess such activities. To examine whether the targeted numbers of assessment against non-filer in income tax has been achieved, the targeted and achieved assessment are compared and analyzed.

Table 4.5
Assessment Against Non-filer in Income Tax

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	258	233	----	90.31
2003/04	262	251	7.73	95.80
2004/05	281	304	21.12	108.19
2005/06	353	374	23.03	105.95
2006/07	401	398	6.42	99.25
2007/08	365	372	-6.53	101.92
2008/09	386	410	10.22	106.22
2009/10	422	438	6.83	103.79
2010/11	473	459	4.79	97.04
2011/12	596	500	8.93	83.89

(Source: Annual Reports of IRD)

If the number of registered entities is considered, the assessment against non-filer in Income Tax is comparatively not enough. The targeted assessment against the non-filer is even not satisfactory. However, if only the targeted and

actual assessment is compared, the performance of the IRD in assessment against non-filer is satisfactory, since the performance is higher than the targeted in most of the fiscal years, and in the rest of the periods, the performance has close proximity to the target. The variance in between the target and the performance of assessment against non-filer in Income Tax has just ranged from 83.89% in the fiscal year 2011/12 to 108.19% in the fiscal year 2004/05. Except in the fiscal year 2008/09, not only the targeted assessment but also the actual assessment against non-filer has followed increasing trend. The target assessment has been increased from 258 to 596 in the decade, and the actual assessment has been increased from 233 to 500 in the same period. Also, the highest growth of 23.03% has been observed in the fiscal year 2005/06 and the lowest decrement of -6.53% has been observed in the fiscal year 2007/08. From the observation, it can be said that the performance of IRD in assessing the entities that are not filing in Income Tax should be enhanced greatly. It is awkward to say that only 500 or even less entities have been assessed against non-filer in Income Tax.

4.1.3.4 Decrease in No. of Income Tax Defaulters

The greater initiatives that the tax administration shows, the lower will be the number of income tax defaulters. The performance of the tax administration could be judged from the corner of the decrement in the income tax defaulters as well. The targeted and achieved decrement in the number of defaulters is analyzed in this section.

Table 4.6
Decrease in No. of Income Tax Defaulters

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	2404	2020	----	84.03
2003/04	2865	2561	26.78	89.39
2004/05	3544	3209	25.30	90.55
2005/06	3829	3048	-5.02	79.60

2006/07	4361	3556	16.67	81.54
2007/08	4049	3825	7.56	94.47
2008/09	4261	3956	3.42	92.84
2009/10	4872	4228	6.88	86.78
2010/11	5253	4381	3.62	83.40
2011/12	5983	4666	6.51	77.99

(Source: Annual Reports of IRD)

The target of IRD to decrease the number of income tax defaulters is increasing and thus making the possible defaulter aware that the tax they apparently think paying to the government is returned to them in various forms. However, the targeted numbers of decreasing the defaulters have never been fully achieved. Nonetheless, whatever achieved by the IRD in decreasing the number of defaulters is satisfactory. The achievement of the targeted numbers has ranged from 77.99% in the fiscal year 2011/12 to 94.47% in the fiscal year 2007/08. Moreover, it has been found that IRD has decreased at least 2020 income tax defaulters and at most 4666 defaulters within the observed periods. In addition, the actual growth in the decrement of the number of defaulters is highest, 26.78%, in the fiscal year 2003/04 and is least, -5.02%, in the fiscal year 2005/06. Though IRD has been quite success to reach the proximity of the targeted numbers of decreasing the number of income tax defaulters, the such targeted numbers and achieved numbers are not adequate, considering both the numbers of registrants in income tax, and the entities that need to be registered.

4.1.3.5 Refer to IRO to undertake Legal Action Against Income Tax Defaulters

After the assessment of the tax payments of the entities, the personnel of tax office decides whether taxpayer has made any evasion, and if he deems that there is probable default in the payment, the personnel refers to IRO to undertake legal action.

Table 4.7

Refer to IRO to undertake Legal Action Against Income Tax Defaulters

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	58	42	----	72.41
2003/04	73	60	42.86	82.19
2004/05	66	51	-15.00	77.27
2005/06	75	89	74.51	118.67
2006/07	82	94	5.62	114.63
2007/08	97	83	-11.70	85.57
2008/09	91	78	-6.02	85.71
2009/10	122	116	48.72	95.08
2010/11	118	103	-11.21	87.29
2011/12	130	154	49.51	118.46

(Source: Annual Reports of IRD)

Both the target and actual numbers of income tax defaulters referred to Internal Revenue Office to undertake the legal action have been increased in the observed periods. The targeted number to be referred to IRO has been increased to 130 by the end of the fiscal year 2011/12 from 58 in the fiscal year 2002/03. Similarly, the actual number that has been referred to IRO has been increased from 42 in the fiscal year 2002/03 to 154 in the fiscal year 2011/12. In the fiscal year 2005/06, 2006/07 and 2011/12, the performance of IRD in referring to IRO for taking legal action against the income tax defaulter is above the targeted, while in other remaining periods, the performance is lower than the target. The variance in the performance and the target number has ranged from 72.41% to 118.67% in the observed periods. Similarly, the growth

in actual referred number has been highest, 74.51%, in the fiscal year 2005/06 and lowest, -15.00%, in the fiscal year 2004/05.

4.1.3.6 Legal Action Against Income Tax Defaulters

After getting the report from the personnel about the probable tax default case, the IRO steps to judge whether the evasion has been really undertaken, and if such report turns true the legal action is initiated. The targeted number of legal action to defaulter and the actual legal action taken are compared and analyzed in this section.

Table 4.8
Legal Action Against Income Tax Defaulters

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	58	31	----	53.45
2003/04	70	46	48.39	65.71
2004/05	58	38	-17.39	65.52
2005/06	60	71	86.84	118.33
2006/07	67	62	-12.68	92.54
2007/08	89	64	3.23	71.91
2008/09	72	58	-9.38	80.56
2009/10	112	82	41.38	73.21
2010/11	108	86	4.88	79.63
2011/12	114	125	45.35	109.65

(Source: Annual Reports of IRD)

Not all the tax defaulters that have been referred to IRO to undertake legal action have been actually legally punished, as the referred number is lower than the action numbers in both the targeted and actual. The targeted number that has to be legally punished has ranged from 58 in each fiscal year 2002/03 and 2004/05 to 114 in the fiscal year 2011/12. Similarly, the actual number of defaulters that has been legally punished has ranged from 31 in the fiscal year 2002/03 to 125 in the fiscal year 2011/12. However, the performance of the

IRO in taking legal action to the targeted numbers of income tax defaulters is quite poor; first because the targeted numbers is awfully small in comparison to the number of registered income tax entities and second because such small targeted numbers have also been not fully achieved in most of the fiscal years. The achieved to targeted number of defaulters that have been undertaken legal action has ranged from 53.45% in the fiscal year 2002/03 to 118.33% in the fiscal year 2005/06.

4.1.3.7 Income Tax Due Collection from Legal Action

This section of the study presents the amount further collected from the legal action taken to the income tax defaulters. However, the targeted amount and the achieved amount differed in each year.

Table 4.9
Income Tax Due Collection from Legal Action (Rs. in Million)

FY	Target	Achieve		Target Achieved %
		Rs.	Growth	
2002/03	136.45	125.33	----	91.85
2003/04	137.64	126.44	0.89	91.86
2004/05	143.05	133.54	5.62	93.35
2005/06	145.51	142.64	6.81	98.03
2006/07	154.58	146.89	2.98	95.03
2007/08	159.41	150.08	2.17	94.15
2008/09	165.07	172.54	14.97	104.53
2009/10	170.23	201.56	16.82	118.40
2010/11	172.56	238.43	18.29	138.17
2011/12	180.00	259.00	8.63	143.89

(Source: Annual Reports of IRD)

In the later periods, exactly after the fiscal year 2008/09, the income tax due collection due to the initiation of legal action to the income tax defaulter has been observed to be higher than the expectation. The targeted income tax due collection by taking the legal action to the defaulter has been observed to be Rs. 136.45 million at the inception of the observed periods, and it has been

gradually increased, and by the end of the fiscal year 2011/12, the targeted income tax due collection has been recorded to be Rs. 180 million. Though the actual income tax due collection by penalizing the income tax defaulters are below the target up to the fiscal year 2007/08, the achieved income tax due is not unsatisfactory. The variance in the performance and the targeted income tax due is least, 91.85%, in the fiscal year 2002/03 and is highest, 143.89%, in the fiscal year 2010/11. Similarly, the growth in actual income tax due collection has been highest, 18.29%, in the fiscal year 2010/11, and has been lowest, 0.89%, in the fiscal year 2003/04. Finally, it can be said that the legal action undertaken against the income tax defaulter has been lucrative to the IRO to some extent, and such collectible legal action surely has aid the IRO to disseminate the information among the taxpayers that nobody can escape from liable income tax.

4.1.3.8 Survey Targeting to Income Tax on Rental Income

Many of the landlords are not paying the rent tax they are liable to pay for earning the income from tenants. For levying the rent tax to the landlord, the tax administration makes survey in each fiscal year related to the rental income.

Table 4.10
Survey Targeting to Income Tax on Rental Income

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	8813	8044	----	91.27
2003/04	8621	8218	2.16	95.33
2004/05	8905	8053	-2.01	90.43
2005/06	9203	8526	5.87	92.64
2006/07	9474	8819	3.44	93.09
2007/08	10256	8655	-1.86	84.39
2008/09	13109	11256	30.05	85.86
2009/10	12553	10414	-7.48	82.96
2010/11	16659	10208	-1.98	61.28

2011/12	14535	9576	-6.19	65.88
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(Source: Annual Reports of IRD)

As a part of administering the income tax effectively, and collecting the rental income much effectively, the IRO frequently makes market survey. The landlord needs to pay 10% of the rental income, but in most cases the landlords have been found to have evaded from the taxable rental income. To comply these evading landlords with the income tax act, the frequent market survey is thus essential. The IRO has targeted to survey 8813 cases of rental income in the fiscal year 2002/13, however, such targeted numbers has gradually increased in most of the periods, and thus it has been numbered to 16659, highest, in the fiscal year 2010/11. In none of the fiscal years, the IRO has been able to fully survey the targeted numbers for rental income. The achievement is 95.33% of target in highest in the fiscal year 2003/04 and is 61.28% in lowest in the fiscal year 2010/11. Numerically, the number of houses that have been surveyed ranged from 8044 in the fiscal year 2002/03 to 11256 in the fiscal year 2008/09.

4.1.3.9 House Rent Collection form Market Survey

The purpose of making survey relating to the rental house is to levy tax to those landlords who wittingly or unwittingly do not pay rent tax. The actual and targeted collection of rent tax collected from such market survey are presented and analyzed in this section.

Table 4.11

House Rent Collection form Market Survey (Rs. in Million)

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	6.23	5.59	----	89.73
2003/04	6.67	5.92	5.90	88.76
2004/05	6.89	6.14	3.72	89.11
2005/06	7.03	6.83	11.24	97.16
2006/07	7.28	9.06	32.65	124.45

2007/08	7.50	11.64	28.48	155.20
2008/09	8.14	15.13	29.98	185.87
2009/10	8.56	17.44	15.27	203.74
2010/11	9.03	21.14	21.22	234.11
2011/12	9.47	23.13	9.41	244.24

(Source: Annual Reports of IRD)

In each fiscal year, the IRD targeted to collect more rental income tax than that of previous year, as evidenced by the increasing target amount. However, such targeted rental income tax could not be achieved absolutely in the first four fiscal years. For instance, the IRD targeted to collect Rs. 6.23 million as rental income tax through market survey in the fiscal year 2002/03, however, the IRD could achieved only Rs. 5.58 million, 89.73%. Nonetheless, the achieved rental income tax in such four fiscal years, in also praiseworthy. After the first four fiscal years, the achieved rental income tax is higher than the targeted amount. In the fiscal year 2011/12, the achieved house rent collection from market survey is 244.24% of the targeted amount. The targeted rental income tax has been gradually increased from Rs. 6.23 million in the fiscal year 2002/03 to Rs. 9.47 million in the fiscal year 2011/12. Similarly, the achieved rental income tax has been increased from Rs. 5.58 million to Rs. 23.13 million within the observed periods. It seems that the IRD has paid more concern to rental income tax through market survey in the recent periods, while implementing the policy. In terms of growth, there has been a great jump in the fiscal year 2006/07, when the rental income has increased by 32.65%, and the lowest increment is on the fiscal year 2003/04, when the growth rate is just 5.90%. Nevertheless, it is recommended that the IRD make persistent market survey to force the landlords who are contriving to escape from the liable rental tax.

4.1.3.10 Registration on PAN through Market Survey

Registering in PAN means paying tax for operating the business, so in some cases, the people are operating the business without such registration. The tax administration makes survey on such activities and in some instances forces

them to register. However, the effectiveness of the tax administration in registering the entities to PAN needs to be judged.

Table 4.12**Registration on PAN through Market Survey**

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	7099	5527	----	77.86
2003/04	7538	5832	5.52	77.37
2004/05	7959	6224	6.72	78.20
2005/06	8247	6950	11.66	84.27
2006/07	8501	7481	7.64	88.00
2007/08	9370	7702	2.95	82.20
2008/09	13364	12282	59.47	91.90
2009/10	10180	13517	10.06	132.78
2010/11	12451	15924	17.81	127.89
2011/12	15278	17765	11.56	116.28

(Source: Annual Reports of IRD)

Except in the fiscal year 2010/11, IRD has targeted to registered more entities on PAN than that of the previous years in the remaining periods. The registration to PAN here indicates the registration of those entities that are operating the business without any registration to the Company Registrar Office. The targeted number of PAN registrants has been increased from 7099 in the fiscal year 2002/03 to 15278 in the fiscal year 2011/12. However, such targeted numbers could not be actually achieved fully till the fiscal year 2008/09. In other words, the actual registrants' number on PAN has been less than the targeted numbers till that year. After the fiscal year 2008/09, the actual number of registrant on PAN through market survey has been higher than the targeted numbers. It means that the actual registrants' number has crossed the expectations from the fiscal year 2008/09, and thus the market survey for registering the entities that are operating without registration has turned to be much fruitful than the expectation. It would thus not be unusual to say that the market survey should be conducted frequently for forcing the unregistered small firms to register on PAN. The actual number of registered firms on PAN

through market survey has been increased from 5527 in the fiscal year 2002/03 to 17765 in the fiscal year 2011/12, and the variance on the performance and the target has ranged from 77.37% in the fiscal year 2003/04 to 132.78% in the fiscal year 2009/10. Also, it can be categorically said that the market survey of IRD proved to be most effective in the fiscal year 2008/09, as the growth rate on registered number on PAN through such survey is highest, 59.47%, in that year.

4.1.3.11 Upgrading of PAN to VAT through Market Survey

If the transaction of the entities is below Rs. 2 million, it should be registered under PAN. However, if the entity registered under PAN desires to expand the business and cross such limitations of transactions, it should be upgraded to VAT registration. The number of upgraded entities from PAN to VAT in the surveyed periods is presented in this section.

Table 4.13
Upgrading of PAN to VAT through Market Survey

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	955	817	----	85.55
2003/04	998	832	1.84	83.37
2004/05	1090	895	7.57	82.11
2005/06	1231	1416	58.21	115.03
2006/07	1544	1639	15.75	106.15
2007/08	1862	1705	4.03	91.57
2008/09	1645	2213	29.79	134.53
2009/10	1865	2446	10.53	131.15
2010/11	2217	3018	23.39	136.13
2011/12	3120	3666	21.47	117.50

(Source: Annual Reports of IRD)

As compared to the registration on PAN after making market survey, the upgrading of those entities registered on PAN to VAT but doing the transactions greater than permitted amount, mainly for evading from the liable

tax, is much lower. It means that small number of firms that are operating by taking PAN are transacting above Rs. 2 million. In most of the fiscal years, especially after the fiscal year 2004/05, the actual number of upgrading the firm from PAN to VAT has crossed the targeted numbers. The targeted number for upgrade has been increased from 955 to 3120 within the decade, while the actual upgrade has been increased from 817 to 3666 in the same period. Thus, the variance in between the performance and plan in relation to the upgrade of firm from PAN to VAT has ranged from 82.11% in the fiscal year 2004/05 to 136.13% in the fiscal year 2010/11. Similarly, the growth rate in actual number of upgrade of firm from PAN to VAT has ranged from 1.84% in the fiscal year 2003/04 to 58.21% in the fiscal year 2005/06. Though it apparently seems that the market survey conducted by IRD turned success for upgrading of firms from PAN to VAT, the IRD needs to conduct the market survey much effectively and efficiently to trace out those entities that have been unwittingly left during the survey, since the small numbers of upgrades compared to the tremendous number of registrants in each fiscal is quite unbelievable.

4.1.3.12 Forced Registration in VAT through Market Survey

Some entities operate their business without upgrading from PAN to VAT either knowingly or unknowingly about the provision of transaction amount, and some entities do not even think necessary to register in VAT. The number of forced registration in VAT by tax administration by conducting market survey in each year are presented and analyzed in this section.

Table 4.14

Forced Registration in VAT through Market Survey

FY	Target	Achieve		Target Achieved %
		No.	Growth	
2002/03	889	665	----	74.80
2003/04	920	705	6.02	76.63
2004/05	958	881	24.96	91.96
2005/06	1080	905	2.72	83.80
2006/07	1290	1211	33.81	93.88
2007/08	1331	1503	24.11	112.92
2008/09	1446	1964	30.67	135.82
2009/10	1505	1741	-11.35	115.68
2010/11	1723	2037	17.00	118.22
2011/12	1850	2518	23.61	136.11

(Source: Annual Reports of IRD)

The numbers of unregistered entities doing transactions below Rs. 2 million is comparatively higher than the number of unregistered entities doing transaction above Rs. 2 million, as evidenced by lower number of entities forced to register on VAT in comparison to that on PAN by market survey. However, the effort of tax office's personnel in market survey is certainly laudable and hence such activities have certainly raised the income tax revenue of government to some extent. The targeted number of forced registration on VAT has increased from 889 in the fiscal year 2002/03 to 1850 in the fiscal year 2011/12, but the IRD could not fully achieve the target till the fiscal year 2006/07. After this fiscal year, the IRD, however, has achieved more the expectations, since the actual forced registration on VAT is greater than the targeted from such fiscal year. In fact, the actual achievement on forced registration is 136.11% of the target in highest and 74.80% of the target in lowest. Similarly, the actual number of forced registration has increased from 665 in the fiscal year 2002/03 to 2518 in the fiscal year 2011/12 and the growth rate in the performance of IRD related to forced registration through market survey is 33.81% in highest in the fiscal year 2006/07.

4.2 Primary Data Analysis

This chapter analyses information collected from primary sources i.e., through questionnaire. The questionnaire was distributed to the employees of tax office, tax experts (i.e. Auditors, Professors, Lawyers) and tax payers. The responses received from various respondents have been arranged tabulated and analyzed in order to facilitate the descriptive analysis of the study.

4.2.1 Attitude Towards Tax Education

To know the responses attitude towards tax education, a question was asked “Do you think that people are well inform about the tax system in Nepal”? The responses have been tabulated below:

Table 4.15
People’s Knowledge Towards Tax System

Respondents	Yes		No		Total	
	No.	%	No.	%	No.	%
Tax Employees	2	8	23	92	25	100
Tax Experts	5	20	20	80	25	100
Taxpayers	10	40	15	60	25	100
Total	17	22.67	58	77.33	75	100

(Source: *Opinion Survey, 2014*)

From the above table it has been clear that 77.33% of the respondents were against the question “Do you think that people are well informed about the tax system in Nepal?” It can be concluded that tax education is most necessary in Nepal to increase the tax consciousness of tax payer.

4.2.2 Specific Objective of Income Tax in Nepal

In order to know the specific objectives of income tax in Nepal, respondents were requested to rank their responsible. The question was asked” what should be the specific objective of income tax in Nepal?” Table 4.16 gives the breakdown of responses:

Table 4.16
Opinion Towards Objectives of Income Tax

Response	Group			Total	%	Rank
	Employees	Experts	Taxpayers			
To enhance the revenue of government	7	6	7	20	26.67	1
To meet the government expenditure	5	5	3	13	17.33	4
To narrow the income gap between rich and poor	5	4	6	15	20	3
To achieve the goals of national development and equal economic distribution	6	6	6	18	24	2
To check inflation	2	4	3	9	12	5
Total	25	25	25	75	100	

(Source: Opinion Survey, 2014)

Most of the respondents are supporting the objectives of to enhance the revenue of the government. 26.67% are in favor of the objective of to enhance the revenue of the government. 24% of them choose the objective of national development and equal economic distribution, another 20% choose the objective of to narrow the income gap between rich and poor, 17.33% are of them choose to meet the government expenditure and 12% of them gave to check inflation. In overall, to enhance the revenue of the government has been ranked 1, to achieve the goals of nation development and equal economic distribution has been ranked 2, to narrow the income gap between rich and poor has been ranked 3, to meet the income government expenditure has been ranked 4 and to check the inflation has been ranked 5 as the specific objective of income tax.

4.2.3 Attitude Towards Income Tax System in Nepal

To know whether the income tax system of Nepal is sound and efficient or not a question asked. “Are you satisfied with the existing income tax system of Nepal?” The responses received from the various respondents are tabulated below.

Table 4.17

Satisfaction Towards Existing Income Tax System

Respondents	Yes		No		Total	
	No	%	No	%	No	%
Tax Employees	2	8	23	92	25	100
Tax Experts	-	-	25	100	25	100
Taxpayers	2	8	23	92	25	100
Total	4	5.33	71	94.67	75	100

(Source: Opinion Survey, 2014)

From the above table, it has been clear that most of the respondents i.e. 94.67% of respondents are not satisfy with the existing income tax system of Nepal. More precisely, 92% of the surveyed tax employees, cent percent of the surveyed tax experts and 92% of the surveyed taxpayers showed dissatisfaction on the existing income tax system and thus urged for the prompt amendment. They further revealed that the complicated income tax act, rules & regulations, lack of education and awareness to taxpayers, lack of training & sufficient incentives to tax employees, lack of expertise in administration, practice of tax evasion and others are making the income tax system ineffective. It can be concluded from the above results that in the opinion of respondents, the income tax system of Nepal is not sound and efficient.

4.2.4 Appropriate Method while Assessing the Income tax in Nepal

Method of income tax assessment is very important in the assessment of income tax sound and appropriate assessment procedure is essential for collection of the large amount in the form of income tax. It is very important in managing the income tax because the amount of income tax is realized through the assessment finding out an appropriate method of income tax assessment a question put toward to the respondents asking “what method is more appropriate in Nepal while assessing the income tax?” The responses received are tabulated below:

Table 4.18

Appropriate method while Assessing the Income tax in Nepal

Methods	Groups			Total	
	Employees	Experts	Taxpayers	No	%
Assessment on the basis of account submitted	4	6	4	14	18.67
Self assessment	18	12	15	45	60
Assessment by the committee	3	7	6	16	21.33
Total	25	25	25	75	

(Source: Opinion Survey, 2014)

From opinion survey, it has been clear that self- assessment method is more appropriate for Nepal while assessing income tax 60% of respondents have positive opinion about self-assessment followed by 21.33% of respondents about the assessment by the committee. If each group is reviewed, the 18 out of 25 surveyed tax employees, 12 out 25 surveyed tax experts and 15 out of 25 surveyed taxpayers have supported the self assessment program.

4.2.5 Income tax- Evasion in Nepal

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

Table 4.19

Income Tax Evasion in Nepal

Response	Group			Total	%
	Employees	Experts	Taxpayers		
Yes	20	23	21	64	85.33
No	5	2	4	11	14.67
Total	25	25	25	75	100

(Source: Opinion Survey, 2014)

The above table reveals, that 85.33 respondents supported tax evasion as a major problem of income tax evasion in Nepal. Rest 14.67 % was again above view. It can be noted that almost all the person with high denominates were in favor of the question.

4.2.6 Factors Responsible for Tax Evasion

There may be much response for wide spread tax evasion. In order to know the main reason for tax evasion, the respondents were provide eight reasons and were provide eight reasons and were requested to rank them. The response has received are tabulated as below.

Table 4.20
Factors Responsible for Tax Evasion

Factors	Group			Total	%	Rank
	Employees	Experts	Taxpayers			
Defective tax administration	2	5	7	14	22	1
Inefficient income tax policy	3	3	1	7	11	5
In appropriate Income tax rate	1	1	1	3	4	8
Loopholes in income tax act.	2	1	1	4	6	7
Unwillingness of tax payers to pay tax	2	4	6	12	19	2
Lack of conscious in tax payers	4	4	1	9	14	4
Corruption in tax authority	5	2	3	10	16	3
Lack of political commitment	1	3	1	5	8	6
Total	20	23	21	64	100	

(Source: Opinion Survey, 2014)

The major reason for evasion of income tax from the above table according to the respondent's performance is the defective tax administration, as it has been ranked 1. Next to it is the unwillingness of tax authority, which is ranked 2. Similarly, the corruption in tax payers to pay tax has been ranked 3, the lack of conscious in tax payers has been ranked 4, the inappropriate income tax policy has been ranked 5, the lack of political commitment has been ranked 6, the loopholes in income tax act has been ranked 7 and the inappropriate income tax act has been ranked 8. The other factors stated by a respondents are wide spread practice of illegal business inadequate auditing and investigation and poor develop of corporate system.

4.2.7 Attitude Toward Provisions of fees, fines and Penalties

Income tax system of Nepal has the provisions of fees, fines and penalties for the regulation of low to find out the reasonability of these provisions, a question was asked, “Are penalties under income tax system is reasonable?” the response are tabulated as below:

Table 4.21
Attitude towards Reasonability of Existing Provisions of Fees, Fines and Penalties

Group	Yes		No		Total	
	No	%	No	%	No	%
Tax Employees	19	76	6	24	25	100
Tax Experts	20	80	5	20	25	100
Taxpayers	14	56	11	44	25	100
Total	53	70.67	22	29.33	75	100

(Source: Opinion Survey, 2014)

The table shows that 70% of respondents have expressed the provisions of fines and penalties are reasonable and 30% respondents have not taken the provision of fees, fines and penalties as reasonable. The respondents, who were against provisions of fees, fines and penalties has stated either to increase or decrease the amount of fees, fines and penalties.

4.2.8 Effectiveness of Income Tax Administration in Nepal

In order to find out the effectiveness of income tax administration, a question was asked “what do you feel about the current income tax administration of Nepal? The respondents who do you agree on the effectiveness, they have got alternative to choose about the position of income tax administration. The responses received from respondents are as follows:

Table 4.22

Effectiveness of Income Tax Administration

Response	Respondents			Total	%
	Employees	Experts	Taxpayers		
Efficient	5	3	4	12	16
Inefficient	13	19	18	50	66.67
Satisfactory	7	3	3	13	17.33
Total	25	25	25	75	100

(Source: Opinion Survey, 2014)

From above table, it is clear that income tax administration is not efficient to collect tax and has got majority percentage from the respondent's i.e. 66.67% and this group said that the lack of trained and competent tax employees, complicated tax laws, lack of proper communication, lack of voluntary compliance by tax payers, undue delay in assessment are making the tax administration inefficient.

4.2.9 Most Important Factors for Effectiveness of Income Tax in Nepal

In order to know the most important factor for effectiveness of income tax in Nepal respondents were requested to rank their responses on given choices.

Table 4.23

Important factors for Effectiveness of Income Tax in Nepal

Response	Group			Total	%	Rank
	Employees	Experts	Taxpayers			
Honest tax officers	7	7	7	21	28	1
Honest tax payer	5	6	7	18	24	3
Clear act, rules & regulation	7	6	6	19	25.33	2
Effective administration	6	6	5	17	22.67	4
Total	25	25	25	75	100	

(Source: Opinion Survey, 2014)

The most important factor for effectiveness of income tax is the honesty of the tax officers to their job, as it has been ranked 1. Next to it is the clear act, rules

and regulation, which has been ranked 2. Only then, the honest tax payers, who are ranked 3, are responsible for making the tax administration effective, and finally the effective administration, which is ranked 4, is responsible for making the whole income tax system effective.

4.3 Major Findings

From the analysis, the following major findings have been drawn;

Findings from Secondary Data Analysis

- The VAT is the most important tax revenue source of government. After that, the custom duty is the other most dependable tax revenue, and only then the income tax is the major source of the government. The income tax of the government has been increased from Rs. 967.64 crore in the fiscal year 2002/03 to Rs. 5245.15 crore in the fiscal year 2011/12.
- The tax paid by the corporate bodies is the major constitute of the income tax. After then, the tax paid by the small but tremendous numbers of individual firms is the major component. However, the tax levied on the public enterprises is less dependable to increase the income tax. The corporate tax has been increased from Rs. 192.43 crore to Rs. 1964.35 crore in the observed decade.
- Out of 541180 entities registered in Income Tax, 370821 has been registered within the observed decade. In fact, 77239 entities has been registered in the fiscal year 2011/12. Among various types of registered entities, the weight of individual firms numbering 414487 is highest.
- In most of the years, the actual assessment against non-filer in income tax has close proximity to the targeted assessment numbers. In some of the years, the actual assessed is even greater than the target. The actual to target assessment ratio has ranged from 83.89% to 108.19% in the observed decade.

- At the end of the fiscal year, the tax office has reduced 4666 income tax defaulters. However, the targeted numbers at that period was 5983, implying that 77.99% of the target has been achieved.
- In some fiscal years, the targeted number of income tax defaulters that would be referred to IRO to undertake legal action is less than the actual referred numbers, showing the greater performance of the IRD in these periods. In the fiscal year 2011/12, the IRD has targeted 130 defaulters but actually referred 154 defaulters to IRO for taking legal actions.
- Not all the tax defaulters that have been referred to IRO have been legally punished. In the fiscal year 2011/12, 154 defaulters were referred but after the assessment of the cases, 125 were legally punished either by charging fees, penalties or by cancelling registration.
- Administering the legal action aid the IRD to collect the revenue from the defaulters. The actual income tax due collected by the IRD has been increased from Rs. 125.33 million to Rs. 259.00 million in the observed decade. In last four fiscal years, the IRD collected such due even more than the targeted amount.

Findings from Primary Data Analysis

- Tax education is most necessary in Nepal to increase the tax consciousness of tax payers, as 77.33% of the respondents said that people are not well informed about the tax system.
- The major objective of the income tax in Nepal is to enhance the revenue of the government, as per the opinion 26.67% of the respondents and to achieve the goals of National Development and equal economic distribution and narrow the gap between rich and poor; stated by the 24% of the surveyed respondents.
- 94.67% of the respondents said that the Income tax system of Nepal is not sound and efficient basically due to inefficient tax evasion and lack of awareness of tax payers.
- Self-assessment method is more appropriate for Nepal while assessing

income tax. This suggestion is made by the 60% of the total surveyed respondents.

- 85.33% of the respondents said that the Income tax evasion is the major problem of Nepal for income tax generation.
- 22% of the respondents said that the main reason for tax evasion is due to defective tax administration, while 19% of the respondents claimed that the unwillingness of tax payers to pay tax and the other 16% of the respondents said that the corruption in tax authority are the main reasons behind tax evasion.
- 66.67% of the respondents said that the Income tax administration is not efficient to collect tax. Lack of trained and competent tax personal, complicated tax laws and undue delay in making assessment are the most important cause of ineffectiveness of Nepalese tax administration.
- 28% of the respondents said that the honest tax officer and the other 25.33% respondents stated that the clear act, rules and regulations are the most important factors for the effectiveness of income tax in Nepal.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

In most low-income countries, like Nepal, the tax administration are often corrupt, inefficient and do not operate in a transparent manner. This condition is the result of the mix of the taxes used, their faulty design, and the methods of tax administration. These tax administrations are generally affected by policies relating to the traditional public sector personnel system, salary levels, and criteria for advancement or discipline that usually are rooted deeply in the country's history. In these countries, the systems of tax administration follow a predictable pattern of behavior, - but in a traditional way. Governments have been able to generate revenue by setting revenue targets for the tax administration while not being very concerned about how these targets are achieved. Tax officials cannot be blamed individually; any official joining tax administration will have to follow existing practice and procedures. This has created a stable system in which government revenue targets are met, most taxpayers pay less than their legal tax liabilities, and tax officials make considerable income as a result of side payments, which arise from their negotiations with taxpayers. A great deal of uncertainty and administrative congestion are by-products of such a system.

Among various revenues of the government of Nepal, the income tax is one of the major revenues. To make the income tax administration more transparent and much effective, the government formulated 'Income Tax Act Nepal, 2058'. However, whether such Act has been administered in a way it was supposed to be done while making the plan is still a big question. Nonetheless, the persistent efforts of the government and bureaucracy to improvise the income tax administration are significant. Thus, to know the income tax administration

in Nepal, the present study has been conducted by analyzing both the primary and secondary data. The study is empirical, descriptive, and analytical in nature. To collect the primary data, the study sets a questionnaire related to the tax administration and collects opinions from taxpayers, auditors and tax employees. The study finds that to some extent the administration of income tax is satisfactory but still the exercise to make the administration much effective is insufficient.

5.2 Conclusion

Although the income tax is considered as one of the most important revenues of the government, in reality it is the third source of revenues in Nepal. In fact, the VAT is the most important source of revenue for the government. It can be said that income tax source of the government relies heavily on the tax paid by the corporate bodies, however, the contribution of tremendous small and medium firms to raise the income tax revenues could not be undermined. Day by day, the awareness among the people to operate any business activity only by registering in the Company Registrar Office has been increased, as a result the number of registrants has noticeably increased. In most of the years, the actual assessment against non-filer in income tax has close proximity to the targeted assessment numbers. The activity of the Income Tax Office in actively reducing the income tax defaulters and punishing fines and penalties and even seizing the business in some of the cases truly reflects the gradual increasing activeness of the Office. However, still the targeted number to undertake the legal action has not been fully achieved.

From the primary data analysis, it can be concluded that the effort to government to aware the people about the benefits of the tax payments in the form of the development of the basic infrastructures and the opportunities of the employment and the economic benefits is not sufficient. Moreover, it can be said that the Income tax system is not sound and efficient basically due to inefficient tax evasion and lack of awareness of tax payers. Although the self

assessment method is appropriate while assessing the income tax, it would be appropriate in the initial operation year of the company, and in other periods, the assessment of the account by the tax official would be better so to avoid the tax evasion by the taxpayers. Main reason for tax evasion is due to defective tax administration, unwillingness of tax payers to pay tax and corruption in tax authority. Finally, it can be said that to make the tax administration much effective, the effort of all the stakeholders; government, tax payers, tax office and others, are equally significant.

5.3 Recommendations

Finally, the following measures are recommended for the enhancement of the income tax administration of Nepal;

- The tax administration can be structured by type of tax or by function of tax administration. The tax office is advised to follow the unified functional system, Under this system, a tax officer is made responsible for the administration of each and every aspect, including the registration, assessment and collection of specific tax in particular area.
- The personnel development is one of the major problems for the inefficiency of the income tax administration. So the tax office is recommended to pay concern to the human resource development. A specialized group should be created for administrating taxes with special rules relating to recruitment, transfer, training, promotion, salary, and so on. The Office should contrive to change the attitude of the tax officials, if necessary, so as to make them more service-minded.
- In Nepal, tax administrations use traditional techniques and procedures, which are far from desirable. Tax administrators are guided by the traditional excise tax mentality. A computerized and modern administrative techniques needs to be adopted by the tax office of Nepal.
- One of the important function of the modern income tax administration is to raise the level of voluntary tax compliance. In order to encourage this,

the tax administration needs to carry out an extensive taxpayer education program.

- Simple and transparent tax provisions enhance compliance with the law, while consistently applied penal provisions discourage noncompliance. Therefore, along with the simple and transparent provisions, uniformly enforced penal provisions also form the basis of the effective income tax administration.
- It is necessary to establish an appeal system that is independent and impartial. At the same time, there must be specific rules and time requirement in order to maintain revenue levels. The appeals system should be structured to balance a number of interests.

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APPENDIX I

Questionnaire

Name:

You are: Tax Employees/Tax Expert/Tax payer (Tick one)

Please tick (√) the answer of your choice or wherever appropriate put in order of preference from I to last number on the basis of alternatives. Number I stand for the most important and vice versa.

1. Do you think that people are well informed about the tax system in Nepal?"
 - a. Yes
 - b. No

2. what should be the specific objective of income tax in Nepal"?(please rank)
 - a. To en chance the revenue of the government.
 - b. To meet the government expenditure
 - c. To narrow the income gap between rich and poor.
 - d. To achieve the goals of national development and equal economic distribution.
 - e. To check inflation
 - f. Other, please specify.....

3. Are you satisfied with the existing income tax system of Nepal"?"
 - a. Yes
 - b. No

If no, please specify:

4. What method is more appropriate in Nepal while accessing income tax"?
- a. Assessment on the basis of accounts submitted by the tax payer.
 - b. Self-assessment.
 - c. Assessment by the committee.
 - d. Assessment by the committee.
 - e. Other, Please specify

5. In your opinion, is there a major problem of tax evasion in Nepal?
- a. Yes
 - b. No

6. What are the factors responsible for income tax evasion? (Please rank according to the priority).
- a. Defective tax administration.
 - b. Inappropriate income tax policy
 - c. Inappropriate income tax policy.
 - d. Loopholes in income tax act.
 - e. Unwillingness of tax payers to pay tax.
 - f. Lack of unconsciousness in tax payer.
 - g. Corruption in tax authority.
 - h. Lack of political commitment.
 - i. Others please specify.

7. Are the provisions of fees, fines and penalties under income tax system is reasonable?
- a. Yes
 - b. No

If no, how can be made reasonable? (Please Specify)

8. What do you feel about the current income tax administration of Nepal?

- a. Efficient
- b. Inefficient
- c. Satisfactory

If inefficient what are the major causes? (Please Specify)

9. What are the most important factors for effectiveness of income tax in Nepal? (Please rank).

- a. Honest tax officers.
- b. Honest tax payers.
- c. Clear act, rules and regulations.
- d. Effective income tax administration.
- e. Others, Please specify.....

Thank You.