

**A Thesis on
A STUDY OF
INCOME TAX EXEMPTIONS AND DEDUCTIONS
IN NEPAL**

Submitted By:

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Master of Business Studies (M.B.S.)**

RECOMMENDATION

This is to certify that the thesis

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A study of Income Tax Exemptions and Deductions in Nepal

Has been prepared as approved by this department in the prescribed format of the faculty of management.

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DECLARATION

I hereby, declare that the work reported in this thesis entitled “A Study of Income Tax Exemptions and Deductions in Nepal” submitted to office of the Dean, faculty of management, Tribhuvan University, Kirtipur, is my original piece of work done in the form of partial fulfillment of the requirement for the Master’s Degree in Business Studies under the supervision and guidance of Dr. Gopi Nath Regmi, Central Department of Management, Kirtipur.

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ABBREVIATIONS

A.D.	:	Anno Domini
B.S.	:	Bikram Sambat
C.D.M.	:	Central Department of Management
CEDA	:	Centre for Economic Development and Administration
DDC	:	Dairy Development Corporation
Dr.	:	Doctor
DT	:	Direct Tax
e.g.	:	example granta or for example
ed.	:	edition
eds.	:	editors
etc	:	and the other
et.al	:	and others
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
GON	:	Government Of Nepal
i.e.	:	that is
IT	:	Income Tax
IRD	:	Inland Revenue Department
ITA	:	Income Tax Act
Ktm.	:	Kathmandu
Ltd.	:	Limited
MBA	:	Master in Business Administration
MBS	:	Master in Business Studies
MOF	:	Ministry Of Finance
Mr.	:	Mister
No.	:	Number
NRB	:	Nepal Rastra Bank
Prof.	:	Professor
Pvt.	:	Private
Re.	:	Rupee
Rs.	:	Rupees
S.N.	:	Serial Number

Sec.	:	Section
SEZ	:	Special Economic Zone
T.U.	:	Tribhuvan University
TR	:	Total Revenue
TDS	:	Tax Deduction at Source
USA/US	:	United State of America
VAT	:	Value Added Tax
Viz.	:	Namely
Vol./Vols.	:	Volume(s)
\$:	Us Dollar

CHAPTER-I

INTRODUCTION

1.1 Background of the Study

One of the prime need of almost all the developing and underdeveloped countries of the world has been economic development. Similarly government efforts of those countries have been directed towards achieving high economic growth rate, reducing poverty and economic disparities, improving living standards of people etc (Bhattarai and Koirala, 2011).

The government of a country requires more revenue mobilization for overall economic development and state welfare. Besides this, government also requires some sources of income called revenue to handle day to day administration work, to maintain peace and security and to launch other public welfare activities (Bhattarai and Koirala, 2004). The government of a nation requires revenue to run the country just like the blood is needed to perform a circulatory system in a body. In a developing country like Nepal, there is a necessity for raising larger volume of funds for the development and administration expenses by the government to fulfill its responsibilities towards its people.

The government collects the required resources mainly from two sources: debt and revenue. The debt can be collected either from internal or external sources. The internal debt is collected within the country while external debt is collected from outside the country. The debt financing of the government is known as deficit financing. The revenues on the hand come basically from two sources: tax and non tax. Non tax sources include different revenues like gifts, grants, revenue from public enterprises, administrative revenues such as registration fees, fines and penalties. Tax sources include custom duty, excise duty, VAT, income tax etc (Bhattarai and Koirala, 2011).

The revenue collection is a challenging task in itself which demands increasing necessity of regular expenditure in general and development expenditure in particular. However, resource mobilization is very low compelling the government to rely heavily on foreign assistance. External assistance (foreign aids) is not bad for

economic development of the nation. But the experience of the most of the developing and underdeveloped countries shows that there are negative effects of increasing international grants and loans to finance the public development activities. They are uncertain, precarious, inconvenient and not conducive to the healthy and overall development of the nation (Sharma and Luitel, 2002).

The expenditures incurred by the state can be fulfilled by two sources. They are namely: internal and external sources as described earlier. Internal sources are the best alternative for the nation because they are certain, convenient and reduces the dependability upon other countries. Uses of external sources to meet expenses are not good because it reduces the liquidity position of the government, increases over dependency upon other countries and increases the inflation. So, internal sources are more important not only for financing necessary funds but also for the proper mobilization of external sources (Sharma and Luitel, 2002).

Within internal sources of fund non-tax sources are imposed according to the necessity of the government. So, they are uncertain and inconvenient. So, taxes are the better sources of public revenue. The use of tax is safer for financing public revenue in developing countries. So, taxation has been taken as the best effective tool for raising the public fund from foreign countries and international organization. External sources of fund are more important for developing and underdeveloped countries. It is used for economic development, reconstruction, foreign exchange and to recover from crisis condition for productive use etc (Sharma and Luitel, 2002). But external sources are uncertain, inconvenient and not good for healthy development of the nation because they have to be paid after a certain time. So, it is better to mobilize internal sources rather than looking with beggars eyes the donors (Pant, 1996).

Findlays Shirras defined tax as “a compulsory contribution to public authorities to meet the general expenses of the government which have been incurred for the public good and without reference to special benefits.”

Prof. Seligman defined tax as “a compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all without reference to special benefit conferred.”

Adam Smith defined tax as “a contribution from citizens for the support of the state”

From the definitions given above, it can be said that firstly, a tax is a compulsory levy from individuals, household and firms and those who are taxed have to pay it without getting corresponding benefit of services or goods from the government. A taxpayer is not entitled to compel the government, while paying taxes, to give something to him in return of the amount he has paid. Due to this compulsory nature, people have expressed different views in satirical way about the taxation. In this respect, some say “Nothing is certain in this world but death and taxes”, some say “Death and taxes are both certain ... but death is not annual”; while others say “Death means stopping to pay tax”. Here, it should be noted that all compulsory payments are not taxes. For example, fines and fees are also compulsory payments without having direct benefit to the payer but they are not taxes because the objective is not to collect revenue but to curb certain types of offences. Secondly, the taxpayer does not receive equivalent benefit from the government. A tax is not a price paid by one for which he can claim for goods and services. The charge of price for goods and services by public authority is not a tax. Thirdly, the tax is paid to the government for running it. Fourthly, the amount is spent for common interest of the people. The tax is collected from haves and basically, spent for the interest of have-nots in the society. Fifthly, a natural or an artificial person pays the tax (Kandel, 2004:3).

In conclusion, it can be said that a tax is a liability to pay an amount to the state on account of the fact that the assesses have income of a minimum amount from certain specified sources or that they own certain tangible or intangible property or that they carry on certain economic activities or they consume certain goods and services which have been chosen for taxation (Kandel, 2004:3).

Generally taxes can be classified into two types. They are: (a) Direct tax and (b) Indirect tax.

A direct tax is a form of tax paid by a person on whom it is legally imposed. It is collected directly by the government from the person who bears the tax burden. Each individual's tax liability is assessed separately. The great merit of this tax is that being progressive and imposed as per the property and income. Heaviest burdens are placed on the broadest back. Their progressive character also gives additional weight to their

role as built in stabilizers. Examples are income tax, property tax, vehicle tax, interest tax, expenditure tax, death tax, gift tax etc (Bhattarai and Koirala, 2011).

An indirect tax is a form of tax imposed on one person but paid partly or wholly by another. In other words, such tax is levied on one person who does not bear it from his/her own income. Instead, the tax liability is transferred by collecting it from customers by adding it to the price of goods or services. It means it is collected by mediators who transfer the taxes to the government. The person bearing and paying the tax is different. The great merit of this tax is that there is a less chance of tax evasion and there is mass participation. It is the tax on consumption or expenditures. Custom duty, excise duty, VAT, sales tax, import and export tax etc. are indirect tax (Bhattarai and Koirala, 2011).

Income tax has very important role in the Nepalese economy. Income tax is one of the better sources of the public revenues. Income tax is the tax of equity. It is imposed according to the paying capacity of taxpayers. Therefore, there is possibility of reducing gap in income by imposing higher rate to those who have higher income and lower rate or none to the people having poorer economic condition. It is tool of achieving maximum social and economic objectives as per the expectation of the constitution of Nepal. "Income tax is essential not only for collecting government revenues but also for controlling over consumption for saving and for generating more employment" (Joshi, 1998). Different acts and laws are in action to improve tax system and policy so as to maximize the collection. Income tax is charged on person's income according to the law of nation. It covers all the fees, additional fees, fines etc. Income includes all income, which are received from business, investment and employment.

Within the income tax system, exemptions and deductions are more important to know about income tax because they are used continuously and treated differently year to year. To make updated knowledge about income tax system, it should be given a due care as a result of which we can compute net income and tax liability. Income tax law of every nation has clearly mentioned about the exemption of incomes and deduction of expenses.

Although the legal provision has been made and updated timely, there are many problems about income tax and exemptions and deductions. There are many problems in income tax practice in Nepal such as; leakage in tax, feeling of people about tax as a penalty, lack of consciousness of people, inability of tax administration to cover new tax payer, delays in computation and collection, lack of accuracy and unity in accounting system, etc. The main objectives of taxation are more revenue collection. Exemptions and deductions play important role to collect the tax. Because of all these reasons exemptions and deductions of income tax system must be reviewed and immediate correction should be made.

1.2 Statement of the Problem

The government expenditure in Nepal is increasing but the government revenue is not growing equivalently as per expenditure. So, the government is facing deficit financing. The deficit financing increases share for external as well as internal and foreign aids. For the payment of external as well as internal loan, financing the government expenditure, internal revenue is the main source. Tax revenue is one of the main sources of government revenue. Income tax is a strong component of tax revenue. But lack of proper implementation of tax policies, lack of knowledge, lack of public awareness, lack of support from business community and lack of efficient management are problems on revenue collection.

As other developing countries, Nepal is in need of huge capital investments for development purposes. The government has to make heavy spending on the several overheads. The funds required to make expenditure for development activities can be obtained by two sources: external sources and internal sources. The external financing depends upon the interest and the conditions of the funding countries and agencies and internal source has no obligation towards the third party and less risky compared to the external funds.

Economic growth is the indicator of the development of the nation but economic condition of Nepal is not satisfactory because of low economic development and growth. It needs huge amount of capital for the economic development of Nepal. For this revenue collection should be increased to boost up the economic development.

Higher resource mobilization is the best option of healthy economic development for the nation.

Nepal's low revenue is due to poorly designed and defective tax system where taxes are less productive, less responsible and distortion. In Nepal, the coverage of income tax is very low (Agrawal, 1978). There is greater propensity to evade taxes. Corruption is also a serious problem has been causing to increase the inequality of income and wealth of Nepalese people. Tax authorities are inefficient and ineffective in enforcement. There is no integrated program for taxpayer's education, assistance, guidance and counseling. Most of the rich people do not pay tax by using loopholes and advantages of an inefficient tax administration and a significant amount of tax revenue collected goes in the unseen hand of government machinery.

ITA, 2058 has provided some exemptions granted to the special industries and the industries established in the backward areas of Nepal are not effective and scientific. Although tax incentives or concessions encourage or support to establish industries in certain area but they vanish or change name, ownership or place of the business when the tax exemptions and concession period expires.

ITA, 2058 has also provided exemption limit to an individual into two distinct categories in Nepal. They are individual and the family according to the marital status. The classification does not recognize the various sizes of the dependent family member. There is no discrimination between a taxpayer having only a single spouse and taxpayer with a spouse, parents and children. Therefore this limit in the Nepalese context neither shows any specific or definite relationship with per capita GDP nor with the rate of inflation or poverty.

In Nepal, the present deduction allowed are the provident fund contribution of the tax payer, the life insurance premium, investment or contribution for citizen investment fund, medical expenses, research and development expenses, pollution control cost etc. Besides these expenses, donation made for non profit making organization is also allowed for deduction. At present there are no any provisions for deduction of the necessary expenses like the higher education expenses, security expenses in the unsecured and politically polluted area like Terai of Nepal, pregnancy delivery expenses etc.

However, various problems of income tax and exemptions and deductions can be stated in terms of the following questions:

- Is the contribution of income tax to national revenue of Nepal satisfactory?
- Are the exempted items of income and exemption limit being provided by enacted Income Tax Act are sufficient?
- Are the current deductions of expenses sufficient?
- Are the provisions made under the Nepalese Income Tax Act sufficient in all respect?

1.3 Objectives of the Study

As even the title suggests, the main objective of this study is to analyze the present system of tax exemptions and deductions in Nepal. Giving the suggestion as much as possible to improve the tax system help the government to collect more revenue and use it in the process of national development. Most of the people think that tax is burden and there is no any benefit against paying tax. Our objective is to change this type of mentality and encourage people to pay tax. This research will make people aware about exemption of incomes and deduction of expenses. However, the main objective of the study is:

- To analyze the contribution of income tax to national revenue of Nepal.
- To examine the deduction facilities provided by the ITA, 2058.
- To evaluate the exemption limit under the ITA 2058.
- To analyze the views of tax experts, tax officers, tax payers about the exemption and deduction facilities provided in the present ITA, 2058.

1.4 Scope of the Study

The study tries to cover the major constituents of income tax system in Nepal. It aims to find out the exemption and deduction of income tax provided by ITA, problems and weaknesses in income tax system, contributions of income tax to the government revenue and tries to suggest some possible areas for reform. Especially the income tax exemption and deduction is discussed in detail.

In brief the study covers the following aspects of income tax system of Nepal:

- Nepalese tax structure.
- Role of income tax in Nepal.
- Exemption limit and deduction facilities under ITA 2058.
- Existing position of Income Tax in Nepal.

1.5 Significance of the Study

Developing country like Nepal requires higher magnitude of financial resources for the development program. Internal resources have more significant role than the external resources for developmental program. The income tax is one of the most important internal sources of government revenue. Income tax plays significant role in the economy. But it is a matter of great embarrassment to quote that the contribution of income tax to the national revenue is very low in Nepal. To increase the contribution of income tax to the national revenue, problem faced by the income tax system should be researched and analyzed objectively and then the corrective actions should be started. Few studies and research works have been conducting in the area of income tax in Nepal. Within income tax, the intensive study on tax exemption and deduction hasn't been done in Nepal. Most of the researchers are based on contribution of income tax on national revenue. They are not giving main emphasis to research on exemption and deduction topic which is maintained in ITA. Due to this context need and significance of this study can be known easily.

This study will also be basically useful for the readers who are interested in the field of taxation, policy makers, researchers, tax officials and especially those students who are engaged in the research works on exemptions and deductions of income taxation in Nepalese tax system. It also clears the role of exemptions and deductions in total revenue collection, exemption and deduction system in Nepal and problems with regard to collection procedure and other important information. At last, it is expected that the study will add a drop of literature to the field of income tax.

1.6 Limitation of the Study

There are various constraints in this study. The present study aims to analyze only certain aspects of income tax and study of exemption of incomes and deduction of expenses in Nepalese income tax. It is not the complete study of income tax system in

Nepal. As every study has its own limitations this research is also conducted according to the objectives, statement of problems and methodology. Basically, the study has been conducted as partial fulfillment of the requirement of the degree in “Master of Business Studies”. So, it has the following limitations:

- It is based on exemptions of income and deductions of expense but not as the complete study of income tax.
- The reliability of this study depends largely upon the reliability and validity of the primary and secondary datas.
- Due to the small sample size it does not represent Nepal as a whole.
- The views of respondents are collected only from Katmandu valley.
- Absence of required related data of various countries concerned with the study limits to detail study.
- This research is based on limited year.

1.7 Organization of the Study

The whole study is organized in five chapters. They are:

- **Introduction**
It serves as an orientation for readers of the report, providing them perspective view of the report for better understanding. It includes background, statement of the problem, objectives of the study, scope of the study, limitation of the study and scheme of the study.
- **Review of literature**
The second chapter is about the review of the literature and conceptual frame works. Books, unpublished dissertation reports and articles etc have been reviewed for the study. Conceptual frame work includes legal provisions regarding ITA 2058, concept of tax, concept and meaning of income tax, income tax in international context, and some legal provisions of income tax in Nepal etc.

- **Research methodology**

The third chapter is concerned with research methodology which includes research design, population and sample, nature and sources of data collection procedure, data processing and analysis procedure etc.

- **Data presentation and analysis**

The fourth chapter is the major part of this study. This chapter is termed as presentation and analysis of data. This chapter includes research gap in Nepal, tax GDP ratio, Nepalese government revenue structure, composition of tax revenue in Nepal, exemption of incomes and deduction of expenses in income tax system etc and opinion survey is analyzed. It also describes the problems and weaknesses of tax administration in Nepal. It also contains major findings of the study.

- **Summary, conclusion and recommendation**

Fifth is mainly concerned with summary, conclusion and recommendation.

Appendix and bibliography are presented in the last part of the study.

CHAPTER-II

REVIEW OF LITERATURE

The review of literature is a very important aspect of the research. It is reviewing of research studies of other relevant proposition in related area of the study so that all the past studies, their conclusion and deficiencies may be known and further research can be conducted. For this several books, dissertation, reports, and articles published in journals are reviewed. Even though lacking the materials resembles topic, efforts were exerted for searching literature through various sources as well.

2.1 Theoretical Concept/Conceptual Framework

Modern income tax was first adopted by the Great Britain in 1799, as a temporary instrument to generate revenue required for the war against France. This tax was introduced by many countries for similar reasons. But due to its revenue potential, the tax has had been used as a permanent instrument by the government in various countries despite its strong opposition in the initial stage of its implementation. The United Kingdom imposed the income tax regularly from 1860. Income tax was introduced in Switzerland in 1840, Austria in 1849, India in 1862, Italy in 1864 and Nepal in 1959.

Now this tax is the major source of revenue in the developed countries and has been appearing as an important source of revenue in the developing world as well. This tax is also considered as fairest revenue since it can be tied with the taxable capacity of the taxpayers.

The finance act annually prescribes tax rates and classifies some of the procedures mentioned in the ITA whereas income tax governs procedure, penalty and administration of taxes. Hence provision and procedure of income tax can be analyzed by the study of exemptions and deductions. The provision of income tax exemption and deduction has started since the enactment of the first finance act in 1959. The first slice of income has always been exempted from income tax. The original level of statutory exemption limit was Rs. 7000. This limit has been increased time to time. The income tax laws in Nepal have been specific regarding deductions. There has

been a practice of enumerating allowable deductions and those expenses not mentioned in the list are not deductible.

2.1.1 Concept of Tax

In general, tax can be defined as a levy or other type of financial charge or fee imposed by state or central government on legal entities or individuals. It is a compulsory levy from individuals, household and firms to central or local government. It is the legal duty of every citizen of the country to pay honestly. It may be levied on income, property and even at the time of purchasing a commodity. It is computed and prescribed in the law. If a person defies the tax payment, he may be punished in the court of law. A taxpayer is not entitled to compel the government, while paying taxes, to give something to him in return of the amount he has paid (Bhattarai and Koirala, 2011). According to plehm, “taxes are general contribution of wealth levied upon persons, natural or corporate to defray expenses incurred in conferring common benefits upon the residents of the states. Similarly according to Dalton, “A tax is compulsory contribution imposed by a public authority irrespective of exact amount of services rendered to tax payers in return”.

In conclusion, it can be said that a tax is a liability to pay an amount to the state on account of the fact that the assessor have income of a minimum amount from certain specified sources or that they own certain tangible or intangible property or that they carry on certain economic activities which have been chosen from taxation.

In the modern day, the main objective of taxation has been shifted from security perception to the economic development. The modern objective of taxation is not only to maintain peace and security but also to conduct development activities. We can enumerate the objectives of taxation as follows:

- a. To increase the revenue for welfare state,
- b. To regulate the economy in accordance with the need of the country,
- c. To have equitable distribution of income and property,
- d. To prevent concentration of wealth in a few hands,
- e. To increase the production of particular goods,
- f. To increase the employment, saving and investment,
- g. To minimize regional disparity,

- h. To implement government policy, and
- i. To control the production of certain goods.

From the above, we can conclude that the tax has the objectives of raising revenue, to have resource mobilization, equal distribution of wealth and income in the society, encouragement in production of certain products, encouragement in employment, saving and investment, removal of regional imbalances and enforcement of government policy.

2.1.2 Concept and Meaning of Income Tax

The term income may be defined as the best measure of ability in the sense of economic well being. Income is the primary determinant of level of living which a family enjoys. Income refers to the economic gain to a particular period of time. Incomes consist of total increase in net wealth and consumption.

Section 2 of ITA 2058 defines “Income” as the total amount received (receivable in case of the accrued method of accounting) from business, employment and investment. Income denoted the total receipt, which are included in calculation of taxable income.

Income tax, as the word itself, is a tax on income. In a broad sense, income tax is a levy based upon the production or receipt or gain of the taxpayers within a definite period of time. ITA, 2058 as well recognizes that income encompasses both revenue and gain. Revenue is treated as gross receipt from the disposal of goods. Gain is treated as gross receipt of the property less the outflows to acquire it. Income tax is charged on the taxable income. Taxable income is derived by deducting the allowed expenditure from the revenues and gains. So the formula may be framed like this:

$$\text{Revenues} + \text{Gains} - \text{Allowable Expenses} = \text{Income}$$

Income is derived for a certain period. In Nepal the period for twelve month commencing from 1st Shrawan to end of Ashad is treated as one income year. ITA 2058 has classified the taxable income into three classes: income from business, income from employment and income from investment. The total of the incomes of a person is said to be an income of the person.

Income from business is derived by deducting allowed expenses of the business from the revenues of the business. In the same way the income from employment and investment are derived. Income as shown by financial statements may differ from the taxable income. Income tax is payable on the taxable income. Thus, income tax is defined as tax chargeable on income of a person as per the relevant ITA.

2.1.3 Income Tax in the International Context

Great Britain is the first country in the world to introduce the modern income tax. This country introduced income tax in 1799 in order to generate revenue to finance the war fought with France between 1793 A. D. and 1816 A.D. This income tax law was enacted on January 9, 1799, which was the first modern income tax law in the world. It came into force on April 5, 1799 A.D. Since this was levied as a war tax it was repealed on April 5, 1802 A.D. after the end of the war with France at first. However, the income tax was reinstated in 1803 after the outbreak of war again with France on May 18, 1803 A.D. The new ITA was enacted on August 1st, 1803 A.D. as a war tax. It was abolished on March 18th, 1816 after the end of the Napoleonic wars. Income tax was again proposed on March 11th, 1842 A.D., as temporary measure for three years to generate revenue to enable government to avoid budget deficits while carrying out major tariff reforms. This tax was not abolished even after the lapse of three years because its yield accepted as a permanent tax by the 1980s.

In the USA also income tax was introduced in 1862 A.D. to generate revenue to finance civil war. The federal corporation income tax was introduced in 1909 A.D. In Japan, income tax was introduced in 1887 A.D. through the enactment of the Income Tax Law on March 23rd, 1887 A.D. It was a general individual income tax and extended to the corporate income in 1899 A.D.

Although the income tax has been levied in different form before the unification of Germany in 1871 A.D., income tax became an effective instrument since the Prussian Reforms of 1891 A.D. In India, while income in its modern form was adopted in 1860 A.D., several experiments were made from 1860 to 1886 A.D. and finally the systematic income tax legislation was enacted in 1886 A.D., Income tax was introduced in Switzerland in 1840 A.D., Austria in 1846, Italy in 1864, New Zealand in 1891, Canada in 1892, Holland in 1892-93, Australia in 1895, Denmark in 1903,

France in 1909, SriLanka in 1932, Venezuela in 1943, South Korea in 1948 and Nepal in 1959 A.D.

Similarly, this tax system was adopted by many other countries over the years and had undergone considerable changes in those countries that have already adopted it. The main features of the changes in the income tax system over the years are as follows:

- The first income tax adopted by Britain was based on the global principle. However, the 1803 A.D. version of the English income tax was based on scheduler system.
- There has been a different practice in other countries in different times. Initially, income tax was limited to the income generated within the country but with the globalization, taxation of worldwide income came into vogue.
- Most of the developed countries levy tax on the worldwide income of their residents while some developing countries levy tax only on income generated within the country.
- There have been different practices regarding the taxation of individuals and companies. Some countries such as Japan initiated with the taxation of individual and brought companies into the tax net after a few years of the implementation of income tax. In some countries, such as Nepal, initially both individuals and companies were taxed in the similar way but later on they were taxed in different ways, companies with a flat rate and individuals with progressive rates.
- There are different practices regarding the assessment of income tax. The tax is assessed under the official assessment system in some countries while assessed by the taxpayers themselves in some other countries. Official assessment was common in the past but self-assessment has become popular in the recent times, although the concept of self-assessment was already adopted in Britain in 1803 A.D.
- The history of income tax is tumultuous, the situation is different now. Income tax is an important element of the modern tax system.

This tax system has been adopted by all sorts of countries levied as an important instrument to generate revenue required to finance state activities. Thus tax is also considered as a fairest tax since it can be tied with the taxable capacity of the payers.

2.1.4 Evolution of Income tax in Nepal

The idea of introducing income tax in Nepal originated along with the first “Budget” on 21st Magh 2008(1952). The then finance minister in the first budget speech said ‘a proposal to levy an income tax including tax on agricultural income is under consideration.’ Several attempts were made to introduce income tax in subsequent years. However, it could not be introduced until 2016 due to political instability. For the first time, the Finance Act 2016(1959) has imposed tax on business profit and remuneration in Nepal.

The first elected government finally introduced “Business profit and Remuneration Tax Act 2017” to impose income tax on remuneration and business profit in Nepal. The underlying reasons for the introduction of income tax were to generate more revenues in order to finance development activities and to help to establish social justice through redistribution of income. “Business Profit and remuneration Tax Act 2017” had so narrow coverage that income tax was imposed only on business profit and remuneration. Since this act could not cover all the sources of income, it was replaced by “Nepal ITA 2019” after 2 years to avoid such drawbacks. The coverage was extended through this act. The wide coverage divided the heads of income into nine parts: income from business, profession/occupation, remuneration, house and land rent, agriculture, investment, insurance business, agency business and other sources. After a year “Nepal Income Tax Rules 2020” were enacted with the view of implementing the objectives of the ITA. As “Nepal ITA 2019” was incapable in fulfilling the needs of the time, it was replaced by another ITA 2031.

“ITA, 2031” had 66 sections and classified the sources or heads of income into 5 headings (categories) namely (1) Agriculture, (2) Industry, Business, Profession or Vocation, (3) Remuneration, (4) House and Land Rent and (5) Other sources. The act has identified the chargeable incomes and admissible expenses for each head of income. The other features of this act were provision of carry forward of loss, provision of self assessment of tax, provision of fine, penalty and appeal, provision of tax deduction at source, provision of tax refund, provision of tax exemptions, provision of avoidance of double taxation etc. The government also issued “Income Tax Rules 2039” to implement the objectives of income tax effectively.

In the course of development and modernization of income tax system, the new “ITA 2058” has been enacted. Similarly, the new “Income Tax Rules 2059” have also been enacted for the effective implementation of the objectives of the Act. The new rules and regulations are effective from 2059-02-27(2002 June 10). This act has classified the head of income into three categories viz. employment, business and investment.

The following table exhibits the evolution of income tax laws in Nepal.

Table 2.1
Evolution of Income Tax in Nepal

S.N.	Income Tax Law	Effective from and to
1.	Finance Act, 2016(1959)	FY 2016/17 to FY 2017/18
2.	Business Profit and Remuneration Ordinance, 2016(1959)	FY 2016-4-25 to 2017-2-1
3.	Business Profit and Remuneration Act, 2017(1960)	2017-2-2 to 2019-4-9
4.	Nepal Income Tax Act, 2019(1962)	2019-4-9 to 2031-7-4
5.	Income Tax Act, 2031(1974)	2031-4-5 to 2058-12-18
6.	Income Tax Act, 2058(2002)	2058-12-19(2002 April) to date

Source : Newspapers and Websites

2.1.5 Income Tax Act 2058

To enhance revenue mobilization through effective revenue collection procedure for the economic development of the nation, and to amend and integrate the laws relating to income tax, the parliament of Nepal enacted ITA, 2002 A.D. (2058B.S.) since first April 2002 A.D.(19th Chaitra, 2058 B.S.). This act was enacted in Nepal to avoid the following defects of ITA, 2031.

- Narrow base of tax.
- Levying tax only on the income originated in Nepal.
- Dispersion of tax related acts, i.e. income tax related provision were in different acts.
- Low penalty rate to tax evader.
- Incompatible to self-assessment, and
- Unsuitable to modern economy.

The main objectives of ITA, 2058 are presented below:

- Bringing all income generating activities into tax net.
- Harmonizing tax rates and concessions on equity grounds.
- Widening the tax base.
- Confining all the income tax related matters within the act.
- Making income tax elastic and revenue productive.
- Developing a tax payer friendly taxation system by making it clear and transparent.
- Reducing the scope of discretionary interpretation of the tax authorities.
- Minimizing tax avoidance and tax evasion.
- Making taxpayers more responsible by enforcing the self assessment system.
- Integrating Nepalese tax system with the tax system of foreign countries.

The key Features of Income Tax Act, 2058 B.S.

ITA, 2058 has been enacted with wide a perspective. Various new concepts have been introduced in this act as compare to ITA, 2031. Many of the concepts have been put forward in this Act were not prevailing at Nepalese tax culture. This Act contains 143 sections. The key features of ITA, 2058 are:

- All income tax related matters are confined within Act by abolishing all tax related concessions, rebates and exemption provided by different Acts.
- The Act has broadened the tax base. Unlike previous tax Act, tax rates are spelled out in the Act. The tax rates and concessions are harmonized on equity ground.
- The Act has introduced a pool system of charging depreciation. Intangible assets are also depreciated.
- The Act has firstly introduced taxation on capital gains.
- The Act has provided liberal set-off and carry forward / backward provisions and inter head adjustments of losses are clearly specified.
- The Act has provided a stringent fine and penalty for the defaulters.
- The Act has introduced a provision for administrative reviews to allow the tax administration to correct mistakes made by tax administration internally.

- Global income of a resident are made taxable. Non-residents are also taxed on their income with source in Nepal.
- List of expenses is inclusive. All expenses relating to income have been made admissible.
- The Act has made provision of international taxation. Foreign tax credit has been introduced for the first time.
- The Act has separated administrative and judicial responsibilities by distinguishing civil liabilities of the tax payers from criminal liabilities.

2.1.6 Legal provision of Income Tax in Nepal

The function of revenue collection has remained one of the key activities of any government from ancient time in Nepal. At that time, taxes were levied on the merchants, travelers and farmers in the form of cash, kind or labor. In some occasion gold and agricultural products were also paid as taxes but the nature of these taxes were temporary and taxes were raised for special purposes.

In the Lichhavis regime, income taxes from agriculture income called “Bhaga” and business called “Kara” were introduced as a direct tax for the first time in Nepal. During the period of 1768-1846 A.D., different types of taxes were levied to generate maximum revenue. The major sources of revenue were: Birta and Kipat, taxes on land, monopolies, customs, transit and market duties, mines and mint and the export of forest products, birds and animals and various levies and fines. Taxes were collected at three levels: Royal palace levies, government levies and local levies. Various taxes at that period were imposed primarily on occupations and economic activities, not in income or property.

During the Rana regime, there was no any formal provision for imposition and collection of taxes. Taxes were imposed according to the objectives, needs and whims of the ruling prime minister. There was no system of preparing government budget. There was not provision of separating personal income of prime minister and treasury. The surplus of revenue over expenditure was considered as the personal income of the Rana prime minister.

The major sources of revenue in Nepal till 1951 were land tax, custom and excise duties in the form of lump sum contracts, royalties on supply of porters and soldiers, entertainment tax and few other minor taxes. Income were not taxed for raising regular revenue of the state treasury but for meeting specific expenditure of the household of extraordinary expenditure necessitated by war or other emergencies.

There was no direct tax in the country except land tax collected in a contractual basis and “salami” which the government employees used to pay out of their salaries at a very small percentage. The salami was abolished in 1951. The Rana rulers did not think of development of effective revenue administration system. After the advent of democracy in the country in 1951, no taxes are levied and collected in Nepal except in accordance with law.

2.1.7 Sources of Income

Income is the accretion of wealth or purchasing capacity of a person or entity. According to ITA, 2058 income is the term used to define income derived from employment, business and investment. It is the gross income less deduction allowed under the Act. This means, ITA, 2058 has specified sources of income into three heads.

1. Income from a business(section 7)
2. Income from employment(Section8)
3. Income from investment(Section 9)

Section 6 of the Act specifies that the assessable income includes earned from any country of the world in case of resident and income earned in Nepal in case of non-resident.

2.2 Income Tax Exemptions and Deductions

Man is regarded as capital, similar to a machine or a horse, which wears out and must recover in the product the value of that part of it which is worn out. A minimum standard of living should be free of taxation partly for humane reasons and partly because infringement on it will impair people’s capacity to work. The concept of exemptions and deductions is based on the concept of progressive taxation, which is a powerful tool to reduce the inequality of income and wealth. The provision of

exemption is basically for the number of taxpayers who are assumed to earn low income and have low capacity to pay. This will help policy makers to find out exact number of tax payer who can contribute to the nation. The deduction is generally granted to the taxpayer to encourage for further involvement in the work. In the deductions also the specific item wise deduction is for encouragement towards the work done. In many countries there is the provision of no tax (or very low tax) in the agricultural income. It is because of the countries' policy to increase agricultural activities and to develop agriculture sector. The concept of exemption and deduction helps a lot to narrow down the gap between the rich and the poor. The concept of the exemption and deduction is equally important in the industrial sector. The provision of exemption and deduction will help the nation to built stronger and powerful industrialized sector. The major significance of tax incentives however lies in their utilization as a means of promoting objectives associated with manufacturing activities. One such objective may be to encourage investment in selected manufacturing activities. One such objective may be to encourage investment in selected manufacturing activities of special economic of social worth.

In most of the countries there are both the provisions of exemptions and deductions. First they allow the exemption, then deduct the specified expense of the dependents and further provide the deductions on special items.

2.2.1 Exemption from Income Tax

ITA 2058, has clearly defined the amounts, which are exempt and other concessions. They are described in the following section.

1. Exempt Amounts

The following amounts are exempted from tax under section 10, ITA 2058:

- a. Amount derived by a person entitled to privileges under a bilateral or a multilateral treaty concluded between GON and foreign country or an international organizations.
- b. Amounts derived by an individual from employment in the public service of the government of foreign country provided that:

- The individual is a resident person solely by reason of performing the employment or is a non resident person and
 - The amounts are payable from the public funds of the country.
- c. Amounts derived from public fund of the foreign country by an individual who is not a citizen of Nepal as referred to paragraph (b) or by member of the immediate family of the individual.
 - d. Amounts derived by an individual who is not a citizen of Nepal from employment by GON on terms of tax exemption.
 - e. Allowances paid by GON to widows, elder citizens, or disabled individuals.
 - f. Amounts derived by way of gift, bequest, inheritance or scholarship (which are including exception of business employment or investment income).
 - g. Amounts derived by an exempt organization by way of
 - Gift, donation.
 - Other contributions that directly relate to the organization's function of the definition of exempt organization in section 2.
 - Amounts earned by Nepal Rastra Bank as its objectives.
 - h. Pension received by a Nepali citizen retired from the army or police service of a foreign country provided the amounts are payable from the public fund of that country.

In the above section, pension's amount received by Nepalese people being retired from the service by army or police of foreign country is exempted from income tax. It restricts the objective of raising more revenue of government because some of them receive more amount than the exemption limit approved by the government.

2.2.2 Expense not allowed for Deduction

To calculate the income of a persons' for an income year from any business, employment or investment, the following expenses are not allowed for deduction under section 21 of ITA 2058.

- Personal nature or domestic expenses.
- Income tax paid, fines and penalties.
- Expenses incurred for acquiring tax free income and final withholding payments.

- Cash payment in excess of Rs. 50,000 at a time by a person having annual transaction more than Rs. 20,00,000 (2 million) except in certain circumstances.
- Distribution of profits by an entity for example dividend distribution to the shareholders.
- Expenses not related to earning of income.
- Any reserve, provision or fund.
- Expenses of capital nature.
- Foreign income tax.
- Other expenditures not exempted as admissible.

A person whose annual turnover for an income year exceeds Rs. 20,00,000 is not allowed a deduction for a cash payment in excess of Rs. 50,000 incurred at once other than in the following conditions by the person during the year, if:

- Payment made to GON, a constitution body, a corporation owned by the GON, or a bank or financial institution,
- Payment is made to a farmer or producer producing primary agriculture products even in the case where the product is primary processed by the farmer himself,
- Payment is a retirement contribution or retirement, payment,
- Payment is made in an area where banking services are not available. An area not having banking services means the area where there are no banking facilities within the surrounding of ten kilometers.
- Payment is made and must necessarily be made in cash or on a day when banking services are closed.
- Payment is made into a bank account of the payee.

2.2.3 Deduction Allowed

ITA 2058 has provided the provisions relating to expenses, which are allowed for deduction and not allowed for deduction. They are discussed or analyzed in the following section:

1. General Deductions (Sec. 13)
2. Interest Expenses (Sec. 14)
3. Cost of Trading Stock (Sec. 15)

4. Repair and Improvement Costs (Sec. 16)
5. Pollution Control Costs (Sec. 17)
6. Research and Development Costs (Sec. 18)
7. Depreciation Expenses (Sec. 19)
8. Loss Recovery (Sec. 20)

2.3 Review of Related Studies

Brief review of different studies has been performed in this research study. The researchers has consulted many books, dissertations, articles, annual reports of different institutes, new magazines, published and unpublished materials concerning with income taxation during the period of thesis writing. They have studied about the various aspects relating to administrative problem, legal aspects and trends of income tax etc. These studies are useful in the field of income tax. Some of the books, articles and dissertation that are reviewed during this study are as follows:

2.3.1 Review of Books

While reviewing the books, it was found that most of the books were syllabus oriented and some of them had described the problems and prospects of income tax and path for reform of income tax. There were no detail studies made on the topic income tax exemptions and deductions. Nevertheless, some books are most important and relevant for the study, which are as follows:

Agrawal (1980) had written a book entitled “*Resources mobilization in Nepal.*” published by CEDA. The books had been divided into eight chapters; the first chapter deals with special reference to Nepal. The second chapter deals with fiscal policies in developing nation and Nepal and third chapter looks at income tax in Nepal from the historical perspective, the fourth chapter deals with structure of Nepalese taxation. In this chapter, writer had concluded the predominant role of indirect taxes in Nepalese tax structure. More than 60% of tax revenue was derived from foreign trade alone. However, the role of income tax had been increasing since 1974/75 A.D. Dr. Agrawal had made an empirical study taking tax policy makers, tax experts, tax administrator, tax lawyers, accountants and tax payers of different parts of Nepal. From the study, he had concluded that Nepalese tax payers were favorably disposed to income tax. However, the major constrains in the effective functioning of tax system seems to be

administrative deficiencies, poor taxpaying habits, lack of tax payer's education, complicated procedures and defective tax information system.

Poudyal and Timilsina (1990) had described the provisions and laws related to income taxation of Nepal in a book named "*Income tax in Nepal*". This book is extremely based on the syllabus of B.Com. They described the theoretical as well as practical aspects of income tax. He has not analyzed the role of income tax, income tax structure and defects of income tax in Nepal. The book was descriptive rather than analytical.

Prandhanga (1993) wrote a book entitled "*Income Tax laws and Accounting*". Mr. Prandhanga has described the provisions made under income tax laws. This book is divided into 20 chapters. In this book, Mr. Pradhananga has described about the income tax and its development in Nepal. He has also described about fines and penalties, appeal, contribution of income tax for the development of nation, income tax administration and official, collection and return of income tax and admissible and inadmissible expenses etc. He also included some numerical problems in regard to income tax assessment, but this book has not analyzed the importance of income tax, problems and defects in Nepalese ITA and importance of exemptions and deductions in income tax system of Nepal. This book has been written to fulfill the M.com and B.com course of T.U., especially this book is based on the syllabus of B.Com of T.U.

Khadka (2001) has published a book named "*Income Taxation in Nepal Retrospect and Prospect*". This book contains many interesting articles on various aspects of income tax. It first traces out the evolution of income tax around the world. It then analyzes relative importance of income tax in the tax system of some selected countries. It also defines various concepts, which are widely used in modern income tax literature. This book also reviews major changes introduced in the field of Nepalese income tax system since its inception in 1959 and examines its existing structure and operation. It also analyzes the current problems and makes recommendation for the rationalization of the structure and modernization of operation of income tax system.

Bhattarai and Koirala (2003) published a book named "*Income Taxation in Nepal with Tax Planning and VAT*." This book was published second, third, fourth, fifth,

sixth and seventh time in 2004, 2007, 2008, 2009, 2010 and 2011 respectively. This book has described the legal provisions with critical analysis. This book has theory and enough practical problems. Critical and comprehensive problems are given. This book also has added income tax act, 2058 (as amended by Finance ordinance, 2067), value added tax act 2052 (as amended by Finance Ordinance, 2067), an overview of Excise Act, 2058 (as amended by Finance ordinance, 2067) etc. This book has also described the tax planning. This book is very useful to know the new income tax act 2058 with tax planning and VAT but not described the role of income tax and income tax structure.

Amatya, et.al (2004) wrote a book entitled “*Taxation in Nepal*”. This book is also designed to meet the requirement of B.B.B third year syllabus. Theoretical as well as practical aspects of taxation have been included in the book. This book is a descriptive one, not analytical.

Khadka (2007) wrote a book entitled “*Modern Tax Administration in Nepal*”. This book is very much useful to anyone who is interested in Nepalese income taxation. This book gives almost complete information about the tax system of Nepal from its ancient time to current situation of income tax system. He has shared his expertise in his book. Basically, author focuses on the administrative aspect of the tax system in Nepal.

Kandel and Lamsal (2011) wrote a book entitled “*Tax laws and Tax planning in Nepal*”. This book has been written to fulfill the masters’, bachelors’ and chartered accountant course. This book has been organized into 18 chapters. In this book writers have described the process related to the income tax assessment and tax planning. They have also presented an overview of relevant income tax laws, ITA, 2058 and Value Added Tax, 2052. They have also included numerical problems in regard to income tax assessment. This book is informative and descriptive rather than analytical. It has not analyzed the importance of income tax, problems and defects of income tax system, importance of exemption and deductions and calculation of income tax from various sources.

2.3.2 Review of Articles\reports

Agrawal (1978) in his study of "*Resource Mobilization for Development: The Reform of Income Tax in Nepal*," presented to CEDA, T.U., described the different concepts of income tax. Agrawal described the resource mobilization through income tax, fiscal policy, role of income tax, legal provisions relating to income tax, legal aspects of income tax, administrative aspects of income tax etc. Agrawal identified the major problems in income tax system as inefficiency of tax administration and tax evasion. Agrawal observed that the tax authorities were insufficient in enforcement of law. There were no integrated programs for taxpayers' education, assistance, guidance and counseling. Tax offices were taken as heaven for corruption. Delays, unfair dealings, insufficiency, harassment and incompetent personnel were the major problems of tax administration.

About the exemption and deductions, Agrawal suggested to increase the exemption limit from the range of Rs. 8000 to Rs. 12000. On his study, the income tax exemption limit was Rs. 6500- for an individual, Rs. 7500 for a couple. Agrawal also suggested providing additional deductions to the salaried taxpayers for educational expenses, medical expenses and house rent and he was favoured for more progressive rates of income tax.

This study is very useful to find out the reality about the income tax in Nepal. This study was a comprehensive and included various aspects of tax system of that period. All things mentioned in it are not fully relevant today. But some of the problems identified in it are still in existence. Agrawal described various aspects of income tax but he did not describe business expenses. Agrawal did not conduct any research on business expenses as exempted income too.

Bhattarai (2050) critically analyzed the income tax facilities provided by Industrial Enterprises Act 2049 in his draft, "*Income Tax Facilities Provided by Industrial Enterprise Act 2049, an Analysis of Rajaswa*." Bhattarai described the facilities given to the industries. He also critically analyzed the facilities as continuous 7 / 8 years exemption of income tax would develop the tradition of taking exemption by incorporating legal ways. The deduction allowed on modernization of industries, pollution control device, product and technology development, sales promotion

expenses etc. would protect only the big industries but no effect to small industries. Provisions made on advertisement and entertainment or hospitality expenses would create rude on income tax because it is given to all industries in the same manner. There was provision of exemption of income tax of industries which did not get exemption but reinvested on non exempted industries. This provision exempts the tax to the industries of alcohol, tobacco etc. in an industry reinvested on non exempted industry. According to the study, periodic exemption of tax would create bad effects such as; change in sign board, change in name and change in ownership to own family members.

United Nations Organization (1997) published a journal on public finance entitled, “*Guidelines for improving tax administration in developing countries*”. The study was divided into four separate parts. Among them reforming the structural organization of the tax administration are explained in two separate sub topics i.e. guidelines for appropriate initiatives and underlying consideration and explanatory commentary. Functions of tax administration are identification and registration of tax payers, tax payer’s education, information provider and assistance etc. The study had detail explained their functions and recommended some valuable suggestion to the developing countries.

Kandel (2004) presented an article entitled, “*Are Tax Incentives Useful? If so, Which One?*” published in Journal of Finance and Development. In this article Kandel tried to seek the answer from the survey of various empirical studies earlier done in Nepal, India, Pakistan and other investment countries. Kandel found that tax incentives are still the controversial matter whether they promote the investment or not. But Kandel argued the most of the developed countries used tax incentives. As per the studies done in various countries, the conclusion is that among different types of tax incentives, investment allowance or investment tax credit and accelerated depreciation are superior to other types of tax incentives. Tax holiday is the most inferior type of tax incentive which causes revenue loss without enhancing the investment environment. Meanwhile most of the researchers have opposed the tax holiday system both with in Nepal and outside Nepal. Kandel further added the survey of studies indicate the accelerated depreciation system has positive impact on investment. The work of reducing tax rate specially followed after 1990s to such lowest rate was not a

proper decision. That's why if Nepal wants to go to tax incentives system again, investment allowance or investment tax credit, not the full holiday in future should be adopted in future.

Pant (2004) presented an article entitled, "*Problems in Tax Administration and their Remedies*" published in Journal of Finance and Development. Pant comprehensively explained about the problems and their remedies related with tax revenue. The major types of practical problems and challenges in tax administration he has mentioned in his article are; showing limited amount of transaction, showing low selling price, lack of issuing and taking bills, lack of showing the real factory cost, commercial fraud, lack of cooperation in tax auditing, legal ambiguity and complexity in implementation and lack of coordination between Inland Revenue Department and revenue investment unit. Meanwhile Pant has recommended some valuable suggestions to solve the problems and to overcome the challenges. They are, statistical and information system should be properly managed, fixed norms and standards should be used to assess selling price and factory cost, the billing system should be made compulsory, coordination between Inland Revenue Office with various entities, revenue investigation department and its related units should play the important role and auditing of tax should be widened etc.

Neupane (2007) had published an article in economic bulletin 'Rajaswa', "*Contribution of Income Tax to Total Tax Revenue*" which shows the contribution of income tax to total tax revenue, has decreased from 23.93% to 20.83% in the FY.056/057 to 061/62. It may be due to the collection of the property tax by municipalities. But it is not only the cause. Emphasis should be given to the income tax collection. To facilitate tax collection, Inland Revenue Department has implemented E-TDS, E-Pan and E-Filing for the better tax compliance. There is provision of tax plate also. But the frequent change in the act decreases tax compliance which is a major drawback on instable political condition.

New Business Age (2007) the new business published news about "*Tax Paying behaviour in Nepal and European Countries*". The news presented that 95% of taxpayer in European countries were willing to pay tax but in Nepal taxpayer want to hide the income and they did not pay tax as per rules and regulations.

Dhakal (2008) had written an article entitled “*Historical Perspective on Income Tax in Nepal*”. This article has describe previous income tax act and shown main fatigue of Income Tax Act, 2058 are as follows:-

- Provision of set and carry forward of losses.
- Classification and pooling of depreciable Assets.
- Tax on capital gain.
- International taxation.
- Medical tax credit
- Withholding payment and quantification allocation and characterization of the amounts.

Kandel (2009) criticized the “*ITA 2002 on several grounds*”. Exemption of agriculture income from income tax, export duties levied on export, inequality between different capital earned income (i.e. tax on interest, dividend and capital gain) and withdrawal of the provision of exemption suddenly and no adjustment for inflation are the major issue he raised in his article. He further criticized the act for the provision of income tax from export as 0.5% of total export because it is not good choice of income tax base. Lastly, he had recommended to mobilize additional domestic resources through taxation, tax structure should be redesigned in order to increase the role of direct tax; income tax should be reformed in Nepal etc.

2.3.3 Review of earlier studies

Regmi (1986) presented a dissertation entitled “*The Role of Income Tax in Nepal.*” Regmi described the conceptual framework of income tax, structure of income tax, income tax and resource mobilization, problems and income tax. Regmi has also described the objectives of income tax. Regmi has given more concentration on the study of tax structure of Nepal. In his study, Regmi found the share of indirect tax was more than 70 percent of total tax revenue in 1981/82. The share of direct tax was about 30 percent of total tax revenue. Within direct tax, the share of income tax was 17.29 percent in 1972/73 which was increased 35.68 percent in 1981/82.

Regmi found the problems of income tax, they were lack of maintaining the record of taxpayers, assessment delays, lack of responsibility and honesty among the tax

officers, tax evasion, corruption, lack of coordination between the various revenue and other non-revenue departments, leakage in personal income tax collection.

Regmi has given suggestions about the income tax were, income tax law should be clear and precise, widening the tax coverage, application of scientific assessment method, simple and easy procedure of tax payment, honest and efficient staffs, coordination between staff and departments, establishment of research unit, tax holidays to new industries. Although, Regmi did not mention the legal provisions relating to income tax. His topic was about the role of income tax but he did not describe any role of income tax, any numerical examples and mention the exemption and deduction.

Thapa (1993) conducted a research entitled "*Income Tax Assessment Procedure in Nepal, an Analytical Study*". This study was basically concentrated on income tax assessment procedure. Thapa conducted an opinion survey of income tax assessment procedure. Thapa took twenty three respondents as a sample. About the exemption limit, six persons were in positive attitude towards exemption limit, eight were in negative attitude and nine were different about the exemption limit. Out of them, those respondents who gave the negative response, suggested to increase the exemption limit. Thapa suggested adjusting exemption limit according to the inflation of the country. Thapa also suggested giving the tax holidays to new industries as investment allowance. Thapa did not mention the assessment procedure, legal provision relating to income tax and items of exemptions and deductions. His findings about the problems of income tax assessment procedure were as follows:

- Ad-hoc system in tax assessment.
- In tax assessment process, undue delay in tax assessment and lack of adequate accounting skills are considered at present.
- Adjustment of exemption limit to increase must be done.
- Tax holidays to new industries as investment allowance should be provided.

Tripathee (1995) presented a dissertation entitled "*Income Tax System in Nepal and some potential Areas for reforms,*". In this study, Tripathee tried to show the tax structure in Nepal, role of income tax in Nepalese economy, income tax administration and tax evasion in Nepal along with reforms.

Tripathee has more emphasized on the income tax administration and tax evasion. Tripathee conducted an opinion survey about the sufficiency of tax incentives and tax holidays to the industries. Tripathee took a sample of 26 respondents, out of them 16 respondents were in positive response and 10 respondents were in negative response about the sufficiency of tax incentives and holidays. According to the respondents following reformatory activities should be performed.

- The industries, who invest Rs. 500,000 or more, should be defined as employment oriented industries.
- There should be prize system, which may be as the form of tax incentives or tax holidays to the taxpayers.
- The period of tax holiday should be extended for industry, which utilized Nepalese raw materials and produces handicrafts. The period of tax holidays should be extended 10, 8 and 5 years instead of existing period of 7, 5 and 2 years respectively.
- For the expansion of industry, additional incentives should be provided.
- The items of deduction should be added.
- Tripathee suggested should to increase the exemption limit of Res. 25,000 to Rs. 30,000 for an individual, Rs. 35,000 to Rs. 40,000 fore a couple and Rs. 35,000 to Rs. 50,000 for a family

Tripathee's suggestions about deduction of expenses of remigration taxpayers were as follows:

- Expenses for better education of their children not exceeding the amount of Rs. 10,000 p.a.
- House rent allowances not exceeding Rs. 12,000 p.a.
- Educational expenses for taxpayers himself if he is studying in an educational institution.

His dissertation is very useful for further study about income tax purpose. But he did not include the exempted items of income and business expenses and also not mention about the legal provision relating to income tax.

Poudyal (1998) submitted the Ph.D. thesis entitled, “*Corporate Tax Planning in Nepal.*” This thesis report had aimed to examine the implication of tax factors in strategic planning, project planning and optional planning in Nepalese companies. Paudel found that the majority (90%) of the companies considered tax factors while

selecting the line of business. Paudel also found that the positive correlation (+0.8) between tax rate and the debt equity because of interest paid on debt is a tax deductible item. Similarly the correlation coefficient between averages fixed assets and corporate tax rate was (+0.75) in small companies and (+0.12) in medium size companies. As against this, in large companies, there was a negative correlation (-0.2), which showed that, increase the fixed assets in large companies resulted decrease in the corporate tax. Paudel addressed that the tax planning should be considered while making corporate planning and such companies should be set up separate tax system to get maximum benefits of provisions provided by tax law. However, tax assessment under the best judgement blocked the application of tax planning in corporate planning. Paudel has recommended the tax incentives should be given to non-industrial companies too and tax rate should be differentiated for resident and non-resident companies.

Kandel (2000) presented the Ph.D. thesis entitled, “*Corporate Tax System and Investment Behaviour in Nepal.*” He under took the research work to find out problems relating to corporate tax which blocks the development of the private investments. The main objectives and major findings of his study were as follows:

Objectives:

- To evaluate the corporate tax system in general to examine the sensitivity of certain policy like inflation, capital gain tax, dividend tax and interest tax etc. based on their impact on tax burden.
- To know the relationship of private investment with average effective tax rate (AETR), marginal effective tax rate (METR) and tax incentives in Nepal.

The major findings:

- The METR for debt financed projects are almost negative (i.e. -17%) and positive for equity financed projects and debt equity ratio project by 27% and 19% respectively.
- The statutory tax rate deduction has impact on private investments by 60% and 20%. In his regard, he showed the adjusted R2 value 0.87 at 5% level of significance.
- Kandel concluded that the statutory tax rate was in moderate level under the financing options; debt mix and equity i.e. it was not much distortive.

- The relationship between inflation rate and effective tax burden in Nepal was negative.

Khatiwada (2004) conducted a research entitled, “*Structure of Income Tax System in Nepal, A Managerial Study*”. T.U. Khatiwada aimed to evaluate the structure of income tax system and managerial study. Khatiwada accepted that ITA, 2058 and Provisions are difficult to understand, language is vague and unclear, narrow base i.e. agricultural income has not been included in tax net, provision of double taxation in dividend, insufficient provisions related to capital gains.

Khatiwada also analyzed that income tax management system in Nepal is not effective and efficient due to ineffective management system, inadequate government policy and defective income tax laws. Khatiwada also mentioned the major constraints of effective and efficient income tax management system as:

- Misuse of power by tax administrators.
- Less consciousness of tax payers.
- Lack of motivated and trained human resources.
- Inadequate experts in tax management, non-maintenance of books and accounts, time consuming process of income assessment i.e. scientific assessment.

Khatiwada also added income tax assessment procedure is not sound and efficient, high level of evasion found in income tax, income tax administration as a high degree of corruption has been found. But he did not mention any provision about exemption of incomes and deduction of expenses in Nepal.

Niroula (2005) did a research study named, "*Study of Incentives and Facilities to Industries under Income Tax Act. 2058*". This study was aimed to examine and analyze the effectiveness of tax incentives and facilities to industries. Niroula concluded that;

- Income tax incentives and facilities do not play the major role in the establishment of industries but other factors such as political stability, industrial environment, administrative efficiency and availability of market, raw material, labour, infrastructure etc play key role in the establishment of

industries. If these facilities are available the incentives and facilities provided by the ITA might play major role in the establishment of industries.

- Investment tax credit and investment allowance play vital role in the establishment of new industries.
- A flat rate of 20% income tax to all industries seems to be little bit higher to the small industries.
- The deduction facility of PCC and R & D has tremendous effect to achieve its objectives and industries are exploiting these facilities.
- Tax rebate of 25% and 30% to the undeveloped and underdeveloped areas are not sufficient.

Niroula has recommended that investment tax credit and investment allowance should be provided to new industries. The rate of 20% to the export industry is higher and it should be minimized. Niroula further recommended that the contradiction between the Income Tax Act and Industrial Enterprises Act should be eliminated. Niroula further conducted from time to time to make aware about the tax incentives and facilities to current taxpayers and potential investors.

Bhandari (2006) submitted a dissertation named, *“Taxation Knowledge of Taxpayer in Nepal.”* He had pointed out the present position of taxation knowledge of taxpayers in Nepal. Tax payers don’t know about the rapidly changing government policy, rules and regulations etc. are the main problems of the study. Similarly he suggested to the government by following ways:

- To increase the income tax knowledge of tax payers, for that tax related information should be published regularly.
- Special taxpayer education program is necessary for employees and small taxpayers which help to increase the government revenue of the country.
- The school as well as campus level curriculum should include tax related education so that tax payer education program can be more effective.

Dotel (2007) presented a dissertation named *“Income Tax Act 2058; Expectations and Realities”* in 2007. The objectives of the study was to measure the effectiveness of Income Tax Act 2058 both in theory and practice, to review the views of taxpayers, tax experts and tax administrators to ITA 2058. He found that Income Tax Act 2058

seems effective because it has the features of provisions of international taxation, taxing capital gains and dividends income, abolition of various tax related concessions, rebate and exemption etc. He also found that the most of taxpayers, tax administrators and tax experts are acquainted to present Income Tax Act. However they suggest that some of the words in the act needed to be further simplified.

Ojha (2009) wrote a thesis entitled “*A Study of Income Tax structure of Nepal*”. He had analyzed income tax structure, problem of resource mobilization and resource gap in Nepal along with identification of share and trend of corporate income tax on government revenue of Nepal. He had found that there was dominated share of tax structure in Nepalese government revenue. Moreover he suggests that the contribution of income tax to the national budget must be increased to achieve the goal of national development and equal economic distribution. He also found the GON lagging behind in making the income tax management/administration efficient.

Chalise (2010) presented the thesis entitled, “*A study of Income tax Exemptions and Deductions in Nepal*” He undertook the research work to find out problems relating to income tax exemptions and deductions and to collect the view of tax expert, tax officer and tax payer about it.

The major findings of the thesis were:

- All incomes generated by an individual are not taxable income. Because the minimum cost expenses required for living can not be taxed. So, from the commencement of income tax in Nepal, some extent of amounts are exempted from income tax. This extent is known as exemption limit. Income tax exemption limit in Nepal has been changing on the basis of time and condition. From the empirical studies, respondents have suggested to change exemption limit according to the inflationary situation of the country. In 2007/08, the exemption limit provided for an individual and for a family or couple were Rs. 115,000 and Rs. 140,000 and in 2008/09, that limit providing Rs. 160,000 and Rs. 200,000 respectively. The exemption limit is not provided to partnership firms, corporations and non-residents. From the view of respondents, most respondents suggested to increase exemption limit for

individual and for a family or couple were Rs. 200,000 and Rs. 250,000 respectively.

- The family exemption limit must not be provided according to the number of dependent.
- The itemized deductions are not sufficient.

Adhikari (2011) conduct a study entitled “*A Study on corporation Income Tax in Nepal*”.

The objectives of this study were:

- To study and evaluate the status of income tax as major source of revenue.
- To examine the Nepalese income tax structure.
- To review and analyze the trend of income tax collection and tax revenue.
- To identify the factors to increase tax paying habit of income tax payer.

Major findings were:

- The share of tax revenue has always been greater than the share of non tax revenue. Similarly,
- The contribution of indirect tax has been always greater than direct tax revenue during the study period from 2000/01 to 2010/11.
- Income tax is an important source of direct tax.
- Its structure of Nepal is the composition of tax from government sector, public sector, private corporate bodies and remuneration on tax.

Pandey (2012) presented the thesis entitled, “*Exemptions, Deductions and Self Assessment of Income Tax System in Nepal*”. The major objectives of the research were to find out the problems faced by the taxpayers, test the level of understanding of taxpayers and to analyze the exemptions of income and deductions of expenses provided by ITA, 2058 and to measure the extent of exemption limit provided to individual and family and their appropriateness. His major findings were:

- Public awareness programmes are necessary in Nepal for making people well informed about income tax system. In total 88.3333% of the total respondent believed that people are not well informed about income tax system in Nepal.
- Major problem faced by the tax payer while paying income tax among various problems was time consuming process.
- The current income tax exemption limit should be increased to Rs. 2,00,000 and Rs. 3,50,000 for an individual and a couple or a family respectively.
- The exemption limit should be adjusted according to the inflationary situation of the country.
- Agricultural income should be exempted from tax.
- Itemized deductible expenses are insufficient.

2.4 Research Gap

During the research study, the researcher viewed various books, reports, articles and dissertations and thesis. Most of the researchers are concerned on the legal and assessment procedure of income tax, administrative and historical aspect of income tax. The thesis and dissertations presented by the researcher have focused about the trend of income tax collection and buoyancy of income tax with GDP, inefficiency of tax administration, widespread of tax evasion, value added tax, role of income tax, income tax system in Nepal, problems and prospects of income tax in Nepal, corporate tax planning in Nepal, income tax collection from commercial banks etc. There is a limited number of research studies carried out specifying tax payer groups and concentrated on exemptions and deductions of income tax. No attention is paid on a particular problem like exemption of incomes and deduction of expenses. Most of them have been taken various problems as their research objectives and no thoroughly study on a particular subject problem. The researcher has found that no more study done in exemption of incomes and deduction of expenses. This study will help to know the provisions of exemptions and deductions provided by ITA, 2058 and getting optimum benefits within the frame of ITA by exempting of incomes and deducting of expenses to the taxpayers. The solution of the necessary problems in this study has been taken analytically and intensively from the IRD and other sources in Nepal. This study will be fulfilling to those interested persons, students, teachers, scholars, taxpayers etc. for academically as well as policy perspectives.

CHAPTER-III

RESEARCH METHODOLOGY

3.1 Introduction

Research methodology is a research method used to meet the specified objectives. It is a systematic way to find out the probable solution. It refers to the various sequential steps (along with rationale of each step) to be adopted by a researcher in studying the problem with certain objectives in view. Thus the research method designed to achieve the objectives of this thesis contained research design, population and sample, data collection procedure, tools for analysis and methods of analysis and presentations.

3.2 Research Design

The research design is a plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance. The plan is the overall scheme or program of the research. It includes an outline of what the investigator will do from writing the hypothesis and their operational implications to the final analysis of the data. The purpose of the research design is to provide a maximum amount of information relevant to the problem under investigation at a minimum cost.

This research study is concerned with past phenomena both numerical as well as opinions. This study is both descriptive and analytical.

3.3 Population and Sample

The population for this study was comprised of the entire person belonging to or associated with Income Tax in Nepal. They are Income Tax administrators, Experts and Income Tax Payers. In order to fulfill the objectives of the study, 80 samples from the population in the Katmandu Valley were carefully selected by consultation with lecturers and best judgment of the researcher. The respondents could be divided into three groups. The following Table shows the groups of respondents and the size of samples.

Table 3.1
Group of Respondents and Size of samples

S.N	Group of respondents	Sample Size
1	Income Tax Experts	20
2	Income Tax Administrators	30
3	Income Tax Payers	30
Total		80

Source : As per research design, 2013.

3.4 Nature and Sources of Data

Both primary as well as secondary data were collected in order to achieve the real and factual result out of this research. Since the nature of these primary and secondary data is different, collection procedure also tend to vary. A set of questionnaires was designed and distributed to the selected respondents well-learned in and at least familiar to Income Tax and its implications. Information and data were also collected from respondent through field visit by the researcher. The secondary data were collected through annual reports, different books and publications. The sources and data collection procedure is explained below.

- I. Primary data collection.
- II. Secondary data collection

Primary Data

The primary data will be collected through following techniques:

- a. Interview
- b. Questionnaire
- c. Telephone queries
- d. Discussion with resource persons
- e. Field Survey

For collection of primary data and information focus was given on distributing questionnaires to the sample population and analyzing their views. The questionnaires were distributed to different respondents. Tax administrators are selected from department and various sector of tax offices. Tax experts are the faculties having experience of tax management, auditors, chartered accountants etc. Taxpayers are

selected from various sector i.e. finance company, bank, insurance company, private company etc.

Secondary Data

The secondary data of this research were collected from the following sources:

- a. Published and unpublished reports, articles and dissertations on the concerned subject.
- b. Published documents of Nepal Planning Commission.
- c. Publication and annual report of Inland Revenue Department (IRD).
- d. Publications of Nepal Rastra Bank.
- e. Various books written by tax officers and scholars.
- f. Publications, Budgets Speeches and Economic Survey of various fiscal years.
- g. Newspaper, such as, Gorkhapatra, The Rising Nepal, Kantipur Daily etc.
- h. Publications of various VAT Departments.
- i. Websites.

3.5 Data Collection Procedure

In this study data and information was collected both from primary as well as secondary sources. To get the accurate and actual information in time, all questionnaires were distributed and collected personally through field visits. For secondary data information were collected from published reports.

Each sample was selected in such way that it represents a group of industry opinions.

3.6 Data Analysis Techniques

In the process of presentation and analysis of the data, various statistical tools were used in order to get the meaningful result. Collected data from primary and secondary sources were first processed for tabulation and analysis. For the purpose of analysis, following simple statistical tools were used:

- a. Simple Average,
- b. Weighted Mean,
- c. Simple Percentage,
- d. Graphs, Charts and Diagrams.

CHAPTER -IV

DATA PRESENTATION AND ANALYSIS

The presentation of the data is the basic organization and classification, which are then used for analysis purpose. Here, researcher shows the found impression formally at related area or ceremony. Analysis is a method of studying specific content and analyzing communication materials in a systematic, objective and quantitative manner to measure variables.

This is the major part of the study. Data presentation and analysis of income tax exemptions and deductions has been done in this chapter. It aims to make the clear understanding of income tax exemptions and deductions and to analyze the views of the tax experts, tax officers and tax payers about the exemptions and deductions facilities which are presented in this chapter.

4.1 Tax Structure of Nepal

Modern economic development of Nepal was started with the initiation of first economic planning in 1956 A.D. Since then, taxes have been used for the achievement of national economic goals. So, taxes play vital role for the economic development of Nepal. Tax structure should be known to study about the taxes. Tax structure refers to the level as well as relative importance of various taxes in the composition of total tax revenue of a country. Tax structure of any country is composed of both direct and indirect taxes. Total tax structure of Nepal from the fiscal year 2001\02 to 2010\11 is presented below.

4.1.1 Composition of Total Revenue

Total Revenue of Nepal consists of both tax revenue and non tax revenue since the presentation of first national budget in 1951/52 by GON.

Table 4.1 shows the composition of total revenue of government, which includes tax and non tax revenue from FY. 2001/02 to 2010/11. It seems that the share of tax revenue has always been greater than the share of non tax revenue. In FY. 2001/02 share of tax and non tax revenue is 77.96 % and 22.04 % respectively, however it is

86.47 % and 13.53 % in FY. 2010\11. It indicates that tax revenue has been placed as major source of government revenue of Nepal.

The composition of total revenue from FY. 2001\02 to 2010\11 is given below:

Table 4.1
Composition of Total Revenue

(Rs. in Million)

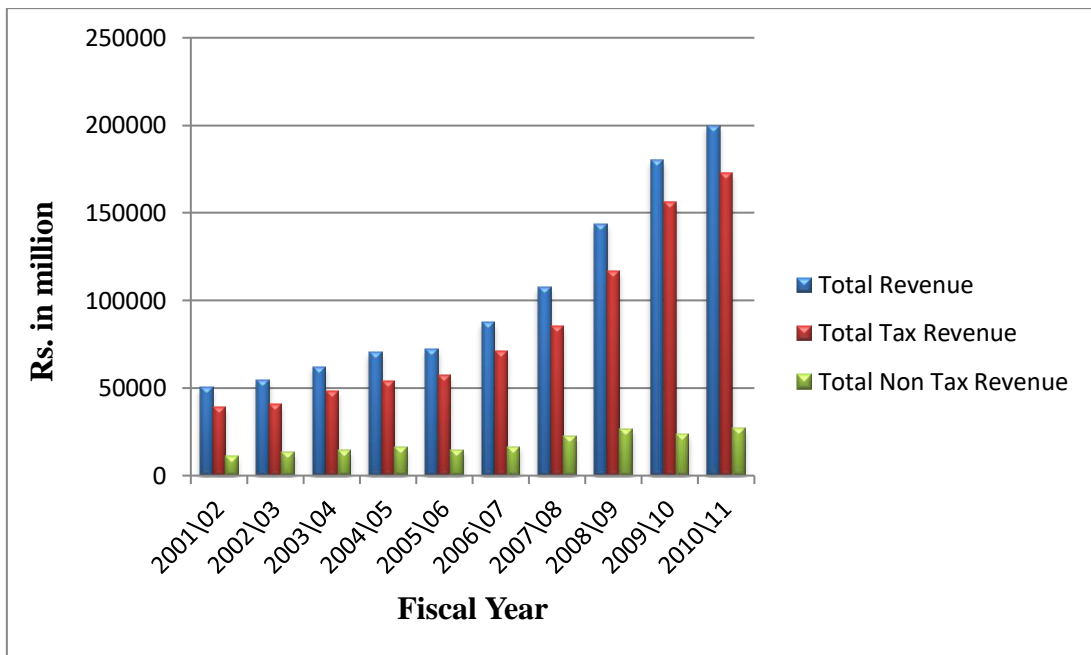
Fiscal year	Total Revenue	Tax Revenue		Non Tax Revenue	
		Amount	As % of total revenue	Amount	As % of total revenue
2001\02	50446.6	39330.6	77.96	11116	22.04
2002\03	54538.9	40896	74.99	13642.9	25.01
2003\04	62331	48173	77.29	14158	22.71
2004\05	70122.7	54104.7	77.16	16018	22.84
2005\06	72281.9	57430.4	79.45	14851.5	20.55
2006\07	87712.1	71126.7	81.09	16585.4	18.91
2007\08	107622.5	85155.5	79.12	22467	20.88
2008\09	143474.5	117051.9	81.58	26422.6	18.42
2009\10	179945.8	156294.9	86.86	23650.9	13.14
2010\11	199818.9	172777.8	86.47	27041.1	13.53
Total	1028294.9	842341.5	801.97	185953.4	198.03
Average	102829.49	84234.15	80.197	18595.34	19.803

Source: Economic Survey 2012\13.

From the table 4.1, it can be concluded that the source of tax revenue on total revenue is fluctuating from 74.99 % to 86.86 %. From the study, total tax revenue, total non tax revenue and total revenue were Rs. 842341.5, Rs. 185953.4 and Rs. 1028294.9 million respectively whereas average percentage of collected tax revenue and non tax

revenue were 80.197 % and 19.803 % respectively during the fiscal year from 2001\02 to 2010\11 A.D. period. So the tax revenue contributes about four fifth of total revenue. This also indicates that the tax revenue plays the significance role in total revenue. The composition of total revenue is shown graphically (in bar diagram) as follows

**Figure 4.1
Composition of Total Revenue**



4.1.2 Composition of Tax Revenue

Tax revenue is the sum of direct tax and indirect tax. The tax on consumption is known as indirect tax whereas tax on income and capital is known as direct tax. Further VAT, custom, sales tax, hotel, entertainment, other services tax, excise duty, contract tax etc. are sources of indirect tax and the sources of direct taxes are income tax, house rent, vehicle, land registration fees etc. So that the distribution of total tax revenue as the sum of direct and indirect taxes is tabulated below:

Table 4.2
Contribution of Direct and Indirect Tax to Total Tax Revenue
(Rs. in Million)

Fiscal year	Total tax revenue	Total direct tax		Total non direct tax	
		Amount	As % of total tax revenue	Amount	As % of total tax revenue
2001\02	39330.6	10597.5	26.94	28733.1	73.06
2002\03	40896	10881.9	26.61	30014.1	73.39
2003\04	48173	11912.6	24.73	36260.4	76.27
2004\05	54104.7	13071.8	24.16	41032.9	75.84
2005\06	57430.4	13968.1	24.32	43462.3	75.68
2006\07	71126.7	18980.3	26.69	52146.4	73.31
2007\08	85155.5	23087.7	27.11	62067.8	72.89
2008\09	117051.9	34320.7	29.32	82731.2	70.68
2009\10	156294.9	41750	26.71	114544.9	73.29
2010\11	172777.8	48655.2	28.16	124122.6	71.84
Total	842341.5	227225.8	264.75	615115.7	735.25
Average	84234.15	22722.58	26.475	61511.57	73.525

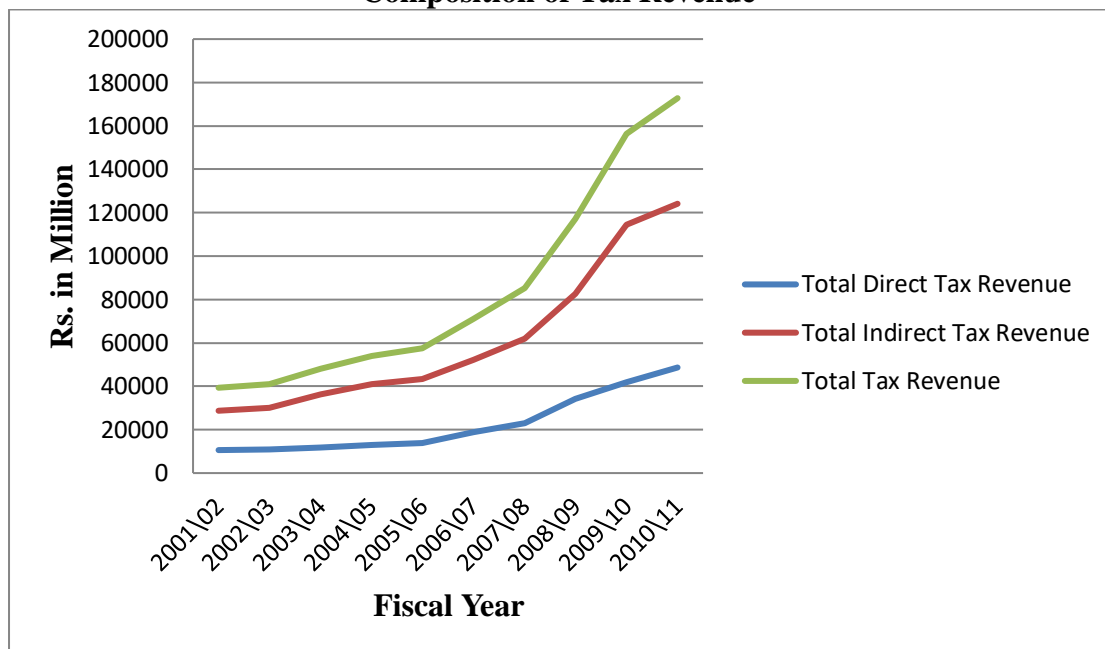
Source: Economic Survey 2012\13.

There has been simultaneous increase in direct tax, indirect tax and the total tax revenue in absolute term. In 2001\02, the amount were Rs. 10597.5 million, Rs. 28733.1 million and Rs. 39330.6 million respectively and during the period of 10 years, these amount became Rs. 48655.2 million, Rs. 124122.6 million and Rs. 172777.8 million respectively. The basic reasons for the increment were due to the expansion of the tax base and tax rates both wide and deep.

The total share of direct tax has increased from 26.94 % amounting to Rs. 10597.5 million in 2001\02 to 28.16 % amounting to Rs. 48655.2 million in 2010\11. The contribution of indirect tax in 2001\02 was 73.06 % amounting to Rs. 28733.1 million and decreased to 71.84 % amounting to Rs. 124122.6 million in 2010\11. The average collection of tax revenue, direct tax and indirect tax were Rs. 84234.12, Rs. 22722.58 and Rs. 61511.57 respectively and average direct tax and indirect tax on total tax revenue were 26.475 % and 73.525 % respectively during the study periods. From the

table 4.2 it can be concluded that there is greatest reliance on indirect tax making our tax system regressive in nature and it needs to shift towards direct tax.

**Figure 4.2
Composition of Tax Revenue**



4.1.3 Contribution of various Taxes as percent to GDP

The contribution of total revenue on GDP has increased from 11 percent to 14.53 percent as compared to 2001\02 and 2010\11. The contribution of tax revenue on GDP is increasing satisfactorily. In 2001\02, the share of tax revenue on GDP was only 8.6 percent, which was increased to 12.56 percent in 2010\11. Within the tax revenue there is significant role of indirect tax which contributes about three fold more than the indirect tax. In 2001\02, the contribution of indirect tax and direct tax was 6.28 percent and 2.61 percent respectively which were increased to 9.03 percent and 3.54 percent in 2010\11.

The contribution of income tax on GDP is increasing gradually. It contributed 1.94 percent in 2001\02 which was increased to 2.83 percent in 2010\11. The contribution of land tax and land and building registration tax was 0.25 percent and 0.26 percent in 2001\02 and 2010\11 respectively which is in fluctuating trend. It is decreased to 0.12 percent in 2002\03 and has started to increase and reached 0.53 percent in 2008\09 and again decreased to 0.46 percent in 2009\10.

Within the indirect tax, there is contribution of custom duty, excise duty and VAT. The custom duty is composed of import and export duties which have contributed 2.76 percent in 2001\02 and 2.60 percent in 2010\11. The contribution of VAT is in increasing trend. It has contributed 2.68 percent in 2001\02 which has increased to 4.48 in 2010\11. VAT as a substitute of sales tax, contract tax, entertainment tax, hotel tax is increasing in recent year. The contribution of excise duty was 0.83 percent in 2001\02 which was increased to 1.93 percent in 2010\11. The contribution of various taxes to GDP is given in the following table 4.3

Table 4.3
Contribution of various Taxes as percent to GDP

Year	Total Revenue	Tax Revenue	Direct Tax	Indirect Tax	Income Tax	Custom duties	Excise duties	VAT	Land Tax and House and land registration Tax
2001\02	11	8.6	2.61	6.28	1.94	2.76	0.83	2.68	0.25
2002\03	11.08	8.3	2.21	6.10	1.97	2.60	0.77	2.73	0.12
2003\04	11.61	8.97	2.22	6.76	1.72	2.90	1.16	2.70	0.32
2004\05	11.90	9.18	2.22	6.96	1.72	2.66	1.09	3.20	0.31
2005\06	11.05	8.78	2.14	6.64	1.59	2.35	0.99	3.30	0.33
2006\07	12.05	9.77	2.61	7.16	2.07	2.30	1.28	3.59	0.30
2007\08	13.19	10.44	2.83	7.61	2.12	2.58	1.37	3.66	0.36
2008\09	14.52	11.84	3.47	8.37	2.54	2.71	1.64	4.02	0.53
2009\10	15.09	13.10	3.50	9.60	2.62	2.95	2.04	4.60	0.46
2010\11	14.53	12.56	3.54	9.03	2.83	2.60	1.93	4.48	0.26

Source: Economic Survey 2012\13.

4.1.4 Composition of Indirect Tax

Indirect tax is imposed on one person but paid partly or wholly by another person. So, impact and the incidence are on different person. Nepal depends heavily on the indirect tax rather than direct tax because there is not any good alternative especially for the optimum level of revenue mobilization on one hand and on the other hand for the solution of wide spread poverty, heavy depending agriculture, snail's pace industrialization, low level of income and very weak administration. Since 1951,

indirect tax had grown rapidly and speedily. Most of the developing countries mobilized it effectively and properly of the domestic resources.

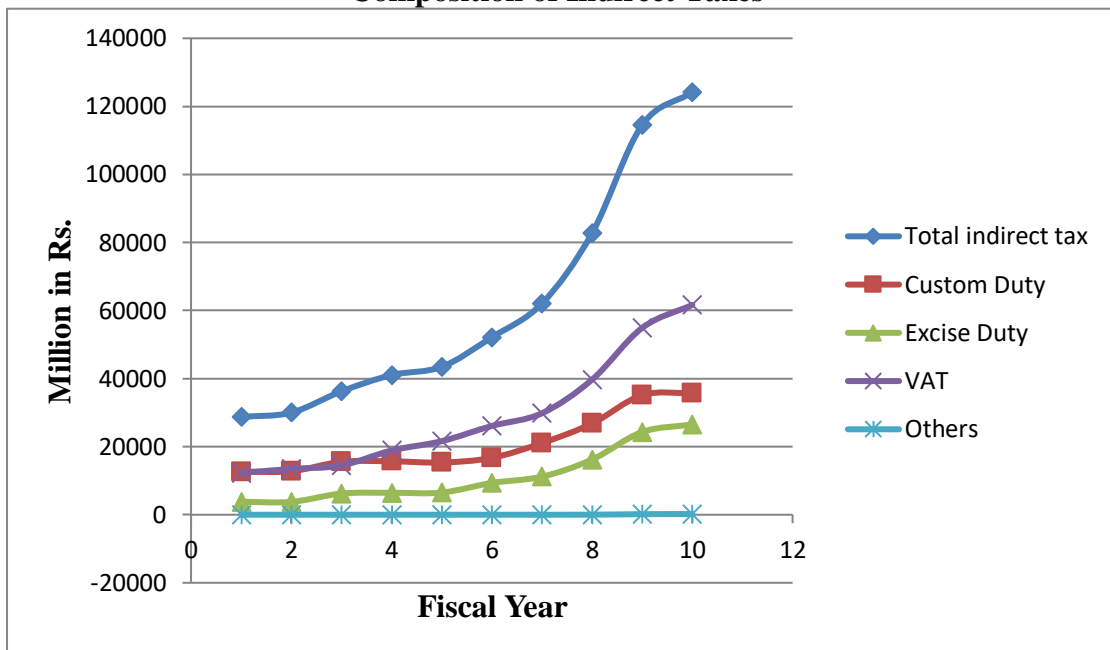
The major components of indirect tax in Nepalese tax structure are custom duty, excise duty, VAT or sales tax etc and the other components of indirect tax like entertainment tax, hotel tax, contract tax, sales tax, air tax are included in VAT and have nominal contribution on tax revenue. The compositions of indirect taxes are given in the table 4.4 and figure 4.3

Table 4.4
Major Sources of Indirect Tax and Their Relative Percentage of Indirect Taxes
Figure in million Rs.

Fiscal Year	Indirect Tax	Custom duty		Excise duty		VAT		Others	
		Amount (Rs)	percentage	Amount (Rs.)	percentage	Amount (Rs.)	percentage	Amount (Rs.)	percentage
2001\02	28733.1	12658.8	44.03	3807	13.25	12267.3	42.72	–	–
2002\03	30014.1	12783.2	42.59	3771.2	12.56	13459.7	44.85	–	–
2003\04	36260.4	15554.8	42.90	6226.7	17.17	14478.9	39.93	–	–
2004\05	41032.9	15701.6	38.27	6445.9	15.71	18885.4	46.02	–	–
2005\06	43462.3	15344	35.30	6507.6	14.97	21610.7	49.73	–	–
2006\07	52146.4	16707.6	32.04	9343.2	17.92	26095.6	50.04	–	–
2007\08	62067.8	21062.5	33.93	11189.6	18.03	29815.7	48.04	–	–
2008\09	82731.2	26792.9	32.39	16220.9	19.61	39700.9	47.98	16.5	0.02
2009\10	114544.9	35150.8	30.69	24306.1	21.22	54920.9	47.95	167.1	0.14
2010\11	124122.6	35711.6	28.77	26542.9	21.38	61663.6	49.68	204.5	0.17
Total	615115.7	207467.8	360.91	114361.1	171.82	292898.7	466.94	388.1	0.33
Average	61511.57	20746.78	36.091	11436.11	17.182	29289.87	46.694	38.81	0.033

Source: Economic Survey 2012\13.

Figure 4.3
Composition of Indirect Taxes



The custom duty and VAT occupies major portion in indirect tax. The total indirect tax revenue collected in 2001\02 is Rs. 28733.1 million of which Rs. 12658.8 million i.e. 44.03 % is contributed by custom duty, Rs. 3807 million i.e. 13.25 is covered by excise duty and Rs. 12267.3 million i.e. 42.72 % is covered by VAT. The share of custom duty is continuously decreasing from 44.03 % in 2001\02 to 32.04 % in 2006\07 and then increased to 33.93 % in 2007\08 and again decreased continuously to 28.77 % in 2010\11. The contribution of VAT seems to be fluctuating in different years. The amount of VAT collected in the year 2001\02 was Rs. 12267.3 million i.e. 42.72 % which increased to Rs. 61663.6 million i.e. 49.68 % in 2010\11. The collection of VAT was maximum in 2006\07 i.e. 50.04 % which is the highest percentage of VAT collection during the study period. Such a pattern of VAT collection indicates improving consumption pattern of Nepalese market. The share of excise duty is fluctuating till 2005\06 and then it is in increasing trend. It is Rs. 3807 million in i.e. 13.25 % in 2001\02, Rs. 6226.7 million i.e. 17.17 % in 2003\04, Rs. 6507.6 million i.e. 14.97 % in 2005\06 and Rs. 26542.9 million in 2010\11 i.e. 21.38 %. There is also a contribution of indirect taxes other than Vat, Custom and Excise duty from the year 2008\09. It has contributed Rs. 16.5 million i.e. 0.02 % in 2008\09, Rs. 167.1 million i.e. 0.14 % and Rs. 204.5 million i.e. 0.17 % in the year 2010\11. Total collection of indirect taxes has increased.

4.1.5 Composition of Direct Tax

In Nepal, the major components of direct taxes are income tax, land tax, house and land registration tax and tax on properties. Until the fiscal year 1993\94 vehicle tax was considered as a direct tax and since the fiscal year 1994\95 budget speech, it has been classified under the indirect tax. On the other hand, interest tax and urban house and land rent tax were included under the income tax since the fiscal year 1994\95. Thus the contribution of income tax has become larger than other taxes. The share of the major components of the direct tax can be more classified from the table 4.5 below:

Table 4.5
Composition of Direct Tax

(Rs. in millions)

Fiscal year	Direct Tax	Income Tax	As % of DT	Land Tax	As % of DT	House and Land Registration	As % of DT	Tax on property	As % of DT	others	As % of DT
2001\02	10597.5	8903.7	84.02	0.8	0.01	1131	10.67	562	5.28	-	-
2002\03	10881.9	9675.8	88.92	-	-	607.8	5.59	432.5	3.97	165.8	1.52
2003\04	11912.6	9245.9	77.61	-	-	1697.5	14.25	700.6	5.88	268.6	2.26
2004\05	13071.8	10159.4	77.72	-	-	1799.2	13.76	806.5	6.17	306.7	2.35
2005\06	13968.1	10373.7	74.27	-	-	2181.1	15.61	847.6	6.07	565.7	4.05
2006\07	18980.3	15034	79.21	-	-	2253.5	11.87	995	5.24	697.8	3.68
2007\08	23087.7	17311.2	74.98	-	-	2940.7	12.74	1069.2	4.63	1766.6	7.65
2008\09	34320.7	25142.4	73.26	-	-	5223.3	15.22	1850	5.39	2105	6.13
2009\10	41750	31285.6	74.94	-	-	5511.1	13.20	2417.9	5.79	2535.4	6.07
2010\11	48655.2	38868.5	79.89	-	-	3572.5	7.34	3022.6	6.21	3191.6	6.56
Total	227225.8	176000.2	783.82	0.8	0.01	26917.7	120.2	12703.9	54.65	11603.2	40.27
Average	22722.58	17600.02	78.382	0.08	0.001	2691.77	12.02	1270.39	5.465	1160.32	4.027

Source: Economic Survey 2012\13.

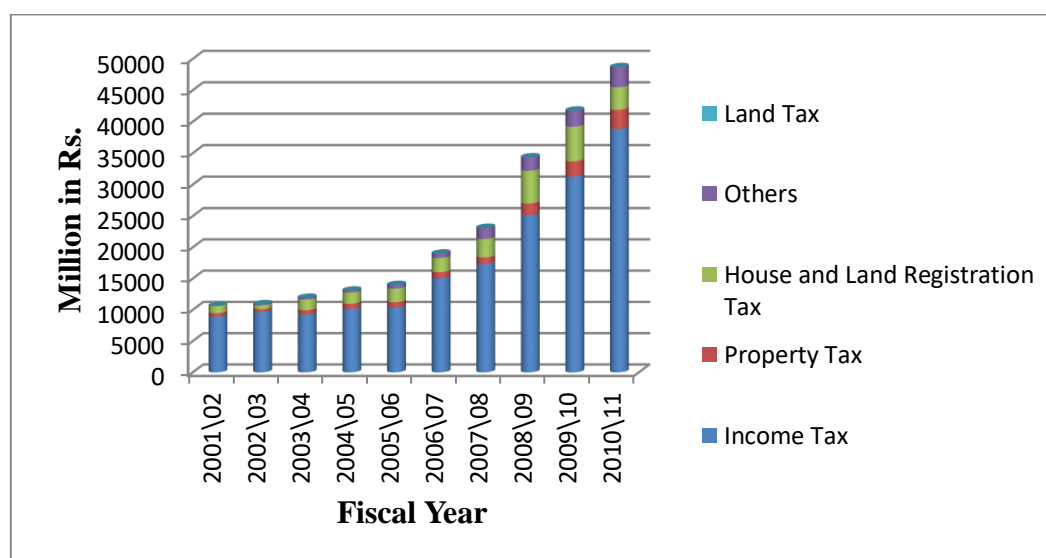
(Provision: Due to reclassification of the heading of revenue amount some tax heading do not match with previous data.)

From the study of direct tax of ten years, we can see that income tax has occupied the largest share in the direct tax. The contribution of income tax was Rs. 8903.7 million

i.e. 84.02 % in 2001\02 and Rs. 38868.5 million i.e. 79.89 % in the year 2010\11. The collection of income tax was in fluctuating trend during the study period. Collection from land tax was Rs. 0.8 million (0.01%) in 2001\02 and then gone zero up to 2010\11. During the research period the contribution of house and land registration tax was Rs.1131 million i.e. 10.67 % in the year 2001\02 which has decreased to 7.34 % in the year 2010\11 i.e. Rs. 3572.5 million. Contribution of property tax has been increased from 5.30 % in 2001\02 to 6.21 % in 2010\11. Other sources of direct tax has significantly contributed to the sources of direct tax i.e. Rs.165.8 million in 2001\02 to Rs. 3161.6 million in 2010\11. The total collection of income tax, land tax, house and land registration tax and other tax were Rs. 176000.2 million, Rs. 0.8 million, Rs. 26917.7 million, Rs. 12703.9 million and Rs. 11603.2 million respectively, in which average collection on direct tax were 78.382, 0.001, 12.025, 5.465 and 4.027 percent respectively.

The composition of direct tax can also be shown from following figure:

Figure 4.4
Composition of Direct Tax



4.1.6 Contribution of Direct Tax

The contribution of direct tax in tax revenue and total revenue were 28.16 percent and 24.35 percent respectively in 2010\11 as against 26.94 percent and 21.01 percent in 2001\02, which is given in the table 4.6

Table 4.6**Contribution of Direct tax on tax revenue, GDP and total revenue**

Fiscal Year	Direct Tax	Direct tax as % of tax revenue	Direct tax as % of GDP	Direct tax as % of total revenue
2001\02	10597.5	26.94	2.31	21.01
2002\03	10881.9	26.61	2.21	19.95
2003\04	11912.6	24.73	2.22	19.11
2004\05	13071.8	24.16	2.22	18.64
2005\06	13968.1	24.32	2.14	19.32
2006\07	18980.3	26.69	2.61	21.64
2007\08	23087.7	27.11	2.83	21.45
2008\09	34320.7	29.32	3.47	23.92
2009\10	41750	26.77	3.50	23.20
2010\11	48655.2	28.16	3.54	24.35
Total	227225.8	264.81	27.05	212.59
Average	22722.58	26.481	2.705	21.259

Source: Economic Survey 2012\13.

From table 4.6 we can conclude that the contribution of direct tax on total tax revenue was decreased until to the fiscal year 2004\05 and then continuously increase by one to two percent until the fiscal year 2008\09. Then it has decreased in 2009\10 and again increased in 2010\11. The main reason of this low contribution of direct tax in Nepal is the exemption of income from agricultural sectors. The share of direct tax on GDP is very low. Its share on GDP was 2.31 percent in 2001\02 and fluctuated continuously until 2006\07. Share of direct tax on GDP was 2.83 percent on 2007\08, 3.50 percent in 2009\10 and 3.54 percent in 2010\11. In the other hand share of direct tax on total revenue remained from 21.01 percent in the fiscal year 2001\02 to 24.35 percent in the fiscal year 2010\11. The average percentage of direct tax on tax revenue, GDP and total revenue were 26.481, 2.705 and 21.259 percentage respectively found during the study period.

4.1.7 Contribution of Income Tax in Nepal

The idea of introducing income tax in Nepal originated along with the first ‘Budget’ on 21st magh 2008 (1952). The then finance minister in the first budget speech said ‘a proposal to levy an income tax including tax on agricultural income is under consideration.’ Several attempts were made to introduce income tax in subsequent years. However, it could not be introduced until 2016 due to political instability. For the first time, the finance ordinance 2016 (1959) has imposed tax on business profit and remuneration in Nepal. Since then it has been contributing revenue to the nation. In the beginning of this system of income tax, it contributed Rs. 203 thousand as revenue in fiscal year 1959\60. In 1962, the first income tax act was enacted which replaced the Business Profit and Remuneration Tax, 1959 into Income Tax Act, 1962. After the introduction of new act, the share of income tax was about 10 folds increased within four years. The contribution of salary tax and business tax to total income tax during the first four years after the introduction of income tax is given in the following table:

Table 4.7
Income Tax Revenue collection (Amount Rs. in thousands)

Heading	1959\60	1960\61	1961\62	1962\63
Business	162	339	1031	1767
Salary Tax	41	67	135	169
Total	203	406	1166	1936
Foreign Investment Tax	–	–	1	140
Grand Total	203	406	1167	2076

Source: budget speeches and economic survey of various fiscal years, MOF.

Table 4.8**Contribution of Income Tax on Different Revenue Heads**

Fiscal year	Income Tax	IT as % of Direct Tax	IT as % of Tax Revenue	IT as % of Total Revenue	IT as % of GDP
2001\02	8903.7	84.02	22.64	17.65	1.94
2002\03	9675.8	88.92	23.66	17.74	1.97
2003\04	9245.9	77.61	19.19	14.83	1.72
2004\05	10159.4	77.72	18.78	14.49	1.72
2005\06	10373.7	74.27	18.06	14.35	1.59
2006\07	15034	79.21	21.14	17.14	2.07
2007\08	17311.2	74.98	20.33	16.09	2.12
2008\09	25142.4	73.26	21.48	17.53	2.54
2009\10	31285.6	74.94	20.02	17.39	2.62
2010\11	38868.5	79.89	22.50	19.45	2.83
Total	176000.2	784.82	207.8	166.66	21.12
Average	17600.02	78.482	20.78	16.666	2.112

Source: Economic Survey 2012\13.

Within the study period income tax increased about four folds in 2010\11 as against in 2001\02. Total income tax in 2001\02 was Rs. 8903.7 million and it increased to Rs. 38868.5 million in 2010\11. The share of income tax to total direct tax was 84.02 % in 2001\02 and it has decreased to 79.89 % in 2010\11. The share of income tax to total tax revenue was 22.64 % in 2001\02 which decreased to 22.50 % in 2010\11. Similarly the shares of income tax to total revenue and to GDP were in increasing trend during study period. The relative share of income tax on total revenue and GDP was 17.65 and 1.94 percent in 2001\02 which increased to 19.45 and 2.83 percent in 2010\11. The average percent collection of income tax on direct tax, tax revenue, total revenue and GDP were 78.482, 20.78, 16.660, 2.112 percent respectively during the study period. Hence, we can say that income tax is one of the prime sources of direct tax in Nepal. But the contribution of income tax to total tax revenue is still lower.

4.1.8 Composition and trend of Income Tax

Till the fiscal year 1993\94 income tax revenue was divided into corporate income tax, individual income tax and remuneration. From the fiscal year 1993\94, the

income tax revenue was divided into four groups. They were: corporate income tax, individual income tax, house and land rent tax and interest tax. Corporate tax is collected from Government Corporation, public & private limited companies and partnership firms. Individual income tax is collected from remuneration, industry, business, profession and others. Interest tax is collected from banks and financial companies which are paid by those companies/banks on all type of deposits. House and land rent tax is levied on income obtained from renting houses and land in urban areas.

Now, the structure of Nepalese income tax is composed of income tax from public enterprises, income tax from private bodies, income tax from individuals, income tax from remunerations and income tax from interest:

Table 4.9
Components of Income Tax (Rs. in millions)

Fiscal year	Income Tax	Government sectors	As % of IT	Public sectors	As % of IT	Private sectors	As % of IT	Remunerations	As % of IT	Interest	As % of IT	% increase in collection
2001\02	8903.7	1769.3	19.87	1412	15.86	4419.1	49.63	835.6	9.38	467.7	5.26	(2.27)
2002\03	9675.8	2928	30.26	1924.3	19.89	3362.2	34.75	597.3	6.17	864	8.93	8.67
2003\04	9245.9	2056.6	22.24	1531.3	16.56	3533.4	38.22	1391.2	15.04	733.4	7.94	(4.44)
2004\05	10159.4	1332.4	13.11	2467.8	24.29	3926.3	38.65	1675.9	16.50	757	7.45	9.88
2005\06	10373.7	195.7	1.89	3404.3	32.82	4234.7	40.82	1764.1	17.01	774.9	7.46	2.11
2006\07	15034	1019.7	6.78	5717.1	38.03	5234.4	34.82	2007.9	13.36	1054.9	7.01	44.92
2007\08	17311.2	204.6	1.18	7186.5	41.51	6381.2	36.86	2451	14.16	1087.9	6.29	15.15
2008\09	25142.4	959.1	3.81	9425.1	37.49	9877.5	39.29	3195.6	12.71	1685.1	6.7	45.24
2009\10	31285.6	1131.8	3.62	12234.4	39.11	11039.9	35.29	4413.1	14.11	2466.4	7.87	24.43
2010\11	38868.5	1281.8	3.30	13965.5	35.93	13627.4	35.06	5863.3	15.08	4130.5	10.63	24.24
Total	176000.2	12879	106.06	59268.3	301.49	65636.1	383.39	24195	133.52	14021.8	75.54	167.93
Average	17600.02	1287.9	10.606	5926.83	30.149	6563.61	38.339	2419.5	13.352	1402.18	7.554	16.793

Source: Economic Survey 2012\13.

From the study of income tax of ten years, the income tax was more decreased in the year 2002/03 in comparison to the year 2001/02. The highest increase rate was 45.24% in 2008/09 is seen from table analysis. Here, we can see the fluctuating increasing rate in the above studies.

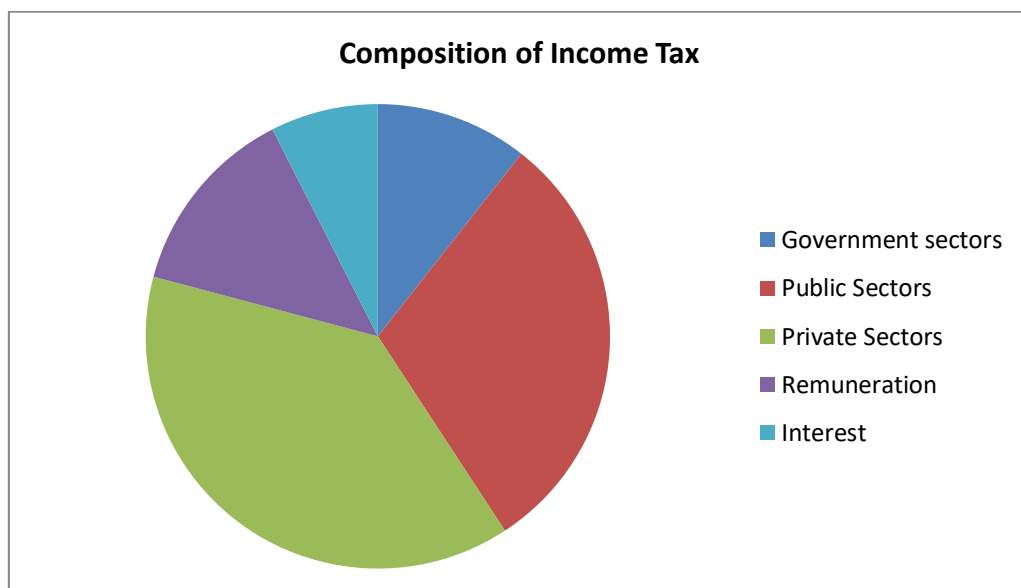
The contribution of income tax from government sectors was 19.87 in 2001/02 and then increased to 30.26 % in 2002/03. Then we can see decreasing contribution of government sectors to income tax till 2005/06. Then the contribution of government sector was between 3% to 4%. Contribution from public sectors, remuneration and interest is comparatively lower than that from private sectors. The average contribution to income tax from government sectors, public sectors, private sectors, remuneration and interest were Rs. 12879 million, Rs. 5926.83 million, Rs. 6563.61 million, Rs. 2419.5 million and Rs. 1402.18 million respectively.

The contribution from public sectors to income tax was also in increasing trend being 15.86% in 2001/02 to 35.93% in 2010/11. The contribution from private sectors was Rs. 4419.1 million i.e. 49.63% in 2001/02, Rs. 3926.3 million i.e. 38.65% in 2004/05, Rs. 9877.5 million i.e. 39.29% in 2008/09 and Rs. 13627.4million i.e. 35.06% in 2010/11. It shows that the contribution of private sector to income tax was in fluctuating trend during the study period.

Income tax from remuneration in 2001/02 was 9.38% in 2001/02 which was increased to 15.08% in 2010/11. This shows that remuneration’s contribution to income tax is increasing. Income tax from interest was 5.26% in 2001/02 and 10.63% in 2010/11 which shows the increasing trend of income tax from interest.

Composition of income tax can also be shown with the help of the following figure:

Figure 4.5



4.1.9 Income Tax Rate

Tax rate and its structure have been changing frequently since its introduction in 1959\60. Since 1959\60 to date, there are various records of highest and lowest income tax rate. In 1963\64, the lowest income tax rate was 4 percent and in 1975\76, the highest income tax rate was 60 percent. After introduction of income tax, tax rate is charged on different slabs. In 1975\76, the income tax rate for personal income was 10 percent to 60 percent for 7 different slabs. From 1988\99 to till date, the income tax rate for personal income is 15 percent and 25 percent for two different slabs.

ITA, 2031 and earlier had not specified the tax rates for each year. Unlike earlier income tax laws, ITA 2058 has specified the tax rates applicable to different taxpayers in schedule 1. Tax rate differ in structure and in terms of percentage depending on whether the taxpayer is an individual or an entity.

➤ **For individual or couple**

- a. A resident individual or a resident couple having taxable income from employment is taxed as under:

For Individual	For Couple	Tax Rates
Up to Rs. 200000	Up to Rs. 250000	1%
Next Rs. 100000	Next Rs. 100000	15%
Next Rs. 2200000	Next Rs. 2150000	25%
Balance	Balance	35%

- b. A resident individual or a resident couple having taxable income from business/ investment only is taxed as under:

For Individual	For Couple	Tax Rates
Up to Rs. 200000	Up to Rs. 250000	Nil
Next Rs. 100000	Next Rs. 100000	15%
Next Rs. 2200000	Next Rs. 2150000	25%
Balance	Balance	35%

- A resident individual or a couple having taxable income exceeding Rs. 25 lakh is imposed an additional tax of 40 % of tax liability of taxable income exceeding Rs. 25 lakh.

- c. A resident individual or a resident couple having taxable income from employment and business and/or investment is taxed as under:

For Individual	For Couple	Tax Rates
Up to Rs. 200000*	Up to Rs. 250000*	1%
Next Rs. 100000	Next Rs. 100000	15%
Next Rs. 2200000	Next Rs. 2150000	25%
Balance	Balance	35%

**even if the assessable income from employment is less than exemption limit, 1% social security tax is imposed on whole exemption amount enjoyed by taxpayer.*

- d. An individual engaged in a special industry is taxed at 20% on the slab where 25 % is applicable normally.
- e. Taxable income of an individual earned from export is taxed at 15 % on the slab where 25 % tax is applicable normally.
- f. Resident couples are normally taxed as two single individuals until and unless they elect to be treated as a couple for tax purpose in writing (Section 50).
- g. An individual working in a remote area specified by GON is entitled to a reduction of remote area allowance up to a maximum of Rs. 50000 from taxable income. The exemption limits specified in Rule 38 of ITR, 2059 for various remote areas are:

Area 'A'	Rs. 50000
Area 'B'	Rs. 40000
Area 'C'	Rs. 30000
Area 'D'	Rs. 20000
Area 'E'	Rs. 10000

- h. a resident individual or couple having pension income is entitled to a 25 % basic exemption as additional exemption.
- i. A disable resident individual or couple is entitled to an additional reduction of 50 % of basic exemption from taxable income.
- j. An employee posted abroad at Nepalese Diplomatic Mission is subject to a reduction of 75 % of foreign allowance.
- k. If a resident individual has investment (life) insurance, annual premium paid or Rs. 20000 (whichever is lower) is subject to a reduction from taxable income.
- l. If a resident individual is a woman having remuneration income only, she is entitled to a rebate of 10 % on tax liability.

dealing in petroleum products established under Nepal Petroleum Act, 2040 are taxed at 30 %.

- d. Entity wholly operating as special industry (under section 11) and entity that has operated any road, bridge, tunnel, rope-way, sky bridge after their construction or entity that has operated trolley bus or tram, cooperatives (except involved in tax exempt transactions) established under Cooperative Act, 2048 are taxed at 20 %.
- e. Entity engaged in the projects to build and operate public infrastructure, and transfer it to GON and entity engaged in power house construction, power generation and transmission are taxed at 20 % on taxable income.
- f. Taxable income of an entity from export with source in Nepal is taxed at 20 %.
- g. Taxable income of a trust acquiring and protecting assets of a deceased resident individual or taxable income of a trust of an incapacitated resident individual is taxes as resident individual.
- h. Repatriated income of a foreign permanent establishment of a non resident person situated in Nepal is taxed at 5 %.
- i. Taxable income of a non-resident person providing shipping, air transport or telecommunication service is taxed at 5 %. However, 2 % tax is applied if these services are provided within the boundary of Nepal only.

For every financial year, finance acts prescribe the exemption limit for individual, family and couple. Above the exemption limit, different income tax rate have been levied. The exemption limits in different years are shown in the following table:

Table 4.10
Exemption Limit in Nepal

(Amount in rupees)

Fiscal Year	Individual	Couple	Family	All taxpayers
1959/60 – 1962/63	-	-	-	7000
1963/64 – 1964/65	-	-	-	6000
1965/66 – 1966/67	-	-	-	5000
1967/68 – 1973/74	3000	4500	6000	-
1974/75	4500	6000	6000	-
1975/76	5500	6500	7500	-
1976/77 – 1978/79	6500	7500	8500	-
1979/80 – 1980/81	7500	10000	10000	-
1981/82 – 1982/83	10000	15000	15000	-
1983/84 – 1989/90	15000	20000	20000	-
1990/91 – 1991/92	20000	30000	30000	-
1992/93 – 1996/97	25000	35000	35000	-
1997/98	30000	40000	40000	-
1998/99	40000	50000	50000	-
1999/2000	50000	60000	60000	-
2000/01 – 2001/02	55000	75000	75000	-
2002/03	65000	85000	85000	-
2003/04	80000	100000	100000	-
2004/05	85000	115000	115000	-
2005/06	100000	125000	125000	-
2006/07	115000	140000	140000	-
2007/08	115000	140000	140000	-
2008/09	160000	200000	200000	-
2009/10	160000	200000	200000	-
2010/11	160000	200000	200000	-
2011/12	160000	200000	200000	-
2012/13	160000	200000	200000	-
2013/14	200000	2500000	250000	-

Source: Finance Acts of Various Year, MOF, GON and budget speech 070/71.

The table 4.10 shows that there was only one exemption limit for all individual, taxpayers from 1959/60 to 1966/67. After 1967/68, individual taxpayers were

categorized into 3 heads i.e. individual, couple and family. From the FY 1967/68 to 1978/79, exemption limit was distinct for each 3 categories. But after 1981\82 to till date, the exemption limit of couple and family is treated equal. This indicates that the exemption limit is given only for 2 categories i.e. individual and family or couple. Above the exemption limit of individual income, different sets of tax rates are levied for different slabs. The following table shows the rates for personal income tax in Nepal.

Table 4.11
Rates for Personal Income Tax in Nepal
(Slab amount in rupees)

Fiscal year	Slab and Tax Rates on Slabs Over Exemption Limit							
	1'st	2'nd	3'rd	4'th	5'th	6'th	7'th	8'th
1975\76	5000 @7%	5000 @10%	10000 @20%	10000 @30%	10000 @45%	50000 @55%	Balance @60%	
1980\81	5000 @5%	5000 @10%	10000 @15%	20000 @20%	20000 @30%	30000 @40%	Balance @50%	
1985\86	5000 @10%	5000 @15%	10000 @20%	15000 @25%	15000 @40%	30000 @40%	30000 @50%	Balance @55%
1990\91	10000 @15%	15000 @20%	20000 @35%	25000 @40%	30000 @45%	Balance @50%		
1995\96	40000 @10%	25000 @20%	Balance (a)30% (b)33%					
2000\01	75000 @15%	Balance @25%						
2001\02- 2006\07	75000 @15%	Balance @25%	Addition al 1.5%					
2007\08- 2010\11	85000 @15%	Balance @25%						
2011\12	100000 @15%	Balance @25%	*Addition al tax 40%					

**If total taxable income is more than Rs.2500000, additional 40% of 25 % or 35 % on additional amount is levied.*

Source: Finance Acts of Various Years, MOF, G/N.

Where, (a) Remuneration (b) Others.

From the table 4.11, the rates for personal income tax in Nepal are different for different slabs. In 1975/76, the tax rate for personal income was 7 to 60 percent for 7 different slabs. After 1975/76, the slabs were increased to 8 in 1985/86. But after 1985/86, the numbers of slabs and rates of personal income tax are decreasing till date. From 2001/02 to 2006/07 there was 15% rate for first Rs. 75,000 and 25% for balance and additional 1.5% for balance too. From fiscal year 2007/08, the additional tax for balance has been eliminated. There was 15% tax rate for first 85000 and 25% for balance. From the fiscal year 2011\12 there was 15% rate for the first Rs. 1, 00,000 and 25% for balance.

Similarly, income tax is charged for partnership firms, corporations and non residents. The exemption limit for them is not provided by the income tax act. Tax is charged on the income after deducting all expenses. The rates and slabs approved for different years are given below:

Table 4.12
Income Tax Rates for Partnership Firms, Corporation and Non-Residents

Fiscal year	Slabs over exemption limit							
	1	2	3	4	5	6	7	8
1975/76	10000 15%	10000 25%	10000 40%	50000 55%	Balance 60%	-	-	
1980/81	5000 5%	5000 10%	10000 15%	20000 20%	20000 30%	30000 40%	Balance 50%	
1985/86	5000 10%	5000 15%	10000 20%	15000 25%	15000 30%	30000 40%	200000 50%	Balance 55%
1990/91	10000 15%	15000 20%	20000 35%	25000 40%	30000 45%	Balance 50%		
1995/96	33% in total							
2000/01- 2005/06	30% (a) 25% (b)							
2006/07- 2011/12	30% (a) 25% (b) 20% (c)							

Source: Finance Act of various years, MOF, GON.

a) For banks and finance companies and alcohol/tobacco industry.

- b) Others (including partnership firms).
- c) For special industry.

The table 4.12 shows that the income tax rates for partnership firms, corporation and non-resident were different for different slabs in the earlier years. But after 1995/96, the rate and slab is only one. This shows the progressive tax in earlier year and flat tax rate in the recent years. The income tax rate for 1975/76 was 15 to 60 percent for 5 slabs. But in 1995/96, tax rate was in total 33 percent. And from 2002/03 to till date, the tax rate are 30 percent for banking and financial institutions and tobacco and alcohol industries, 25 percent for other (including partnership firms) and 20 percent for the special industry at a flat rate on taxable income.

4.2 An Analysis of Exemption and Deduction

The parliament of Nepal enacted ITA, 2058 with effective from Chaitra 19, 2058 B.S. This act has replaced ITA, 2031, which was amended for eight times and existed for a period of 28 years. This act has classified the income heads into the following heads. They are:

1. Income from Business
2. Income from Employment
3. Income from investment

This act has defined the income head as follows:

1. Income from Business: ITA, 2058 has defined business as an industry, a trade, a profession, or the isolated transaction with a business character and includes a past, present or prospective business. It combined an income from the provision of labour and capital. A person's income from a business for an income year is the person's profits and gains from conducting the business for the year.

2. Income from Employment: ITA, 2058 has not given specific definition of employment. But it has used the term broadly to include past, present or prospective employment. Income from employment is basically remuneration received or accrued periodically for service rendered as a result of expressed or implied contract. It is the payment or benefits received either in cash or kind from the employer or his associate in exchange of labour service. From tax perspective, the employment income can be

defined in terms of whatever compensation an employee receives for a service that the government will tax.

3. Income from Investment: ITA, 2058 has defined investment as an act of holding or investing one or more assets. But, it excludes the act of holding of assets for personal use by the person owing the asset and employment or business. However, the act of holding non-business chargeable asset by the person for personal use is considered as an investment. It is, in fact, a residual income, which is computed only after computing business and employment income. A person's income from an investment for an income year is the person's profits and gains from conducting the investment for the year.

For the calculation of net income of these three income heads, the act has defined the incomes or amounts, which are taxable and non-taxable and expenses, which are allowed for deduction and not allowed for deduction. For the computation of income, act has made the following provisions:

4.2.1 Income from a Business

ITA, 2058, Section 7 has clearly mentioned the incomes or amounts which are includable in computing the income from business. They are:

- a. Service charge (sec. 7.2)
- b. Disposal of business/trading stock (sec. 7.2)
- c. Net gain from disposal of business assets or liabilities (sec. 7.2)
- d. Gain from disposal of pool of depreciable assets (sec. 7.2)
- e. Prizes or gifts in connection with business (sec. 7.2)
- f. Amount received in lieu of accepting any restriction regarding business (sec. 7.2)
- g. Amount received from any investment directly related to business (sec. 7.2)
- h. Incomes to be included due to change in accounting methods (sec 22.6)
- i. Excess amounts received due to exchange rate variation (sec. 24.4)
- j. Bad debts recovered (sec. 25.1)
- k. Proportionate amounts received under long-term contracts (sec. 26.1)
- l. Under payment of interest according to market rate (sec. 27.1)
- m. Receivable amounts paid to others (sec. 29)

- n. Amount received from compensation (sec. 31)
- o. Other amounts received under the head of business income (sec. 7.2)

While computing income tax from business, the following amounts are excluded on profit and income from business for tax purpose.

- a. Amounts exempt from tax under section 10
- b. Taxation of dividends under section 54
- c. Dividends distributed by a controlled foreign entity at the year under section 69.
- d. Final withholding payments under section 92.

4.2.2 Income from an Employment

All the amounts or benefits received in connection with employment are taxable. As per section 8 (2) of ITA, 2058, an employee's income from employment includes the following payments made during the year:

- a. Payments of wages, salary, leave pay, fees, commission, prizes, gifts, bonuses, and other facilities.
- b. Payments of any personal allowance, including any cost of living subsistence, dearness, rent, entertainment and transportation allowance.
- c. Payments providing any discharge or reimbursement of costs incurred by the individual or an associate of the individual.
- d. Payments for the individual's agreement to any conditions of the employment.
- e. Payments for redundancy or loss or termination of the employment.
- f. Retirement contributions (i.e. provident fund, gratuity etc) including those paid by the employer to a retirement fund in respect of the employee and retirement payments.
- g. Other payments made in respect of the employment.
- h. Other amount includable on tax accounting or quantification, allocation and characterization of accounts.

In the above provisions, there is a provision of loss of employment. But the provision has not classified the meaning of loss of employment. In the other hand, retirement contribution are nothing else than the product of sacrifice of oldness of employments. These are the bases for living standards of oldness of employees. So it does not give

good information to the taxpayers/employees. Dearness allowance is given to meet the living standard of employees. It is not lawful to include in taxable income.

Non-includable Amounts on Employment Income: Following incomes are excluded in calculating the employment income of an employee:

- a. Amounts exempt from tax under section 10.
- b. Final withholding payments under section 92.
- c. Meals and refreshments provided to employees at business premises/work site if provided to all employees under equal terms [sec. 8(3)].
- d. Settlement by or reimbursement to an employee of expenses incurred solely for the purpose of business [sec. 8(3)].
- e. Payments by the employer for petty expenses relating to tea expenses, stationeries, tips, prizes and emergency medical treatment up to Rs. 500 at a time whose accounting is not practical or administratively difficult [sec. 8(3)].
- f. Others amounts: as per a notification issued by IRD and also as per Rule 20(6), all amounts exempt from tax under ITA, 2031 which accrued prior to the Act coming into force will remain exempt from tax even if payment as made after Chaitra 18, 2058.

4.2.3 Income from an Investment

A person's profits and gains from an investment for an income year include the following amounts derived by the person during the year:

- a. Any dividend, interest, natural resource payment, rent, royalty, gain from investment insurance, gain from an unapproved retirement fund, interest, or retirement payment made by an approved retirement fund.
- b. Net gains from the disposal of non-business chargeable assets of the investments.
- c. Amount treated as derived in respect of excess depreciation on the disposal of the person's depreciable assets of the investment.
- d. Gifts received in respect of investment.
- e. Amount derived as consideration for accepting restriction on the capacity to conduct the investment.
- f. Income received from joint investment.
- g. Bad debt recovered.

- h. Amount received for compensation.
- i. Under payment of interest related to investment.
- j. Exchange gain.
- k. Incomes to be included due to change in accounting methods.
- l. Other amounts required to be included as a result of tax accounting or quantification or as specified by the Act.

In the above provision, act has included the amounts derived as consideration for accepting or restriction or the capacity to conduct the investment, it is fruitful to the investors who receive the compensation against the restriction. But it will not be possible to implement, if the act does not clarify the nature of restriction, cause of imposing restriction, process of compensation computing and entity which give compensation non-includable amounts on investment income.

Amounts excluded from Investment Income

Following amount are excluded in calculating income from investment:

- a. Amounts exempted from tax under section 10.
- b. Taxation of dividend under section 54.
- c. Dividend distributed by a controlled foreign entity at the end of the year under section 69 and final withholding payments as per section 92.
- d. Amounts that are to be included in the person's income from employment or business.

4.2.4 Exemption from Income Tax

ITA, 2058 has clearly defined amounts which are exempt and other concessions. They are described in the following section.

1. Exempt Amounts

ITA, 2058 has exempted following amounts from income tax under section 10:

- a. Amount received by a person entitled to privilege under a bilateral or a multilateral treaty concluded between the GON and a foreign country or an international organization.
- b. Any amounts received by an individual from employment in the public service of the government of a foreign country. But for this, he must be a resident or

non-resident solely by the reason of employment and the amounts must be paid from the public fund of the country.

- c. Amount received from the public fund of a foreign country by an individual who is not a citizen of Nepal or by a member of the immediate family of the individual.
- d. Amount received by an individual, who is not a citizen of Nepal, from employment at the GON's service on terms of tax exemption.
- e. Allowance paid by the GON to widow, elder citizen or disable individual.
- f. Amount received by way of gift, bequest, inheritance, or scholarship except as required to be included in calculating income from business, employment or investment.
- g. Amount received by an exempt organization by way of the following:
 - i. Gifts, donation
 - ii. Other contributions that directly relate to the organization's function of the definition of exempt organization in section 2.
 - iii. Amount earned by Nepal Rastra Bank as per its objectives.
 - iv. Amount earned by Securities Board of Nepal (SEBON) as per its objectives.
- h. Pension received by a Nepali citizen retired from the army or police service of a foreign country. These amounts must be paid from the public fund of that country.

In the above section, pension amounts received by Nepalese people being retired from the service by army or police of foreign country are exempted from income tax. It restricts the objective of raising more revenue of government because some of the amounts received are more than the exemption limit approved by the government.

2. Exempt Organization (sec. 2 Dha)

Exempt organization means the following entities:

Following entities registered with IRD as tax-exempt entity-

- i. A social, religious, educational, or charitable organization of public character registered without having a profit motive.
- ii. An amateur sporting association formed for the purpose of promoting social or sporting amenities not involving in the acquisition of gain by it or by its members.

- iii. A political party registered with the Election Commission.
- iv. A village Development Committee, a Municipality or a District Development Committee.

However, any benefit acquired by any person out of the assets of and amounts derived by the entity except in pursuit of the entities function or as payment for assets or services rendered to the entity by the person is not exempt from tax.

3. Business Exemptions and Concessions:

ITA, 2058 has provided following business exemptions and concessions in section 11.

- a. Agriculture income received by an individual holding land within the ceiling prescribed in Land Act, 2021 is exempt from tax. But income from agriculture business by a registered firm, company, partnership and corporate body and through the land above the holding ceiling as prescribed in the Land Act, 2021 are not tax exempted.
- b. Incomes derived by cooperative societies registered and functioning under Cooperative Act, 2048 from agriculture or forest products based sericulture and silk production, horticulture production and fruit processing, animal husbandry, dairy industries, poultry farming, fishery, tea gardening and processing, coffee farming and processing, herbiculture and herb processing, vegetable seeds farming, bee-keeping, honey production, rubber farming, lease-hold forestry, agro-forestry, cold storage established for the storage of vegetables and business of agricultural seeds, animals feeds, insecticide, fertilizer and agricultural tools (except those operated with mechanical power) are exempt from tax. Similarly, income of a rural community based saving and credit cooperative is exempt from tax. Dividend distributed by such societies is also exempt from tax.
- c. Income of a special industry and Information Technology (IT) industry of a person with source in Nepal for an income year is taxed as under
 - i. A special industry and an IT industry providing direct employment to 300 or more Nepalese citizens throughout the income year are taxed at the rate of 90% of the applicable tax rate on that's year's income.
 - ii. A special industry providing direct employment to 1200 or more Nepalese citizens throughout the year is taxed at 80% of applicable tax rate on that year's income.

- iii. A special industry providing direct employment to more than 100 Nepalese citizens including at least 33% women, downtrodden (dalit), or the handicapped (apanga) throughout the year is taxed at 80% of applicable tax rate on that year's income.
 - iv. A special industry operating in remote (highly/most undeveloped), undeveloped and underdeveloped area (as defined in Industrial Enterprise Act, 2049) is taxed at 10%, 20% and 30% of the applicable tax rate on its income respectively up to ten income years including the income year of its operation.
- d. Income of an industry established in Special Economic Zone (SEZ) and dividend distributed by such industry are subject to following exemption:
- i. Income of such industry located at mountainous district and GON-specified hilly districts is exempt from income tax for the first ten years of its operation and then taxed at 50% of the tax rate otherwise applicable.
 - ii. Income of such industry located at other than areas specified above is exempt from income tax for the first five years of its operation and then taxed at 50% of the income tax rate otherwise applicable.
 - iii. Dividend distributed by an industry established in SEZ is exempt from tax for the first five years and then taxed at 50% of the tax rate otherwise applicable for the next three years.
 - iv. Royalty, foreign technology or management service fees earned by a foreign investor of such industry are taxed at 50% of the income tax rate otherwise applicable.
- e. The industries related to IT established in IT Park, Technology Park and Bio-tech Park as specified by GON by publishing notice in Nepal Gazette are exempt from 50% income tax.
- f. A person engaged in exploring and excavating petroleum and natural gas commercially within 2075 Chaitra is exempt from tax for the first 7 years and then taxed at 50% of tax rate for the next 3 years.
- g. The income of a manufacturing industry earned from export of goods manufactured is subject to an exemption of 25% of the applicable tax rate.
- h. A rebate of 40% on income tax is granted for income earned from construction and operation of road, bridge, airport and tunnel or from operation of tram or trolley bus.

- i. The entities engaged in manufacturing, tourism service and electricity generation, distribution and transmission and the entities established in IT Park, Technology Park and Bio-tech Park listed in stock exchange market get 10% exemption on applicable tax rate.
- j. The industry established in highly undeveloped area producing fruit based brandy, cider and wine are exempted 40 % income tax for the first ten years the operation commences.
- k. The royalty and income earned from export and sale by the way of transfer of intellectual properties by a person is exempted 25% and 50 % on applicable income tax rate.
- l. The income if more than one exemption or concession is available to the same income, only one exemption is available to the person as per the selection made by the person.
- m. If the properties used in a special industry were used previously by another person operating similar type of special industry, the exemption period for the latter special industry will be counted from the period of such use by the previous person.

4.2.5 Deduction Allowed

1. General Deduction (Sec.13)

Basically all actual costs to the extent incurred during the income year, by the person and in the generation of income from business or investment are allowed for deduction.

2. Interest (Sec. 14)

The interest incurred during the year for the debt obligation that has been created in the generation of income from business or investment is allowed for deduction to the extent that the debt is used in that year or the debt is used to purchase an asset used in that year or the debt obligation is created in any other conditions. An exempt controlled resident entity paying interest to the controlling person or associated person is allowed for deduction to the to the extent of the sum of all interest incomes that are to be included in the entity's taxable income and 50% of the entity's adjusted taxable income for the year calculated without including any interest income and deducting any interest expenses. The portion of the interest not

deducted during the year because of above limitation can be carried forward to next income year.

It is an unlawful step to businessmen not to get the deduction of full amount of interest. It does not fulfill the objectives of industrial or economic development. There is a controversial condition between the law of banking and law of income tax because according to the law of banking interest must be paid to bank but according to the law of income tax there is a provision of not to get the deduction of full amount of interest for an income year.

3. Cost of trading stock (Sec. 15)

Trading stocks are goods held for resale purpose. Trading stock includes raw material, work in progress and finished goods. But it does not include stock in foreign currencies. Cost of trading stock is derived as follows:

Cost of opening stock + purchased or produced during the year – Cost of closing stock = Cost of trading stock

The closing stock of previous year will be the opening stock for this year. Closing stock is valued at cost price or market price whichever is lower. The person keeping account on a cash basis can adopt either the prime cost or factory cost as basis for the valuation of trading stocks while the person keeping accounts on an accrual basis must adopt factory cost basis for the valuation of trading stocks. If actual cost could not be derived for particular trading stock; either FIFO or Weighted Average Cost Method can be used. Once a method is selected, it cannot be changed without the written approval of IRD. Prime cost includes cost of raw material consumed, direct labour cost and variable factory overhead where as factory cost includes cost of raw material consumed, direct labour cost and factory overhead (both fixed and variable).

4. Repair and improvement cost (Sec.16)

The repair and improvement cost incurred during the year for the depreciable assets owned and used by a person in generating income from business or investment is deductible up to 7% of depreciation basis or actual cost whichever is lower. The unabsorbed repair cost is capitalized at the beginning of the next income year in respective blocks. However, the repair and improved costs incurred by airline business for overhauling of aircraft according to the standards prescribed by Civil Aviation Authority of Nepal (CAAN) are allowed for deduction.

5. Pollution Control Cost (Sec.17)

Pollution control cost means cost incurred by a person with respect to a process or an asset that seeks to control pollution or otherwise protect or sustain the environment. Though these costs are of capital nature are allowed for deduction for income tax purpose. Actual pollution control cost or 50% of adjusted taxable income from all businesses conducted by the person whichever is lower is allowed for deduction. The portion of pollution control cost not allowed as deduction is capitalized at the beginning of the next income year under Block “D”.

Government has a will of controlling pollution and then protection of environment but has not spent a little bit money on it. In the other hand all the expenses made by the businessmen to control pollution are not allowed for deduction and has made a standard limit for it. So, it is not a good symptom of controlling pollution.

6. Research and Development Cost (Sec.18)

R & D cost means cost incurred by a person for the purposes of developing the person’s business and improving business products or process. However, it does not include cost in respect of natural resource prospecting, exploration and development incurred by a person in the production of the person’s income from a business, which is treated as an outgoing for an asset used by the person in that production.

Although R & D costs are of capital nature are allowed for deduction for income tax purpose. The actual R&D cost or 50% of adjusted taxable income from all businesses conducted by the person, whichever is lower is allowed for deduction. The portion of R&D cost not allowed as deduction is capitalized at the beginning of next income year under Block ‘D’.

7. Depreciation Allowance (Sec.19)

For the purpose of calculating a person's income for an income year from any business or investment, there shall be deducted in respect of depreciation of depreciable assets owned and used by the person during the year in the production of the person's income from the business or investment. But the following provisions shall be applied in respect of depreciation of machines, equipment and other machinery installed in the electricity projects that are involving in building power station, generating and transmitting electricity and in the projects conducted by any entity so as to build public infrastructure, own, operate and transfer to the GON.

In case where the old machines, equipment and other machinery that are already installed require replacement in any income year as they are out of order due to being too old, the balancing value of the old machines, equipment and other machinery remained after cost shall be allowed as expenses for the year.

At the time of transfer of other assets to the Nepalese government except of old assets replace in accordance with above paragraph, the balancing value of remained, after subtracting the depreciation up the year of the transfer from their cost shall be allowed as expenses.

For the purpose of depreciation calculation, depreciable assets are categorized into five groups on their size, nature, cost, durability, similarly, utility and so on as A, B, C, D and E block, pool or group. Depreciation are charged at the rate of 5, 25, 20 and 15 percent for A, B, C and D respectively and for pool E depreciation is charged on the basis of cost divided by useful life.

Rates of depreciation are far from reality because there is no specific estimation provision of real age of assets and depreciation rate in Nepal. In the other hand, there is no any specific provision of depreciation of assets, which are taken in lease and installment payment basis. It shows a weak point of new income tax act.

8. Bad Debts (Sec. 25.2)

Bad debts can be deducted as expenses under the following conditions:

If the outstanding loan of bank or financial institution has become a bad debt in accordance with the standards prescribed by NRB.

In other case, the person receiving payment believes that the amount could not be recovered after taking reasonable steps.

9. Losses from Business (Sec. 20)

A person is allowed to deduct the following losses while calculating income from business for an income year:

Any unrecovered loss of the year incurred by the person from any other business and any unrecovered loss of previous seven years incurred by the person from any business.

In the case of electricity projects involving in business power station, generating and transmitting electricity and the projects conducted by any entity so as to build public infrastructure, own operate and transfer (BOOT) to the government, entity

conducting petroleum business under Nepal Petroleum Act 2040, losses can be deducted up to next 12 years.

When losses incurred in investment of domestic source, those losses can be set off and carry forwarded up to 7 years from any incomes of investment within the country or outside the country only.

Where a person may deduct an unrelieved loss in calculating the person's income for an income year from more than one business or investment, the person may prioritize in which calculation the loss or part of the loss is deducted.

Carry forward the loss for 7 years is not sufficient as compared to other countries. It is not enough to encourage the business for taking risk. The provision of carry backward is also thoughtful because of accounting system of Nepal is not so standard to apply this provision.

4.2.6 Allowable Reductions

a. Donation to Exempt Organization (Sec 12 and Sec 12 Ka)

Donation given to an exempt organization, approved by IRD, is allowed for reductions from taxable income. Reductions allowed to an individual or an entity will not exceed Rs. 1,00,000 or 5 % of adjustable taxable income. However, the GON may prescribe by publishing a notice in the Nepal Gazette, as to allow full or partial deduction of the expense incurred for special purpose at the time of assessing income.

Expenses incurred by a company for the protection and promotion of ancient, religious and cultural heritage located in Nepal and for building public physical infrastructure of sports are allowed for reduction with a pre-approval of IRD up to Rs. 10 lakhs or 10 % of assessable income or actual, whichever is the lowest.

b. Retirement Contribution (Sec. 63)

An individual who is a beneficiary of an approved retirement fund may claim a reduction for retirement contributions made to the fund. The actual contribution or maximum Rs. 3,00,000 or one-third of the assessable income, whichever is the lowest is allowed for reduction as retirement contribution.

4.2.7 Expenses not allowed for Deduction

To calculate the income of a person's for an income year from any business, employment or investment, the following expenses are not allowed for deduction under 21 of ITA, 2058.

- a. Personal or domestic expenses.
- b. Income tax payable under ITA, 2058.
- c. Fines and penalties paid to government or its local bodies.
- d. Expenses incurred to derive the tax exempted amounts or final withholding payments.
- e. Cash payment over Rs. 50,000 by an individual or an entity having an annual turnover more than Rs. 2 million except in following circumstances:
 - i. If payment is made to the GON, a constitutional body, a corporation owned by GON, or a bank or financial institution.
 - ii. If payment is made to a farmer or a producer producing primary agricultural products.
 - iii. If payment is made to a retirement contribution or retirement payment.
 - iv. If payment is made in an area where banking services are not available within the surrounding of ten kilometers.
 - v. If payment is and must necessarily be made in cash or on a day when banking services are closed.
 - vi. If payment is made into a bank account of the payee.
- f. Distribution of profits by an entity.
- g. Expenses not related to earning of income.
- h. Any reserve, provision or fund.
- i. Expenses of capital nature.
- j. Foreign income tax paid.
- k. Other expenditure not exempted as admissible.

4.3 An Empirical Analysis

4.3.1 Introduction

For providing reliability of this paper findings, efforts of collecting primary data has been done through questionnaire technique as well as face to face interact approach to

few respondents. In order to find out various aspects of income tax from the experience of the real world, an opinion questionnaire was dispatched to 100 respondents representing tax experts, tax administrators and tax payers, but only 80 responses were received. The questionnaire included the various aspects of income tax concerning the provisions of exemptions and deductions and contribution of income tax to the government revenue. This chapter analyzes information collected from primary sources i.e. questionnaire. The questionnaires were asked for yes/no responses or asked for ranking of choice according to the number of alternatives where a first choice was most important and last choice was least important or there were also options to put respondents' views in written form whenever necessary. The responses received from various respondents have been arranged, tabulated into separate format, have been expressed in percent of total numbers or points and analyzed in order to facilitate the descriptive analysis of the research study. The table 4.13 shows the groups of respondents and code used to represent them.

Table 4.13

Groups of Respondents and code use

S.N.	Groups of Respondents	Sample Size	Code Used
1	Tax Experts	20	A
2	Tax Administrators	30	B
3	Tax Payers	30	C
Total		80	

Source : As per research design, 2013.

4.3.2 Contribution of Income Tax to National Revenue of Nepal

In order to know the respondent's opinion about the contribution of IT to national revenue of Nepal, a question was asked to answer in "yes" or "No" option as "Do you think that contribution of income tax to national revenue of Nepal is satisfactory?" The responses received from respondents are tabulated as in the table 4.14 as follows:

Table 4.14

Contribution of Income Tax to National Revenue of Nepal

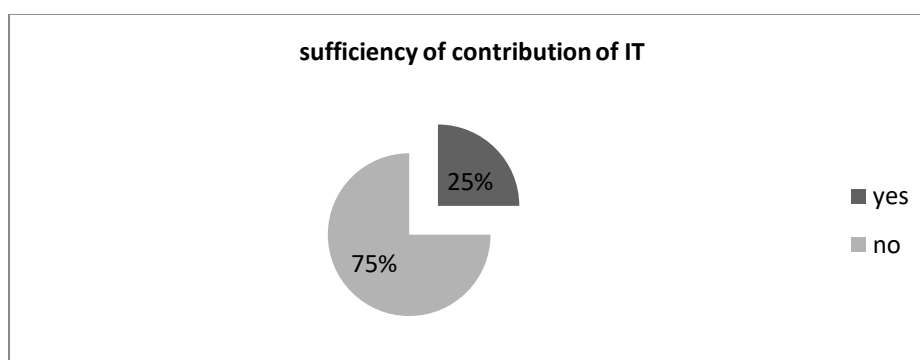
Responses Respondents	Yes		No		Total	
	No.	%	No.	%	No.	%
A	2	10	18	90	20	100
B	12	40	18	60	30	100
C	6	20	24	80	30	100
Total	20	25	60	75	80	100

Source: Opinion Survey 2013.

These responses can be presented in the diagram as well:

Figure 4.6

Contribution of Income Tax to National Revenue of Nepal



From the table 4.14 and figure 4.6 it is known that the 20 respondents i.e. 25% of total respondents were agreed that the contribution of income tax to national revenue of Nepal is satisfactory whereas 60 respondents i.e. 75% of the respondents were not agreed about satisfactory contribution of income tax to national revenue of Nepal. Thus it can be concluded that the contribution of income tax to national revenue of Nepal is not satisfactory.

4.3.3 Major causes responsible for unsatisfactory contribution of Income Tax to national revenue of Nepal

In order to know the causes which are responsible for unsatisfactory contribution of income tax to the national revenue of Nepal, the next question was asked as, "If your answer is 'No', what are the major causes which are responsible for unsatisfactory contribution of income tax to national revenue?" It was requested to all the

respondents who responses ‘No’ to rank from 1 to 8 from the given options in order of preference from first (most important) to the last (least important).

Responses received have been tabulated and analyzed in four groups:

1. Tax experts’ view
2. Tax administrators’ view
3. Tax payers’ view
4. Overall view

In order to find out the ranks we used weighted mean separately for every group.

Weighted mean:

Mean in which each item being averaged is multiplied by a number (weight) based on the item’s relative importance. The result is summed and the total is divided by the sum of the weights. Weighted averages are used extensively in descriptive statistical analysis. In short weighted mean is an average that takes into account the proportional relevance of each component, rather than treating each component equally. In the case of ranking analysis the lowest weighted mean stands for first ranking and the highest one standing for last rank.

The weighted mean is given by,

$$\bar{X} = \frac{\sum WX}{\sum W}$$

Weighted mean (\bar{X}) is calculated by dividing the total value ($\sum WX$) by the total weight ($\sum W$).

Table 4.15
Major Causes which are responsible for unsatisfactory contribution of
Income Tax to the National Revenue of Nepal

		Tax experts’ view								
S.N.	Major Causes	1	2	3	4	5	6	7	8	Total
a.	Defective assessment procedure	2	-	4	2	4	2	4	-	18
b.	Lack of public participation	-	-	4	4	4	4	2	-	18
c.	Inefficient organizational structure of tax administration	-	-	2	2	4	4	4	2	18
d.	Scarce of income tax expert/ professionals in tax administration	-	2	2	2	2	6	2	2	18
e.	Weakness in government’s economic policy	8	4	2	4	-	-	-	-	18
f.	Lack of co-ordination within the tax department	-	2	2	2	4	-	-	8	18
g.	Complicated tax laws and provisions	-	4	-	2	-	-	6	6	18
h.	Corruptions	8	6	2	-	-	2	-	-	18

Source: Opinion Survey 2013.

Further we used the information tabulated in Table 4.15 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as below.

S.N.	Major Causes	Rank * No. of Responses (W * X)								$\sum W$ X	Weighted Mean	Rank
		2	-	1	8	2	1	2	-			
a.	Defective assessment procedure	2	-	1	8	2	1	2	-	82	4.56	3
b.	Lack of public participation	-	-	1	1	2	2	1	-	86	4.78	4
c.	Inefficient organizational structure of tax administration	-	-	6	8	2	2	2	16	102	5.67	6
d.	Scarce of income tax expert/professionals in tax administration	-	4	6	8	1	3	1	16	94	5.22	5
e.	Weakness in government's economic policy	8	8	6	1	-	-	-	-	38	2.11	1
f.	Lack of co-ordination within the tax department	-	4	6	8	2	-	-	64	102	5.67	6
g.	Complicated tax laws and provisions	-	8	-	8	-	-	4	48	106	5.89	8
h.	Corruptions	8	1	6	-	-	1	-	-	38	2.11	1

Weighted mean for the causes “Corruption” and “Weakness in government's economic policy” is the lowest i.e. 2.11. So they are ranked first. So as “Complicated tax laws and provisions” is the highest i.e. 5.89 so it is ranked last. In general the major causes for unsatisfactory contribution of income tax to national revenue in accordance to the view of tax expert are as follows:-

1. Weakness in government's economic policy
2. Corruptions
3. Defective assessment procedure
4. Lack of public participation
5. Scarce of income tax experts/professionals in tax administration
6. Inefficient organizational structure of tax administration
7. Lack of coordination within the tax department
8. Complicated tax laws and provisions

Table 4.16

**Major Causes which are responsible for unsatisfactory contribution of
Income Tax to the National Revenue of Nepal**

Tax administrators' view

S.N.	Major Causes	1	2	3	4	5	6	7	8	Total
a.	Defective assessment procedure	-	-	1	6	5	2	1	3	18
b.	Lack of public participation	4	5	2	3	2	-	1	1	18
c.	Inefficient organizational structure of tax administration	2	3	5	-	2	2	2	2	18
d.	Scarce of income tax expert/ professionals in tax administration	2	-	3	1	3	2	4	3	18
e.	Weakness in government's economic policy	5	6	-	2	-	2	1	2	18
f.	Lack of co-ordination within the tax department	-	-	2	3	2	4	4	3	18
g.	Complicated tax laws and provisions	5	3	2	1	2	2	2	1	18
h.	Corruptions	-	1	3	2	2	4	3	3	18

Source: Opinion Survey 2013.

Further we used the information tabulated in Table 4.16 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as below.

S.N.	Major Causes	Rank * No. of Responses (W * X)								$\sum W$ X	Weight ed Mean	Rank
		1	2	3	4	5	6	7	8			
a.	Defective assessment procedure	-	-	3	2	2	1	7	24	95	5.28	6
b.	Lack of public participation	4	1	6	1	1	-	7	8	57	3.17	1
c.	Inefficient organizational structure of tax administration	2	6	1	-	1	1	1	16	75	4.17	4
d.	Scarce of income tax expert/ professionals in tax administration	2	-	9	4	1	1	2	24	94	5.22	5
e.	Weakness in government's economic policy	5	1	-	8	-	1	7	16	60	3.3	2
f.	Lack of co-ordination within the tax department	-	-	6	1	1	2	2	24	104	5.78	8
g.	Complicated tax laws and provisions	5	6	6	4	1	1	1	8	65	3.61	3
h.	Corruptions	-	2	9	8	1	2	2	24	98	5.44	7

Weighted mean for the causes “lack of public participation” is the lowest one i.e. 3.17. So it is ranked first as major causes. Whereas “lack of coordination within the tax department “is the highest i.e. 5.78 so, it is ranked last. In general the major causes

for unsatisfactory contribution of income tax to national revenue of Nepal according to tax administrator's preference are as follows:-

1. Lack of public participation
2. Weakness in government's economic policy
3. Complicated tax laws and provisions
4. Inefficient organizational structure of tax administration
5. Scarce of income tax expert/professionals in tax administration
6. Defective assessment procedure
7. Corruptions
8. Lack of coordination within the tax departments

Table 4.17

Major Causes which are responsible for unsatisfactory contribution of Income Tax to the National Revenue of Nepal

		Tax payers' view								
S.N.	Major Causes	1	2	3	4	5	6	7	8	Total
a.	Defective assessment procedure	-	1	2	4	3	8	5	1	24
b.	Lack of public participation	3	2	3	2	3	2	5	4	24
c.	Inefficient organizational structure of tax administration	-	2	1	2	4	3	5	7	24
d.	Scarce of income tax expert/professionals in tax administration	1	2	3	3	4	4	2	5	24
e.	Weakness in government's economic policy	6	5	6	2	1	1	2	1	24
f.	Lack of co-ordination within the tax department	2	3	3	5	4	3	2	2	24
g.	Complicated tax laws and provisions	5	4	2	3	4	2	1	3	24
h.	Corruptions	7	5	4	3	1	1	2	1	24

Source: Opinion Survey 2013.

Further we used the information tabulated in Table 4.17 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as below.

S.N.	Major Causes	Rank * No. of Responses (W * X)								$\sum W$ \bar{X}	Weight ed Mean	Rank
		-	2	6	1	1	4	3	8			
a.	Defective assessment procedure	-	2	6	1	1	4	3	8	130	5.42	7
b.	Lack of public participation	3	4	9	8	1	1	3	32	118	4.92	5
c.	Inefficient organizational structure of tax administration	-	4	3	8	2	1	3	56	144	6	8
d.	Scarce of income tax expert/professionals in tax administration	1	4	9	1	2	2	1	40	124	5.17	6
e.	Weakness in government's economic policy	6	1	1	8	5	6	1	8	75	3.125	2
f.	Lack of co-ordination within the tax department	2	6	9	2	2	1	1	16	105	4.375	4
g.	Complicated tax laws and provisions	5	8	6	1	2	1	7	24	94	3.92	3
h.	Corruptions	7	1	1	1	5	6	1	8	74	3.08	1

Weighted mean for the causes “ Corruptions” is the lowest one i.e. 3.08. So it is ranked first as a major cause. Whereas “inefficient organizational structure of tax administration” is the highest i.e. 6 so it is ranked last. In general the major causes for unsatisfactory contribution of income tax to national revenue of Nepal according to tax payer's preference are as follows:-

1. Corruptions
2. Weakness in government's economic policy
3. Complicated tax laws and provisions
4. Lack of coordination within the tax departments
5. Lack of public participation
6. Scarce of income tax expert/professionals in tax administration
7. Defective assessment procedure
8. Inefficient organizational structure of tax administration

Table 4.18
Major Causes which are responsible for unsatisfactory contribution of
Income Tax to the National Revenue of Nepal

Overall view										
S.N.	Major Causes	1	2	3	4	5	6	7	8	Total
a.	Defective assessment procedure	2	1	7	12	12	12	10	4	60
b.	Lack of public participation	7	7	9	9	9	6	8	5	60
c.	Inefficient organizational structure of tax administration	2	5	8	4	10	9	11	11	60
d.	Scarce of income tax expert/ professionals in tax administration	3	4	8	6	9	12	8	10	60
e.	Weakness in government's economic policy	19	15	8	8	1	3	3	3	60
f.	Lack of co-ordination within the tax department	2	5	7	10	10	7	6	13	60
g.	Complicated tax laws and provisions	10	11	4	6	6	4	9	10	60
h.	Corruptions	15	12	9	5	3	7	5	4	60

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.18 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as below.

S.N.	Major Causes	Rank * No. of Responses (W * X)								∑W X	Weighted Mean	Rank
		1	2	3	4	5	6	7	8			
a.	Defective assessment procedure	2	2	2	4	6	7	7	24	299	4.98	5
b.	Lack of public participation	7	1	2	2	4	3	5	40	261	4.35	3
c.	Inefficient organizational structure of tax administration	2	1	2	1	5	5	7	88	321	5.35	8
d.	Scarce of income tax expert/ professionals in tax administration	3	8	2	2	4	7	5	80	312	5.2	7
e.	Weakness in government's economic policy	19	3	2	3	5	1	2	24	173	2.88	1
f.	Lack of co-ordination within the tax department	2	1	2	4	5	4	4	10	311	5.18	6
g.	Complicated tax laws and provisions	10	2	1	2	3	2	6	80	265	4.42	4
h.	Corruptions	15	2	2	2	1	4	3	32	210	3.5	2

Weighted mean for the causes “Weakness in government's economic policy” is the lowest one i.e. 2.88. So it is ranked first. Whereas “inefficient organizational structure

of tax administration” is the highest i.e. 8 so it is ranked last. In general the major causes for unsatisfactory contribution of income tax to national revenue of Nepal according to tax payer’s preference are as follows:-

1. Weakness in government’s economic policy
2. Corruptions
3. Lack of public participation
4. Complicated tax laws and provisions
5. Defective assessment procedure
6. Lack of coordination within the tax departments
7. Scarce of income tax expert/professionals in tax administration
8. Inefficient organizational structure of tax administration

Except these above causes, the respondents were asked to specify any other major causes and some of them specified the major causes in the place provided to write in their words. They are tentatively highlighted consolidating in the following points as the weaknesses and causes of being unsatisfactory contribution of income tax to the national revenue of Nepal.

- Improper tax office culture
- Attitude of government employee towards public demotivate general public to participate in revenue collection process
- Lack of public awareness about income tax and consequences
- Political safety to the corruptors
- Lack of honesty in business sectors
- Under reporting of incomes and transactions by tax payers
- Lack of proper direction for collecting tax
- Social recognition to the wealthy people
- Undue delay in making assessment
- Lack of effective communication for problem solution

In overall, it can be concluded that the factors which are responsible the most for creating unsatisfactory contribution of income tax to national revenue of Nepal is “Weakness in government’s economic policy”.

Some of the respondents verbally suggest that the tax laws need to be simplified so that tax payers become aware, satisfied and motivated to pay tax and they themselves feel proud of it.

4.3.4 Opinion on Current Income Tax Rates

Regarding the opinion on current income tax rates, respondents were requested to tick the best alternatives among three alternatives (high, medium and low). The question was asked, “What is your opinion about the current Income Tax rates?” The respondents’ responses are tabulated as follows in the table 4.19

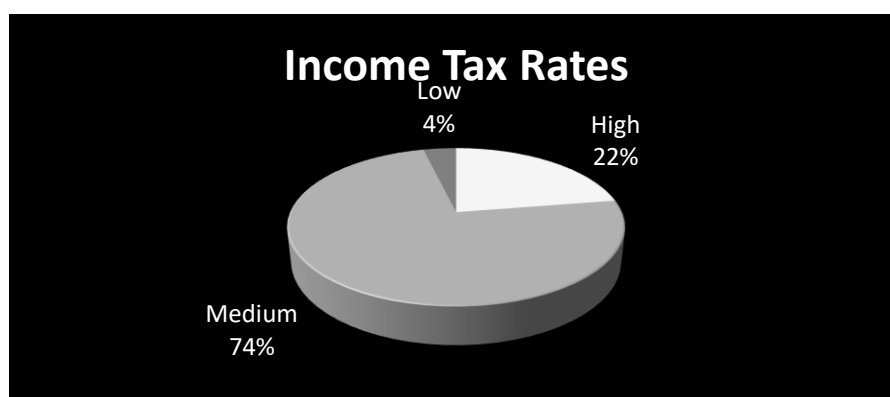
Table 4.19
Opinion on Current Income Tax Rates

S.N.	Tax Rates	Group			Total number	%	Ranking
		A	B	C			
1	High	6	2	10	18	22.5	2
2	Medium	14	25	20	59	73.75	1
3	Low	-	3	-	3	3.75	3
Total		20	30	30	80	100	-

Source: Opinion Survey 2013.

Also it can be presented diagrammatically:

Figure 4.7
Opinion on Current Income Tax Rates



Out of total responses, 73.75 percent of the respondents were agreed that the current income tax rate is medium whereas 22.5 percent of the respondents agreed in high tax rate and only 3.75 percent of the total respondents were agrees on low tax rates. From the above table, it can be concluded that the current income tax rate is not higher in absolute terms but it is higher as compared to tax paying capacity of Nepalese people.

4.3.5 Sufficiency of Tax Exempted Items of Income Tax

ITA, 2058 has provided exemption to the various incomes. The act has clearly pointed the tax exempt organizations which are tax free organizations and the exemption provided to different items of incomes. To know the sufficiency of exempted items of income, a question was asked, “Do you think that the exempted items of incomes are sufficient?” The responses on “Yes” or “No” options were as follows in the table 4.20 and figure 4.8.

Table 4.20

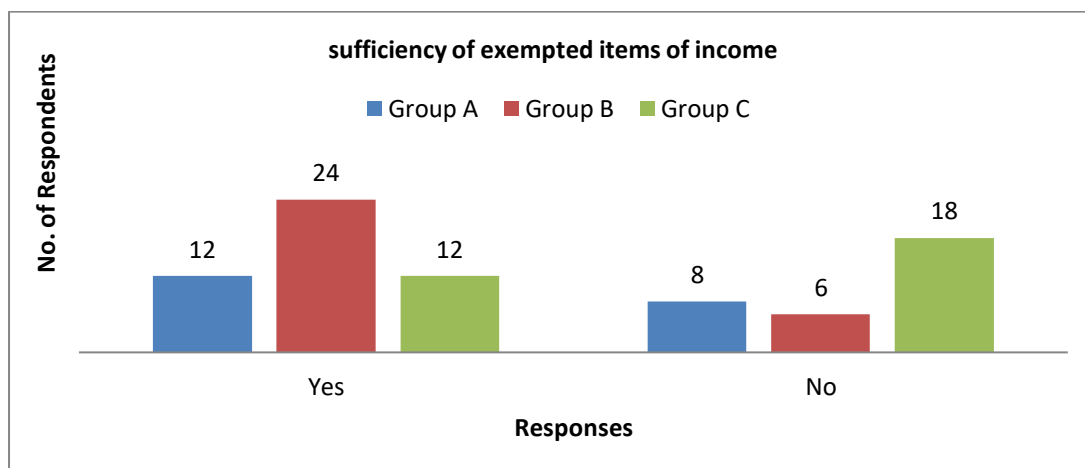
Sufficiency of Exempted Items of Income

Respondents Responses	Groups			Total number	%	Rank
	A	B	C			
Yes	12	24	12	48	60	1
No	8	6	18	32	40	2
Total	20	30	30	80	100	-

Source: Opinion Survey 2013.

Figure 4.8

Sufficiency of Exempted Items of Income



Out of 100% responses received from respondents 60% respondents i.e. 48 respondents were agreed that the exempted items of income are sufficient whereas 40% respondents i.e. 32 respondents were disagreed about the sufficiency of exempted items.

4.3.6 Other incomes that should be Exempted from Tax

Those respondents who gave the responses ‘No’ about the sufficiency of exempted items of incomes were further asked another question, “If no, what kind of incomes should be exempted?” They were requested to rank from 1 to 7 in order of their preference. Responses received have been tabulated and analyzed into four groups:-

1. Tax experts’ view
2. Tax administrators’ view
3. Tax payers’ view
4. Overall view

In order to find out the ranks we used weighted mean separately for each groups as in 4.3.3.

The weighted mean is given by:

$$\bar{X} = \frac{\sum WX}{\sum W}$$

Weighted mean (\bar{X}) is calculated by dividing the total value ($\sum WX$) by the total weight ($\sum W$).

Table 4.21
Incomes that should be exempted from tax

S.N.	Incomes	Tax Experts’ view							Total
		1	2	3	4	5	6	7	
a.	Awards, rewards and scholarship	2	3	1	2	-	-	-	8
b.	Export earnings	1	1	2	-	1	-	3	8
c.	Interest received from government’s bank	-	-	2	3	-	1	2	8
d.	Overtime allowances	2	2	2	-	1	-	1	8
e.	Retirement benefits	2	2	-	2	1	1	-	8
f.	Income from foreign employment	-	-	1	1	1	3	2	8
g.	House rent	1	-	-	-	4	3	-	8

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.21 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Incomes	Rank * No. of Responses (W * X)							ΣW X	Weighted Mean	Rank
a.	Awards, rewards and scholarship	2	6	3	8	-	-	-	19	2.375	1
b.	Export earnings	1	2	6	-	5	-	21	35	4.375	4
c.	Interest received from government's bank	-	-	6	12	-	6	14	38	4.75	5
d.	Overtime allowances	2	4	6	-	5	-	7	24	3	2
e.	Retirement benefits	2	4	-	8	5	6	-	25	3.125	3
f.	Income from foreign employment	-	-	3	4	5	18	14	44	5.5	7
g.	House rent	1	0	0	0	20	18	0	39	4.875	6

Weighted mean for the Income “Awards, rewards and scholarship” is the lowest one i.e. 2.375. So it is ranked first. So as “Income from foreign employment” is the highest i.e. 5.5 so it is ranked last. In general incomes that should be exempted according to tax experts’ preference are as follows:-

1. Awards, rewards and scholarship
2. Overtime allowance
3. Retirement benefits
4. Exports earnings
5. Interest received from government’s Bank
6. House rent
7. Income from foreign employment

Table 4.22
Incomes that should be exempted from tax

Tax Administrators' view

S.N.	Incomes	1	2	3	4	5	6	7	Total
a.	Awards, rewards and scholarship	-	3	1	1	1	-	-	6
b.	Export earnings	-	-	1	1	1	1	2	6
c.	Interest received from government's bank	-	-	2	1	1	2	-	6
d.	Overtime allowances	2	1	1	2	-	-	-	6
e.	Retirement benefits	2	2	-	-	1	-	1	6
f.	Income from foreign employment	-	-	-	-	2	2	2	6
g.	House rent	2	-	1	1	-	1	1	6

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.22 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Incomes	Rank * No. of Responses (W * X)							$\sum W$ X	Weighted Mean	Rank
		1	2	3	4	5	6	7			
a.	Awards, rewards and scholarship	-	6	3	4	5	-	-	18	3	2
b.	Export earnings	-	-	3	4	5	6	14	32	5.33	6
c.	Interest received from government's bank	-	-	6	4	5	12	-	27	4.5	5
d.	Overtime allowances	2	2	3	8	-	-	-	15	2.5	1
e.	Retirement benefits	2	4	-	-	5	-	7	18	3	2
f.	Income from foreign employment	-	-	-	-	10	12	14	36	6	7
g.	House rent	2	-	3	4	-	6	7	22	3.67	4

Weighted mean for the Income "Overtime Allowance" is the lowest one i.e. 2.5. So it is ranked first. So as "Income from foreign employment" is the highest i.e. 6 so it is

ranked last. In general incomes that should be exempted according to tax administrators' preference are as follows:-

1. Overtime allowance
2. Retirement benefits
3. Awards, rewards and scholarship
4. House rent
5. Interest received from government's Bank
6. Exports earnings
7. Income from foreign employment

Table 4.23
Incomes that should be exempted from tax

S.N.	Incomes	Tax Payers' view							Total
		1	2	3	4	5	6	7	
a.	Awards, rewards and scholarship	2	1	2	3	3	5	2	18
b.	Export earnings	4	3	3	2	2	2	2	18
c.	Interest received from government's bank	2	1	3	1	3	3	5	18
d.	Overtime allowances	3	4	4	2	2	1	2	18
e.	Retirement benefits	3	3	2	3	2	3	2	18
f.	Income from foreign employment	1	2	2	4	3	2	4	18
g.	House rent	3	4	2	3	3	2	1	18

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.23 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Incomes	Rank * No. of Responses (W * X)							$\sum W$ X	Weighted Mean	Rank
		2	2	6	12	15	30	14			
a.	Awards, rewards and scholarship	2	2	6	12	15	30	14	81	4.5	5
b.	Export earnings	4	6	9	8	10	12	14	63	3.5	2
c.	Interest received from government's bank	2	2	9	4	15	18	35	85	4.72	7
d.	Overtime allowances	3	8	12	8	10	6	14	61	3.39	1
e.	Retirement benefits	3	6	6	12	10	18	14	69	3.83	4
f.	Income from foreign employment	1	4	6	16	15	12	28	82	4.56	6
g.	House rent	3	8	6	12	15	12	7	63	3.5	2

Weighted mean for the Income “Overtime Allowance” is the lowest one i.e. 3.39. So it is ranked first. So as “Interest received from government’s bank” is the highest i.e. 4.72 so it is ranked last. In general incomes that should be exempted according to tax payers’ preference are as follows:-

1. Overtime allowance
2. House rent
3. Exports earnings
4. Retirement benefits
5. Awards, rewards and scholarship
6. Income from foreign employment
7. Interest Received from government’s bank

Table 4.24
Incomes that should be exempted from tax

Overall view

S.N.	Incomes	1	2	3	4	5	6	7	Total
a.	Awards, rewards and scholarship	4	7	4	6	4	5	2	32
b.	Export earnings	5	4	6	3	4	3	7	32
c.	Interest received from government’s bank	2	1	7	5	4	6	7	32
d.	Overtime allowances	7	7	7	4	3	1	3	32
e.	Retirement benefits	7	7	2	5	4	4	3	32
f.	Income from foreign employment	1	2	3	5	6	7	8	32
g.	House rent	6	4	3	4	7	6	2	32

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.24 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Incomes	Rank * No. of Responses (W * X)							ΣWX	Weighted Mean	Rank
a.	Awards, rewards and scholarship	4	14	12	24	20	30	14	118	3.69	4
b.	Export earnings	5	8	18	12	20	18	49	130	4.06	5
c.	Interest received from government's bank	2	2	21	20	20	36	49	150	4.69	6
d.	Overtime allowances	7	14	21	16	15	6	21	100	3.125	1
e.	Retirement benefits	7	14	6	20	20	24	21	112	3.5	2
f.	Income from foreign employment	1	4	9	20	24	42	56	156	4.875	7
g.	House rent	6	8	9	16	28	36	14	117	3.66	3

Weighted mean for the Income “Overtime Allowance” is the lowest one i.e. 3.125. So it is ranked first. So as “Interest from foreign employment” is the highest i.e. 4.875 so it is ranked last. In general incomes that should be exempted according to overall view are:-

1. Overtime allowance
2. Retirement benefits
3. House rent
4. Awards, rewards and scholarship
5. Exports earnings
6. Interest received from government's Bank
7. Income from foreign employment

Except these above incomes, the respondents were asked to explain any other incomes that should be exempted from tax in the spaces provided. Their answers were:-

Tax Experts

- Provident fund
- Life insurance premium
- Rational exemption to all kinds of incomes

Tax administrators

- Life insurance premium
- Citizen investment fund

Tax payers

- Life insurance premium
- Educational allowances

In overall it can be concluded that the overtime allowances should be exempted from tax. Some of the respondents also verbally suggest that the slab of income on which tax is imposed should be raised.

4.3.7 Adequacy of Current Income Tax Exemption Limit

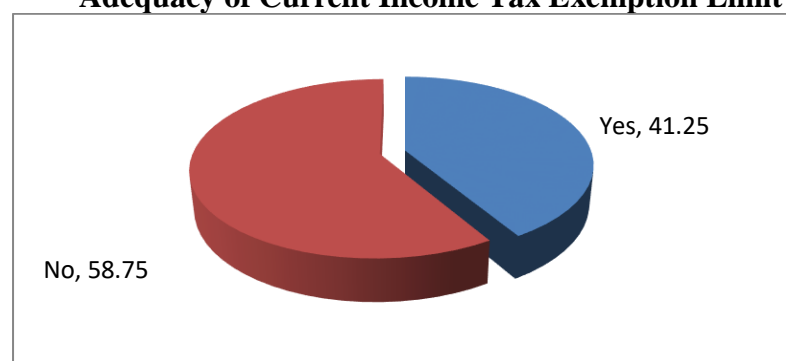
Finance Act of Nepal yearly prescribes the tax rate and exemption limit of income. This year budget speech of 2070/71 prescribed the new exemption limit for an individual and family. To know the respondent's view about the current exemption limit, a question was asked to get the affirmative and negative responses as, "Do you think that the current exemption limit is adequate for individual and couple or a family?" The responses received are tabulated and presented in the table 4.25 and figure 4.9 as follows:-

Table 4.25
Adequacy of Current Income Tax Exemption Limit

Respondents Responses	Group			Total Number	Percent(%)	Rank
	A	B	C			
Yes	8	15	10	33	41.25	2
No	12	15	20	47	58.75	1
Total	20	30	30	80	100	-

Source: *Opinion Survey 2013.*

Figure 4.9
Adequacy of Current Income Tax Exemption Limit



From table 4.25 and figure 4.9, it can be seen that the current income tax exemption limit is inadequate as 58.75 % of respondents i.e. 47 out of 80 respondents were against the sufficiency of current exemption limit whereas 41.25 % of the respondents i.e. 33 out of 80 were for the adequacy of current income tax exemption limit.

4.3.8 Suggestion of Exemption Limit for an individual and couple

The respondents who were against the adequateness of current exemption limit were asked a question, “If no, what exemption limits do you suggest for individual and couple or a family?” The table including current exemption limits providing space to write the limit for individual and couple or a family. The responses received are arranged in the following table 4.26 and 4.27 respectively for individual and for a couple or a family.

Table 4.26
Suggestion of Exemption Limit for an Individual

Respondents Responses	Group			Total number	Percent(%)	Rank
	A	B	C			
Rs. 250000	2	8	6	16	34.04	2
Rs. 300000	6	4	10	20	42.55	1
Rs. 350000	-	3	3	6	12.77	3
Rs. 400000	4	-	1	5	10.64	4
Total	12	15	20	47	100	-

Source: Opinion Survey 2013.

From the table 4.26 that shows that responses about the exemption limit of an individual, it was found that 42.55 percent respondents were in favor of Rs. 3,00,000 whereas 34.04 , 12.77 and 10.64 percent respondents suggested for Rs. 2,50,000, Rs. 3,50,000 and Rs. 4,00,000 respectively.

In accordance to the preference of the respondents, the exemption limit for an individual are ranked as follows:

1. Rs. 3,00,000
2. Rs. 2,50,000
3. Rs. 3,50,000
4. Rs. 4,00,000

From the above in overall, it can be concluded that the exemption limit for an individual should be Rs. 3,00,000.

Table 4.27
Suggestion of Exemption limit for a couple or a family

Respondents Responses	Group			Total number	Percent(%)	Rank
	A	B	C			
Rs. 3,00,000	2	6	3	11	23.40	2
Rs. 3,50,000	2	3	6	11	23.40	2
Rs. 4,00,000	4	4	8	16	34.04	1
Rs. 4,50,000	-	2	2	4	8.52	4
Rs. 5,00,000	2	-	-	2	4.26	6
Rs. 6,00,000	2	-	1	3	6.38	5
Total	12	15	20	47	100	-

Source: Opinion Survey 2013.

From the table 4.27 it is clear that most of the respondents i.e. 34.04 percent suggested for Rs. 4,00,000 as an exemption limit to a family. 11 out of 47 respondents suggested Rs 3, 00, 000 and same number of respondents suggested Rs.3,50,000 as an exemption limit. Similarly 8.52, 6.38 and 4.26 percent respondents suggested Rs. 4,00,000, Rs, 6,00,000 and Rs. 5,00,000. In accordance to the preference of respondents, the exemption limit for a couple or a family is ranked as follows:

1. Rs. 400000
2. Rs. 3,00,000
3. Rs. 3,50,000
4. Rs. 4,50,000
5. Rs. 6,00,000
6. Rs. 5,00,000

So, it can be concluded that family exemption limit should be increased to Rs. 4,00,000. On the personal discussion with the respondents it was found that some of the respondents were in support to provide tax exemption limit equivalent to annual remuneration income of a government employed section officers. Some also personally suggest that some single individuals are taking the benefits of family exemption limit which should be properly checked.

4.3.9 Exemption Limit according to the Inflationary Situation of the country

In the similar way, one question was asked to know the opinion of respondents about the adjustment of exemption limit according to the inflationary situation of the country. The question asked was, “Do you agree that exemption limit should be adjusted according to the inflationary situation of the country?” The responses received were tabulated as below:-

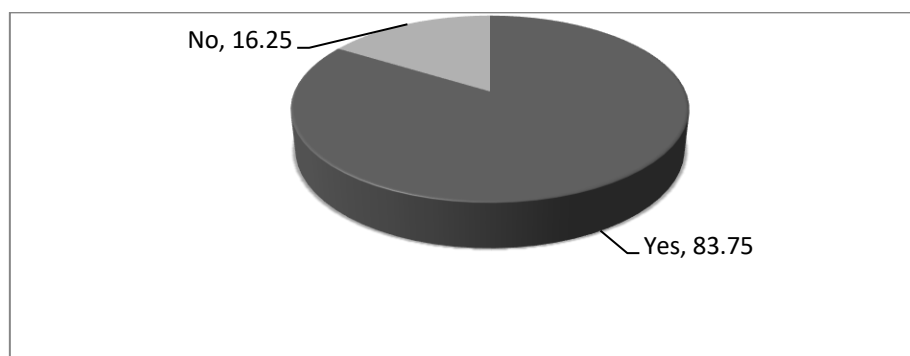
Table 4.28
Exemption Limit according to the Inflationary Situation of the country

Respondents Responses	Group			Total number	Percent(%)	Rank
	A	B	C			
Yes	20	22	25	67	83.75	1
No	-	8	5	13	16.25	2
Total	20	30	30	80	100	-

Source: *Opinion Survey 2013*.

Responses received from respondents are shown diagrammatically as below:

Figure 4.10
Exemption Limit according to the Inflationary situation of the country



The table 4.28 and figure 4.10 show that 83.75 percent of the total respondents were agreed to adjust the exemption limit according to the inflationary situation of the country whereas only 16.25 percent were disagreed about it. They believed that this situation makes tax administration more complicated and vague. The fiscal policy may provide tax relief to accommodate inflation if provisioned.

4.3.10 Family Exemption Limit According to the Number of Dependents

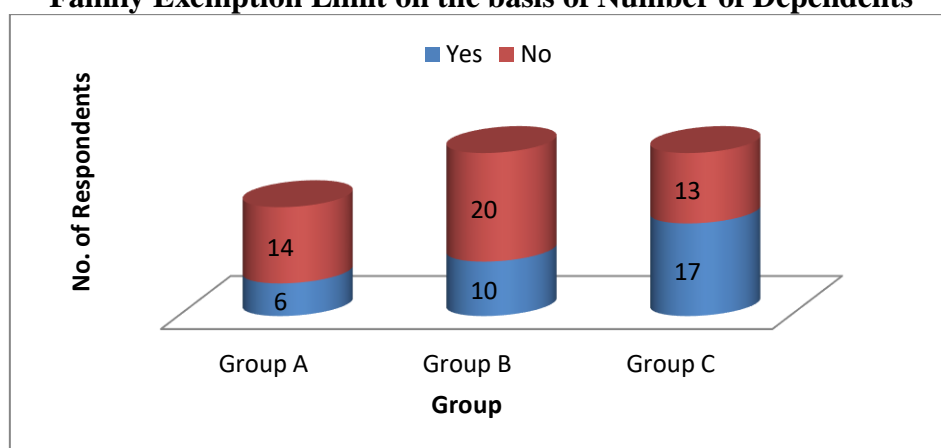
ITA has provided exemption limit to a family. But it has not defined the number of dependents within a family. So, to know the opinion about the exemption limit of a family according to the number of dependents, a question was asked, “Do you agree that family exemption must be provided according to the number of dependents?” The responses received were as follows:-

Table 4.29
Family Exemption Limit on the basis of Number of Dependents

Respondents Responses	Group			Total number	Percent(%)	Rank
	A	B	C			
Yes	6	10	17	33	41.25	2
No	14	20	13	47	58.75	1
Total	20	30	30	80	100	-

Source: Opinion Survey 2013.

Figure 4.11
Family Exemption Limit on the basis of Number of Dependents



The table 4.29 shows that 58.75 percent of the total respondents i.e. 47 out of the 80 respondents disagreed on providing exemption on the basis of number of dependents whereas 41.25 percent of the respondents agreed that the family exemption limit must be provided according to the number of dependents. The majority of respondents of group ‘A’ and ‘B’ were disagreed but group ‘C’ were agreed on providing the family exemption limit according to the number of dependents in families. To provide

exemption on the basis of number of dependents is difficult to execute because it is impossible to apply in real field.

4.3.11 Opinion on providing Exemption Limit on Agricultural Income

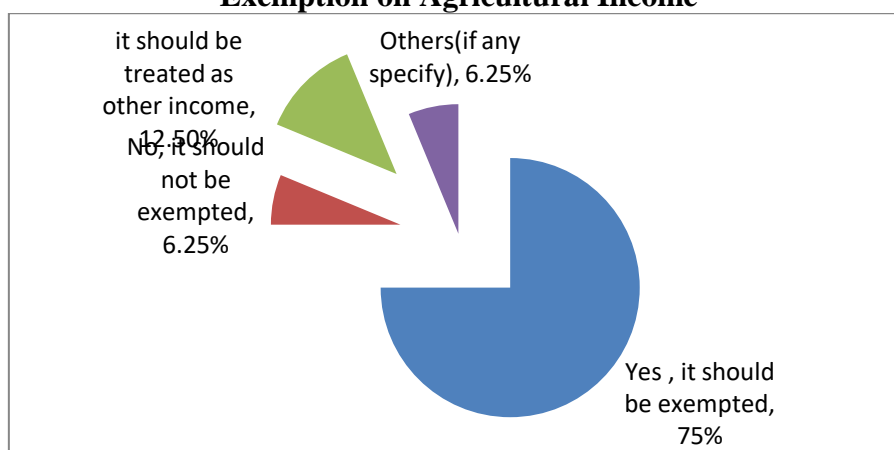
After commencement of ITA, agricultural income has been treated as taxable income in some time in a specific case and sometime as exempted income too. The new ITA has exempted tax on agricultural income other than agricultural business. To know the opinion on it one question was asked as, “What is your opinion on exemption on agricultural income?” The respondents were given four options to choose the most appropriate answer. The table 4.30 gives the breakdown of the responses:-

Table 4.30
Exemption on Agricultural Income

Respondents Responses	Group			Total number	Percent (%)	Rank
	A	B	C			
Yes, it should be exempted	14	24	22	60	75	1
No, it shouldn't be exempted	2	1	2	5	6.25	3
It should be treated as other income	2	4	4	10	12.5	2
Others if any, specify	2	1	2	5	6.25	3
Total	20	30	30	80	100	-

Source: Opinion Survey 2013.

Figure 4.12
Exemption on Agricultural Income



From the table 4.30, it is clear that the 75 percent of the total respondents were in support to exempt the agricultural income whereas 6.25 percent of the total respondents were against this exemption. 12.5 percent of the respondents were in favor to treat it as other income. Only 5 out of 80 respondents i.e. 2 from group ‘A’, 1 from group ‘B’ and 2 from group ‘C’ specified their responses as other options as the suggestions which are mentioned as follows:-

- Must be covered by increasing exemption limit.
- Rich farmers should be taxed.
- A practical arrangement for taxing agriculture should be formulated, for e.g. based on the size of landholding.

4.3.12 Sufficiency about the Itemized Deductions:

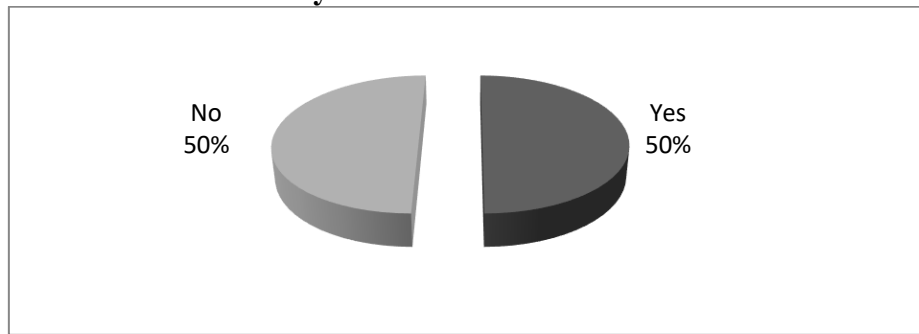
There are different practices around the world regarding deductions for the purpose of Income Tax. Some countries adopt an itemized system of deduction like in Nepal. Under that system, deductible and non deductible items are specified in the law. Under this system no deductions is allowed unless a particular expenses is specifically included in the list of deductible expenses. ITA, 2058 has provided different kinds of expenses as deductions. Some expenses are allowed for deduction as itemized deductions and some are standard deduction. In order to know the attitude toward the item-wise deduction of expenses, a question was asked as, “Do you think that the itemized deductions are sufficient?” The responses received are tabulated as in the table 4.31:-

Table 4.31
Sufficiency about the Itemized Deductions

Responses	Respondents			Total number	Percent (%)	Rank
	A	B	C			
Yes	10	20	10	40	50	1
No	10	10	20	40	50	1
Total	20	30	30	80	100	-

Source: Opinion Survey 2013.

Figure 4.13
Sufficiency about the Itemized Deductions



Out of the total responses received 50 percent of the respondents were against the sufficiency of itemized deductions whereas 50 percent of the respondents said that existing provision of itemized deductions are sufficient. Majority of tax administrators were in support for itemized deduction and majority of tax payer were against it. Some tax experts also informed verbally that ITA of Nepal has provided more facilities about itemized deductions in comparison to other countries.

4.3.13 Other Expenses that should be Deducted while Computing Taxable Income

The respondents who were against the sufficiency about itemized deductions were further asked another question as, “If no, what kind of other expenses should be deducted while computing taxable income?” The respondents were given seven options and asked to rank them in order of their preferences. The responses received were analyzed and tabulated in four groups:-

1. Tax Experts’ view
2. Tax Administrators’ view
3. Tax payers’ view
4. Overall view

In order to find out the ranks we used weighted mean separately for each groups as in 4.3.3.

The weighted mean is given by:

$$\bar{X} = \frac{\sum wX}{\sum w}$$

Weighted mean (\bar{X}) is calculated by dividing the total value ($\sum WX$) by the total weight ($\sum W$).

Table 4.32
Expenses to be Deducted While Computing Taxable Income

S.N.	Expenses	Tax experts' view							Total
		1	2	3	4	5	6	7	
a.	Educational expenses/allowances	5	3	2	-	-	-	-	10
b.	Traveling expenses/allowances	1	-	3	2	-	2	2	10
c.	House rent	-	-	4	2	1	2	1	10
d.	Tiffin allowances	-	-	1	-	1	2	6	10
e.	Medical expenses on the basis of bills	4	3	-	-	3	-	-	10
f.	Full deduction of repair and maintenance expenses	-	3	-	3	2	2	-	10
g.	Full deduction of depreciation	-	1	-	3	3	2	1	10

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.32 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N	Expenses	Rank * No of Responses							$\sum WX$	Weighted Mean	Rank
		(W * X)									
a.	Educational expenses/allowances	5	6	6	0	0	0	0	17	1.7	1
b.	Traveling expenses/allowances	1	-	9	8	0	12	7	44	4.4	4
c.	House rent	-	-	12	8	5	12	7	44	4.4	4
d.	Tiffin allowances	-	-	3	-	5	12	42	62	6.2	7
e.	Medical expenses on the basis of bills	4	6	-	-	15	-	-	25	2.5	2
f.	Full deduction of repair and maintenance expenses	-	6	-	12	10	12	-	40	4	6
g.	Full deduction of depreciation	-	2	-	12	15	12	7	48	4.8	3

The expenses that should be made deductible while computing taxable income in accordance to the preference of tax experts are ranked as follows:-

1. Educational expenses/allowances
2. Medical expenses on the basis of bills
3. Full deduction of depreciation
4. House rent
5. Traveling expenses/allowances
6. Full deduction of repair and maintenance expenses
7. Tiffin allowances

Table 4.33
Expenses to be deducted while computing Taxable Income

		Tax administrators' view							
S.N.	Expenses	1	2	3	4	5	6	7	Total
a.	Educational expenses/allowances	2	1	2	3	2	-	-	10
b.	Traveling expenses/allowances	1	2	3	1	1	1	1	10
c.	House rent	3	1	1	2	1	2	-	10
d.	Tiffin allowances	2	-	-	1	3	2	2	10
e.	Medical expenses on the basis of bills	2	3	2	1	2	-	-	10
f.	Full deduction of repair and maintenance expenses	-	2	1	1	-	2	4	10
g.	Full deduction of depreciation	-	1	1	1	1	3	3	10

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.33 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Expenses	Rank * No of Responses (W * X)							ΣWX	Weighted Mean	Rank
a.	Educational expenses/allowances	2	2	6	12	10	-	-	22	2.2	1
b.	Traveling expenses/allowances	1	4	9	4	5	6	7	36	3.6	4
c.	House rent	3	2	3	8	5	12	-	33	3.3	3
d.	Tiffin allowances	2	-	-	4	15	12	14	47	4.7	5
e.	Medical expenses on the basis of bills	2	6	6	4	10	-	-	28	2.8	2
f.	Full deduction of repair and maintenance expenses	-	4	3	4	-	12	28	51	5.1	6
g.	Full deduction of depreciation	-	2	3	4	5	18	21	53	5.3	7

The expenses that should be made deductible while computing taxable income in accordance to the preference of tax administrators are ranked as follows:-

1. Educational expenses/allowances
2. Medical expenses on the basis of bills
3. House rent
4. Traveling expenses/allowances
5. Tiffin allowances
6. Full deduction of repair and maintenance expenses
7. Full deduction of depreciation

Table 4.34

Expenses to be deducted while computing Taxable Income

Tax payers' view

S.N.	Expenses	1	2	3	4	5	6	7	Total
a.	Educational expenses/allowances	9	4	1	3	1	2	-	20
b.	Traveling expenses/allowances	2	3	3	5	2	3	2	20
c.	House rent	3	6	5	3	2	1	-	20
d.	Tiffin allowances	-	-	3	2	3	4	8	20
e.	Medical expenses on the basis of bills	3	5	6	3	3	-	-	20
f.	Full deduction of repair and maintenance expenses	1	-	2	2	5	5	5	20
g.	Full deduction of depreciation	2	2	-	2	4	5	5	20

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.34 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Expenses	Rank * No of Responses (W *X)							ΣWX	Weighted Mean	Rank
a.	Educational expenses/allowances	9	8	3	12	5	12	-	49	2.45	1
b.	Traveling expenses/allowances	2	6	9	20	10	18	14	79	3.95	4
c.	House rent	3	12	15	12	10	6	-	58	2.9	2
d.	Tiffin allowances	-	-	9	8	15	24	56	112	5.6	7
e.	Medical expenses on the basis of bills	3	10	18	12	15	-	-	58	2.9	2
f.	Full deduction of repair and maintenance expenses	1	-	6	8	25	30	35	105	5.25	6
g.	Full deduction of depreciation	2	4	-	8	20	30	35	99	4.95	5

The expenses that should be made deductible while computing taxable income in accordance to the preference of tax payers are ranked as follows:-

1. Educational expenses/allowances
2. House rent
3. Medical expenses on the basis of bills
4. Traveling expenses/allowances
5. Full deduction of depreciation
6. Full deduction of repair and maintenance expenses
7. Tiffin allowances

Table 4.35
Expenses to be deducted while computing Taxable Income

S.N.	Expenses	Overall view							
		1	2	3	4	5	6	7	Total
a.	Educational expenses/allowances	16	8	5	6	3	2	-	40
b.	Traveling expenses/allowances	4	5	9	8	3	6	5	40
c.	House rent	6	7	10	7	4	5	1	40
d.	Tiffin allowances	2	-	4	3	7	8	16	40
e.	Medical expenses on the basis of bills	9	11	8	4	8	-	-	40
f.	Full deduction of repair and maintenance	1	5	3	6	7	9	9	40
g.	Full deduction of depreciation	2	4	1	6	8	10	9	40

Source: Opinion Survey 2013.

Further we used the information tabulated in table no. 4.35 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Expenses	Rank * No of Responses (W *X)							$\sum WX$	Weighted Mean	Rank
a.	Educational expenses/allowances	16	16	15	24	15	12	-	98	2.45	1
b.	Traveling expenses/allowances	4	10	27	32	15	36	35	159	3.975	4
c.	House rent	6	14	30	28	20	30	7	135	3.375	3
d.	Tiffin allowances	2	-	12	12	35	48	112	221	5.525	7
e.	Medical expenses on the basis of bills	9	22	24	16	40	-	-	111	2.775	2
f.	Full deduction of repair and maintenance expenses	1	10	9	24	35	54	63	196	4.9	5
g.	Full deduction of depreciation	2	8	3	24	40	60	63	200	5	6

The expenses that should be made deductible while computing taxable income in accordance to the preference of all respondents in overall are:-

1. Educational expenses/allowances
2. Medical expenses on the basis of bills
3. House rent
4. Traveling expenses/allowances
5. Full deduction of repair and maintenance expenses
6. Full deduction of depreciation
7. Tiffin allowances

Except these above causes, the respondents were asked to write any other expenses that should be made included in itemized deductions while computing taxable income in the place provided to write in their own words. Only few respondents responses which are explained below:-

- SEZ should be created and alternative tax administration, exemption allowed for industries, processing units, infrastructure development projects in such regions.

- Delivery expenses

In overall we can conclude that the educational expenses/allowances should be made deductible while computing taxable income.

4.3.14 Awareness about the Provision of IT Exemptions and Deductions

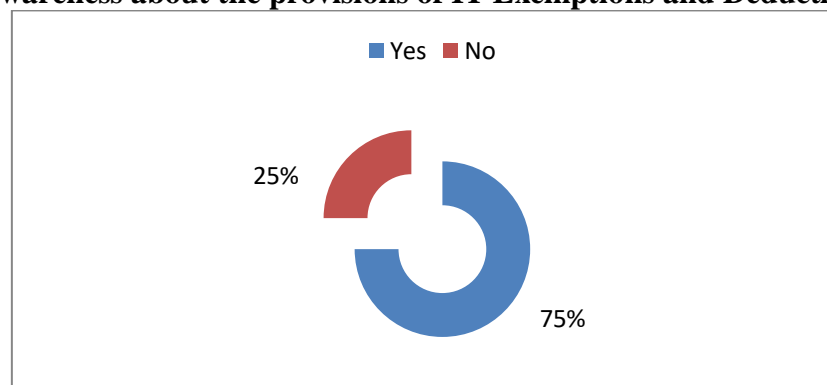
ITA 2058 has provided different provisions regarding exemptions and deductions. To know awareness of respondents about the provision of tax exemption and deduction, a question was asked, “Are you aware about the provision of IT exemptions and deductions as per ITA, 2058 of Nepal?” The responses are tabulated below:

Table 4.36
Awareness about the provisions of IT Exemptions and Deductions

Respondents Responses	Groups			Total number	Percent(%)	Rank
	A	B	C			
Yes	20	30	10	60	75	1
No	-	-	20	20	25	2
Total	20	30	30	80	100	-

Source: Opinion Survey 2013.

Figure 4.14
Awareness about the provisions of IT Exemptions and Deductions



Cent percent responses were received from respondents. Out of 80 respondents, 75% i.e. 60 respondents were aware about the provision of tax exemption and deduction as per ITA, 2058 of Nepal but still 25% of respondents were not aware about the exemptions and deductions facilities as provided in ITA.

As who gave the negative responses about awareness of provisions of IT exemptions and deductions were asked another question, “What are the causes or possible reason of it?” The responses were as below:-

Table 4.37
Reason for unawareness about the provision of tax exemptions and deductions

S.N.	Alternatives	Group			Total number	Percent (%)	Rank
		A	B	C			
1	Different provisions regarding exemptions and deductions	-	-	10	10	50	1
2	Tax Office also in dilemma in this regard	-	-	6	6	30	2
3	I don't think it's necessary	-	-	4	4	20	3
	Total	-	-	20	20	100	-

Source: Opinion Survey 2013.

In the table 4.37, we can see that 50 percent of the respondents who were unaware about such provisions are because of different provisions regarding exemptions and deductions. Respondents ranked the main cause of being unaware about the provision of tax exemptions and deductions as per ITA, 2058 of Nepal in the following way:-

1. Different provisions regarding exemptions and deductions
2. Tax office also in dilemma in this context
3. I don't think it is necessary

4.3.15 Sufficiency of Provisions relating to Exemptions and Deductions under Nepalese ITA

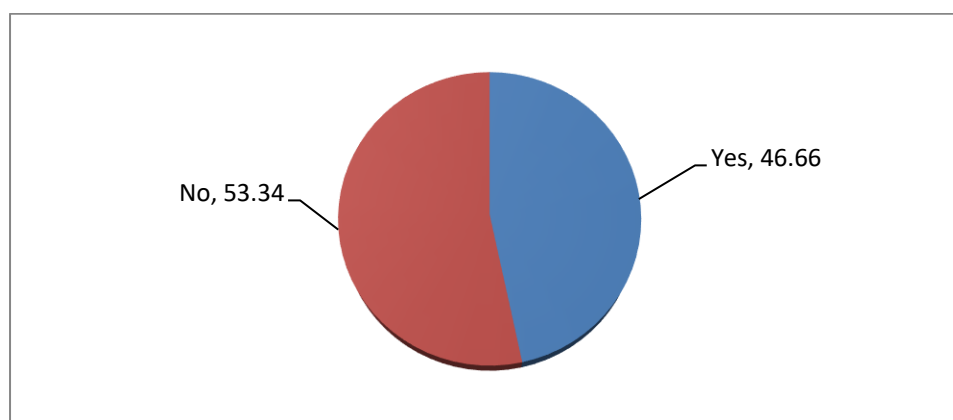
In order to know the sufficiency of provisions related to exemptions and deductions under the Nepalese ITA, respondents who said they were aware of the related provisions were asked a question as, “In your opinion, are the provisions relating to exemptions and deductions under Nepalese ITA, 2058 sufficient in all aspects?” The respondents were asked to answer in “Yes”, “No” alternatives. The responses received on it are tabulated as below:-

Table 4.38
Sufficiency of Provisions relating to Exemptions and Deductions under the
Nepalese ITA

Respondents Responses	Group			Total number	Percent(%)	Rank
	A	B	C			
Yes	5	20	3	28	46.66	2
No	15	10	7	32	53.34	1
Total	20	30	10	60	100	-

Source: Opinion Survey 2013.

Figure 4.15
Sufficiency of Provisions relating to Exemptions and Deductions under the
Nepalese ITA



From the table 4.38 it is clear that out of 60 respondents who were aware about the provisions relating to tax exemptions and deductions 46.66 percent i.e. 28 respondents were agreed about the sufficiency of provisions relating to exemptions and deductions. Whereas remaining 53.34 percent i.e. 32 respondents were against the sufficiency of provisions relating to exemptions and deductions under Nepalese ITA. From the above it can be concluded that majority of the respondents were against the sufficiency.

4.3.16 Improvements needed in the provisions

The respondents who gave negative responses about the sufficiency of provisions relating to exemptions and deductions under the ITA, 2058 were further asked a question as, “If No, in which aspect the improvements are needed?” Respondents

were requested to rank the given option in the order of their preference from one to seven, one being the most preferred and seven being the least preferred. The responses received were analyzed and tabulated into four groups:-

1. Tax experts' view
2. Tax administrators' view
3. Tax payers' view
4. Overall view

In order to find out the ranks we used weighted mean separately for each groups as in 4.3.3.

The weighted mean is given by:

$$\bar{X} = \frac{\sum WX}{\sum W}$$

Weighted mean (\bar{X}) is calculated by dividing the total value ($\sum WX$) by the total weight ($\sum W$).

Table 4.39
Improvement needed in the provisions

S.N.	Aspects	Tax experts' view							Total
		1	2	3	4	5	6	7	
a.	Tax laws should be simplified	4	4	2	2	1	1	1	15
b.	Improvement in accounting system	1	3	2	3	1	2	3	15
c.	Computerized system in all tax offices	2	-	3	-	2	6	2	15
d.	Remove complicated provisions	4	3	2	2	4	-	-	15
e.	Exemption limit on the basis of market price	2	2	3	2	1	2	3	15
f.	Tax base should be enlarged	2	2	2	3	2	1	3	15
g.	Functional system	-	1	1	3	4	3	3	15

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.39 to calculate the weighted mean and ranking analysis where X denotes for no. of rank and W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Aspects	Rank * No of Responses (W *X)							ΣWX	Weighted Mean	Rank
a.	Tax laws should be simplified	4	8	6	8	5	6	7	44	2.93	1
b.	Improvement in accounting system	1	6	6	12	5	12	21	63	4.2	5
c.	Computerized system in all tax offices	2	-	9	-	10	36	14	71	4.73	6
d.	Remove complicated provisions	4	6	6	8	20	-	-	44	2.93	1
e.	Exemption limit on the basis of market price	2	4	9	8	5	12	21	61	4.07	3
f.	Tax base should be enlarged	2	4	6	12	10	6	21	61	4.07	3
g.	Functional system	-	2	3	12	20	18	21	76	5.07	7

Weighted mean for the aspects “Remove complicated provisions” is the lowest one i.e. 2.93. So it is ranked first. So as “Functional system” is the highest i.e. 5.07 so it is ranked last. Following is the arrangement of aspects that need to be improved according to the choice of tax expert:-

1. Tax laws should be simplified
2. Remove complicated provisions
3. Exemption limit on the basis of market price
4. Tax base should be enlarged
5. Improvement in accounting system
6. Computerized system in all tax offices
7. Functional system

Table 4.40
Improvement needed in the provisions

Tax Administrators' view

S.N.	Aspects	Tax Administrators' view							Total
		1	2	3	4	5	6	7	
a.	Tax laws should be simplified	2	1	-	2	4	1	-	10
b.	Improvement in accounting system	-	-	3	3	2	1	1	10
c.	Computerized system in all tax offices	1	1	2	1	1	3	1	10
d.	Remove complicated provisions	3	2	2	-	2	1	-	10
e.	Exemption limit on the basis of market price	-	2	1	3	-	4	-	10
f.	Tax base should be enlarged	4	3	2	-	1	-	-	10
g.	Functional system	-	1	-	1	-	-	8	10

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.40 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Aspects	Rank * No of Responses							$\sum WX$	Weighted Mean	Rank
		(W * X)									
a.	Tax laws should be simplified	2	2	-	8	20	6	-	38	3.8	3
b.	Improvement in accounting system	-	-	9	12	10	6	7	44	4.4	6
c.	Computerized system in all tax offices	1	2	6	4	5	18	7	43	4.3	5
d.	Remove complicated provisions	3	4	6	-	10	1	-	24	2.4	2
e.	Exemption limit on the basis of market price	-	4	1	12	-	24	-	41	4.1	4
f.	Tax base should be enlarged	4	6	6	-	5	-	-	21	2.1	1
g.	Functional system	-	2	-	4	-	-	56	62	6.2	7

Weighted mean for the aspects “Tax base should be enlarged” is the lowest one i.e. 2.1. So it is ranked first. So as “Functional system” is the highest i.e. 6.2 so it is ranked last. Following is the arrangement of aspects that need to be improved according to the choice of tax administrators:-

1. Tax base should be enlarged
2. Remove complicated provisions
3. Tax laws should be simplified
4. Exemption limit on the basis of market price
5. Computerized system in all tax offices
6. Improvement in accounting system
7. Functional system

Table 4.41
Improvement needed in the provisions

S.N.	Aspects	Tax payers' view							Total
		1	2	3	4	5	6	7	
a.	Tax laws should be simplified	2	1	1	2	1	-	-	7
b.	Improvement in accounting system	-	1	2	2	1	-	1	7
c.	Computerized system in all tax offices	-	1	1	3	1	1	-	7
d.	Remove complicated provisions	4	2	1	-	-	-	-	7
e.	Exemption limit on the basis of market price	-	1	1	-	2	3	-	7
f.	Tax base should be enlarged	1	1	1	-	2	1	1	7
g.	Functional system	-	-	-	-	-	2	5	7

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.41 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Aspects	Rank * No of Responses (W * X)							ΣWX	Weighted Mean	Rank
a.	Tax laws should be simplified	2	2	3	8	5	-	-	20	2.86	2
b.	Improvement in accounting system	-	2	6	8	5	-	7	20	2.86	2
c.	Computerized system in all tax offices	-	2	3	12	5	6	-	28	4	4
d.	Remove complicated provisions	4	4	3	-	-	-	-	11	1.57	1
e.	Exemption limit on the basis of market price	-	2	3	-	10	18	-	33	4.71	6
f.	Tax base should be enlarged	1	2	3	-	10	6	7	29	4.14	5
g.	Functional system	-	-	-	-	-	12	35	47	6.71	7

Weighted mean for the aspects “Remove complicated provisions” is the lowest one i.e. 1.57. So it is ranked first. So as “Functional system” is the highest i.e. 6.71 so it is ranked last. Following is the arrangement of aspects that need to be improved according to the choice of tax payers:-

1. Remove complicated provisions
2. Tax laws should be simplified
3. Improvement in accounting system
4. Computerized system in all tax offices
5. Tax base should be enlarged
6. Exemption limit on the basis of market price
7. Functional system

Table 4.42
Improvement needed in the provisions

S.N.	Aspects	Overall view							Total
		1	2	3	4	5	6	7	
a.	Tax laws should be simplified	8	6	3	6	6	2	1	32
b.	Improvement in accounting system	1	4	7	8	4	3	5	32
c.	Computerized system in all tax offices	3	2	6	4	4	10	3	32
d.	Remove complicated provisions	11	7	5	2	6	1	-	32
e.	Exemption limit on the basis of market price	2	5	5	5	3	9	3	32
f.	Tax base should be enlarged	7	6	5	3	5	2	4	32
g.	Functional system	-	2	1	4	4	5	16	32

Source: Opinion Survey 2013.

Further we used the information tabulated in table 4.42 to calculate the weighted mean and ranking analysis where X denotes for no. of rank, W denotes for no. of individual responses. Weighted mean was formulated and tabulated as follows:-

S.N.	Aspects	Rank * No of Responses (W * X)							ΣWX	Weighted Mean	Rank
		1	2	3	4	5	6	7			
a.	Tax laws should be simplified	8	12	9	24	30	12	7	102	3.1875	2
b.	Improvement in accounting system	1	18	21	32	20	18	35	135	4.219	4
c.	Computerized system in all tax offices	3	4	18	16	20	60	21	142	4.44	6
d.	Remove complicated provisions	11	14	15	8	30	6	-	84	2.625	1
e.	Exemption limit on the basis of market price	2	10	15	20	15	54	21	137	4.281	5
f.	Tax base should be enlarged	7	12	15	12	25	12	28	111	3.469	3
g.	Functional system	-	4	5	16	20	30	224	299	9.34	7

Weighted mean for the aspects “Remove complicated provisions” is the lowest one i.e. 2.625. So it is ranked first. So as “Functional system” is the highest i.e. 9.34 so it is ranked last. Following is the arrangement of aspects that need to be improved in overall:-

1. Remove complicated provisions
2. Tax laws should be simplified
3. Tax base should be enlarged
4. Improvement in accounting system
5. Exemption limit on the basis of market price
6. Computerized system in all tax offices
7. Functional system

Except these seven aspects respondents were also asked to specify other aspects to be improved in the place provided to write in their words. They are tentatively highlighted consolidating in the following points as the aspects to be improved in the current provision about exemptions and deductions.

- Tax rates
- Payment system
- Tax administration
- Monitoring unit
- Depreciation allowance should be simplified
- Language
- All rental incomes of the landlords or in urban areas should be brought into tax net by determining the minimum rent that could be collected from the tenant by the house owner, excess of the rent should be taxed using appropriate rate.

From the analysis of different aspects for improvement, most of the respondents have suggested to remove complicated provisions and simplify the tax laws. Also tax administration should be improved.

4.3.17 Suggestion about Income Tax in Nepal

ITA, 2058 is better than ITA, 2031 but this new act is not free from weakness and vague and complicated language used. So the respondents were requested to write suggestions about income tax in Nepal in open ended questionnaire in the blank space available. The question asked was, “Do you have any suggestions about income tax in Nepal?” Only few respondents of all kinds of group have given the suggestions which are given below:-

1. Tax laws should be simplified, easily interpreted, understood and need to cater needs of economic situation of Nepal.

2. There should be a system where bank transactions above certain threshold (say Rs. 1,00,000) be linked with PAN of each individual. Activities like purchase of bike, air travel etc must also be linked with PAN. These measures will help to make tax net bigger which will increase the revenue.
3. Corruptions need to be controlled. It should not be considered in any case.
4. Provision should be made so as to increase the cooperation of tax officer towards public/tax payer.
5. Exemptions and deductions should be provided to the investment made in hydropower and other development sectors.
6. Group of experts should be formed for the interpretation of current tax provisions for the facility of general public.
7. There is a scheduler tax system that is disadvantageous for investment. For e.g. rental income for natural person is taxed at 10%, interest at 5% whereas dividend income after 15% addition 5% tax is levied.
8. There is no provision for indexation of capital gain. Capital gain tax should be simplified.
9. Too many incentives are provided for which are rarely used.
10. Tax administration is discretionary creating harassment for genuine tax payers rather than making it taxpayer friendly and reducing compliance cost.
11. General public should be motivated for contribution to tax through law. The pros and cons should be explained well to the public.
12. Needs ample directives as well as procedure manuals to make tax administration easy and transparent.
13. Public awareness is needed and political commitment and credibility should be increased.
14. Starting court cases to evading people/entity.
15. Compulsory declaration of assets of each individual.
16. Punishment should be given for not paying tax to the government.
17. Motivate and reward early tax payers.
18. Reduce tax evasion and loopholes through proper law.
19. Monitoring and evaluation of laws and regulations.
20. Flow information downward regarding IT.
21. IT in Nepal is somewhat a mixture of some developed countries. So it should be made in accordance to the context of developing countries.

4.4 Major Findings

According to preceding chapters some important findings can be drawn. These major findings of this research are summarized below:

1. The composition of the government revenue is internal revenue and external revenue. Internal revenue includes both tax revenue and non-tax revenue. Tax revenue is dominating to non-tax revenue of Nepalese government. The contribution of tax revenue is fluctuating which contributed 77.96% in 2001/02, 77.16% in 2004/05, 79.12% in 2007/08 and 86.47% in 2010/11 on the total revenue.
2. The total tax revenue, non-tax revenue and total revenue collected were Rs. 842341.5 million, Rs. 18595.34 million and Rs. 1028294.9 million respectively whereas average percentage collected tax revenue and non-tax revenue were 80.197% and 19.803% respectively during the study period of 10 years.
3. The average collection of direct tax and indirect tax were Rs. 22722.58 million and Rs. 61511.57 million respectively and the average percentage of direct tax and indirect tax on total revenue were 26.475% and 73.525% respectively during the study period.
4. The average tax collection in indirect tax viz. custom duties, excise duties, VAT and others during the study periods were Rs. 20746.78 million, Rs. 11436.11 million, Rs. 29289.87 million and Rs. 38.81 million respectively and average percentage on total indirect tax were 36.091%, 17.182%, 46.694% and 0.033% respectively.
5. The average collection in direct tax viz. income tax, land tax, house and land registration tax, property tax and others tax during the study periods of ten years were Rs. 17600.02, Rs. 0.08, Rs. 2691.77, Rs.1270.39, Rs. 1160.32 million respectively whereas average percentage on the same were 78.38, 0.001, 12.025, 5.465, 4.027 percent respectively.
6. The average percentage of direct tax on tax revenue, GDP and total revenue were 26.481, 2.705 and 21.259 percent respectively during the study periods of ten years.

7. The average percentage collection of income tax on direct tax, tax revenue, total revenue and GDP were 78.482, 20.78, 16.666 and 2.112 percent respectively during the study period.
8. Nepalese tax revenue is the composition of direct and indirect tax. But there is dominant role of indirect tax revenue. The contribution of direct and indirect tax revenue were 26.94% and 73.06% respectively in 2001/02 whereas 28.16% and 71.84% in 2010/11. It shows that contribution of direct tax is in increasing trend (i.e. 26.94% to 28.16%) whereas contribution of indirect tax is in decreasing trend (i.e. 73.66% to 71.84%).
9. The tax revenue on GDP (i.e. tax/GDP ratio) of Nepal is not satisfactory. It has never exceeded 14% from 2001/02 to 2010/11. In 2001/02 it was only 8.6%, which exceeded to 12.56% in 2010/11. This shows the increasing trend of tax\GDP ratio in slower pace.
10. Income tax is the composition of income tax from government sectors, public sectors, private sectors, remuneration and income tax from interest. The average contribution of income tax from government sectors, public sectors, private sectors, remunerations, interest were 10.606, 30.149, 38.339, 13.352 and 7.554 percent respectively.
11. Among the various sources of the government revenue custom duty, VAT, income tax and excise duty are the major sources of government revenue.
12. All incomes generated by an individual are not taxable income because the minimum cost expenses required for living cannot be taxed. So, from the commencement of income tax in Nepal, some extents of amounts are exempted from tax. The extent is known as exemption limit. Income tax exemption in Nepal has been changing on the basis of time and condition. In the fiscal year 2007/08, the exemption limit for the individual and family were Rs. 115000 and Rs. 140000 respectively. In the year 2008/09, the exemption limit was extended as per the time and condition up to Rs. 160000 for an individual and Rs. 200000 for a family and a couple. Budget of 2070/71 has recently increased this limit to Rs. 200000 and Rs. 250000 respectively where 1% tax is levied on those ceiling amount according to this provision. The exemption limit has not been provided to partnership firms, corporations and non-residents.

13. The income tax rates and slabs have been changing radically in recent years. Personal income taxes, which ranged from 7% to 60% in seven slabs in 1975/76, which was reduced to only two rates i.e. 15% up to Rs.75000 and 25% of the rest amount in 2000/01. Now it is 15% for Rs. 100000 and 25% for balance amount. For the income more than Rs. 2500000 35% is charged. Similarly income tax rate has been reduced from 60% in the fiscal year 1975/76 to 30% for banking and financial companies, 25% for others including partnership firm and 20% for special industries from 2006/07.
14. In Nepal coverage of income tax base is very low. Agricultural income is exempted from income tax. Exclusion of agriculture income from the tax net alone cuts out about half of the GDP. On the other hand, employment income is taxed more heavily than the capital income. Retirement amount received by Nepalese people being retired from the service of army or police of foreign country is also exempted from income tax. Such provision provides loopholes for tax evasion.
15. Some exemption are granted to achieve certain objectives are not effective. Tax incentive is one of the examples. Although the concession encourage for the establishment of industries in certain areas but they vanish or change names, ownership or place of the business when the tax incentive facility expires.
16. Income tax act has clearly mentioned the organizations, which are tax free which is called exempt organization. Act has exempted a social, religious, educational or charitable organization of a public character registered without having profit motive.
17. Donation made to an exempt organization, approved by Inland Revenue Department (IRD) is allowed for deduction from taxable income. Deduction allowed for an individual or an entity will not exceed Rs. 100,000 or 5% of adjusted taxable income. However, the GON may prescribe, by a notification in the Nepal Gazette, as to allow full or partial deduction at the time of assessing income of the expense incurred for special purpose or donation given by the person. Here, the act has not defined "What is special purpose?"
18. For the purpose of calculating the income of person for an income-year from a business or investment, all the interest expenses are allowed for deduction. But in the case of an exempt-controlled resident entity, it can deduct the amount of

interest but not exceeding the sum of all the interest derived by the entity during the year that is to be included in calculating the entity's taxable income for the years and 50 percent of entity's taxable income for the year calculated without including any interest derived by the entity or deducting any interest by the entity. It is an unlawful step to business which is not getting the deduction of full amount of interest. Here a controversial condition exists between the law of banking and law of income tax because law of banking says that the interest must be paid to bank but the law of income tax does not give the deduction of full amount of interest for an income year.

19. For the purpose of calculating a person's income for an income year from any business, no deduction is otherwise allowed for the cost of trading stock except the allowance determined by subtracting the amount of closing value of trading stock of the business from the opening value of trading stock plus the cost of trading stock of the business acquired by the person during the year.
20. For the purpose of calculating a person's income for an income year from any business or investment, there shall be deducted all costs to the extent incurred during the year in the respect of the repair or improvement of depreciated assets owned and used by the person during the year in the production of the person's income from the business or investment. But the deduction allowed should not exceed 7% of the depreciation basis of the pool at the end of income year and the deduction shall be allowed with respect to cost in the order to which they are incurred. Any excess cost, or part thereof, for which deduction is not allowed shall be added to the depreciation basis of the pool to which it relates in accordance. The provision of adding any cost or part thereof to the depreciation basis amount is not contextual and lawful provision because it shows that the repair or improvement cost of depreciable assets has not got full approval. In the other hand, the tendency of carrying forward of this cost will increase the income tax revenue of the government in some content but it will not bring the cordial relationship between the taxpayers and the government.
21. All the costs made on pollution control by a person during the year in conducting the business are allowed for deduction. But the expenses shall not exceed 50% of the person's taxable income calculated without deduction for pollution control costs. Any excess costs, or part thereof, for which a

deduction is not allowed shall be capitalized and may be depreciated in accordance. Here, the government has a will of controlling pollution and then protection of environment but has not spent a little bit money on it. In the other hand, all the expenses made by the business to control pollution are not allowed for deduction and has made a standard limit for it. So, it is not a good symptom of pollution control.

22. All the expenses made on research and development by a person during the year in conducting the business is allowed for deduction. But the deduction allowed shall not exceed 50% of the persons' tax income calculated without a deduction for research and development costs. Any excess or part thereof for which deduction is not allowed shall be capitalized and may be depreciated in accordance. Researcher is an instructor of development. For successful industrial development research and development is more important and must be expended on it. Expenses made on it must be approved and should be allowed for deduction for tax purpose. But the provision of income tax has not given full deduction on it. It is a myopic vision of government.

23. Depreciation of depreciable assets owned and used by the person during the year in the production of person's income from the business or investment allowed for the deduction. But the following provision shall be applied in respect of the depreciation of the machines, equipment and other machinery installed in the electricity projects that are involved in building power station, generating and transmitting electricity and in the projects conducted by any entity so as to build public infrastructure, own, operate and transfer to the government. In case where the old machines, equipment and other machinery that are already installed require replacement in any income year as they are out of order due to being too old, the balancing value of the old machines, equipment and other machinery remained after subtracting the depreciation up to the year from their cost shall be allowed as expenses for the year.

At the time of transfer of other assets to the government except of old assets replaced in accordance with above paragraph, the balancing value, if remained, after subtracting the depreciation up to the year of the transfer from their cost shall be allowed as expenses.

Rates of depreciation are far from reality because there is no specific estimation provision of real age of assets and depreciation rate in Nepal. In the other hand, there is no any specific provision of depreciation of assets, which are taken in lease and installment payment basis. It shows a weak point of new Income Tax Act.

24. Any unrelieved loss of the year incurred by the person from any other business and unrelieved loss of the previous 7 years incurred by the person from any business are allowed for deduction. In the case of electricity projects involving in building power station, generating and transmitting electricity and the projects conducted by an entity so as to build public infrastructure, own, operate and transfer (BOOT) to government, entity conducting petroleum business under Nepal Petroleum Act 2040, and losses can be deducted up to next 12 years. Carry forward of losses for 7 years is not sufficient to encourage the business for taking risk. The provision of carry backward is also thoughtful because the accounting system of Nepal is not so standard to apply this provision.
25. For the purpose of calculating the income of a person for an income year from any business, employment or investment, the following expenses are not allowed for deduction such as domestic expenses, income tax paid, tax exempt expenses mentioned under section 10 or final withholding payments, distribution of profits, foreign income tax and any other amount to the extent to which a deduction is not derived, defined and clarified the amount by the Act. This kind of provision will provide a loophole for tax evasion.
26. A person whose annual turnover for an income year does not exceed Rs. 20,00,000 is not allowed for deduction for cash payment of more than Rs. 50,000 incurred at once. But if the payment of more than Rs. 50,000 is made to the government, a constitutional body, a corporation owned by GON, a bank or financial institution is allowable. A farmer or producer producing primary agricultural products even in the case where the products are primarily processed by the farmer himself/herself or in an area where banking services are at least 10 K.M. away from the place, the cash expenses or payment more than Rs. 50,000 is deductible.

27. Income Tax Administration is not efficient due to various causes like weaknesses in government's economic policy, complicated tax laws and provisions, lack of public participation and lack of trained and competent employees etc.
28. Income Tax System is suffering from various problems and weakness such as lack of trained employees, lack of cooperation in tax administration, increased corruption, voluntary compliance, ambiguous provisions under the Nepalese tax laws, limited tax base, difficult to maintain the account for tax purpose, relatively high tax rate, lack of timely adjustment of tax laws etc.
29. An opinion survey was conducted in order to find out the various aspects of income tax, exemptions and deductions. From the survey of various respondents (i.e. tax experts, tax administrators and tax payers), the following findings have been drawn as:
- i. The contribution of IT to the national revenue of Nepal is not satisfactory. Most of the respondents of all groups (A, B, C) were disagreed that contribution of IT to national revenue is satisfactory. 90, 60 and 80 percent respectively of each group were against the satisfaction.
 - ii. The main causes which are responsible for the unsatisfactory contribution of IT to national revenue of Nepal are ranked in order as follows:
 1. Weakness in government's economic policy.
 2. Corruptions.
 3. Lack of public participation.
 4. Complicated tax laws and provisions.
 5. Defective assessment procedure.
 6. Lack of coordination within the tax department.
 7. Scarce of income tax experts/professionals in tax administration.
 8. Inefficient organizational structure of tax administration.
 - iii. Income tax rates of Nepal are considered as medium. Most of the respondents (73.75) were agreed that the income tax rates are medium. Only 22.5 and 3.75 percent of respondents were agreed that income tax rates are high and low respectively.
 - iv. Out of 80 respondents, 48 respondents i.e. 60% were agreed that the exempted items of income are sufficient whereas 32 respondents i.e.40 % were disagreed about the sufficiency of exempted items.

- v. Disagreed respondents ranked overtime allowances as no. one income to be exempted from tax and then retirement benefits, house rent, awards, rewards and scholarship, export earning, interest received from government's bank and income from foreign employment respectively.
- vi. The current IT exemption limit is not adequate. Most of the respondents suggested to provide Rs. 3,00,000 and Rs. 4,00,000 exemption limit for an individual and a couple or a family respectively.
- vii. The exemption limit should be adjusted according to the inflationary situation of the country.
- viii. The family exemption limit must not be provided according to the no. of dependents because of impracticability.
- ix. 75% of the total respondents were in support to exempt the agricultural income whereas only 6.25% were against the exemption. 12.5% of the total respondents were in favor to treat it as other income. Thus it can be concluded that the agricultural income should be exempted from tax.
- x. Half of the respondents were against the sufficiency of itemized deductions of expenses whereas half of the respondents were in favor of the sufficiency of itemized deduction of expenses.
- xi. Expenses that should be deducted while computing taxable income are ranked by respondents in the following order:-
 1. Educational expenses/allowances
 2. Medical expenses on the basis of bills
 3. House rent
 4. Traveling expenses/allowances
 5. Full deduction of repair and maintenance expenses
 6. Full deduction of depreciation
 7. Tiffin allowances
- xii. 75% of the total respondents were aware about the provision of tax exemptions and deductions per ITA, 2058 of Nepal where as 25% were unaware about it. The respondents who were unaware about it were tax payers. They were unaware mostly because of different provisions regarding exemptions and deductions. Some of them do not consider necessary to know about it and some think that tax offices are also in dilemma in this regard.

xiii. 46.66% of respondents were agreed whereas 53.34% of respondents were disagreed about sufficiency of provisions relating to exemptions and deductions under Nepalese ITA. Improvements should be made in various aspect which can be shown in the following order:-

1. Remove complicated provisions
2. Tax laws should be simplified
3. Tax base should be enlarged
4. Improvement in accounting system
5. Exemption limit on the basis of market price
6. Computerized system in all tax offices
7. Functional systems

Also various suggestions were received from respondents about income tax in Nepal.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

Income Tax is one of the major sources of government's revenue and instrument for the economic development of Nepal. However due to poorly design defective tax system, the coverage of IT is very low. There is so much conflict and complication on tax laws and rules which is not motivating the willingness to pay tax to the general tax payers. Tax authorities are also lacking proper tax enforcement. General people have always doubt the GON.

This study aims to analyze the exemptions and deductions of present IT system. Though some studies were previously made on exemptions and deductions in Nepalese perspective, it is still felt a research gap where lots of confusion exist and lots of facts to be explored about the matter. For the purpose, in partial fulfillment of the MBS, a research is being started to prepare a thesis.

Like other research paper, it has also been prepared in the format of research paper for which total research work has been classified in five chapters: Introduction, Literature Review, Research Methodology, Data Presentation and Analysis and finally Summary, Conclusion and Recommendation.

The first chapter exhibited the specific objectives of this study along with background of the study, statement of the problem, scope of the study, significance of the study, limitation of the study and organization of the study.

Second chapter has included conceptual framework, legal provisions regarding tax exemptions and deductions and the past study of the related literature. In which were clearly defined income tax in Nepal and international context, Exempt amount, Deduction allowed, Expenses not allowed for deduction and brief review of ITA, 2058. Various books, dissertations, reports and articles published in journal and newspapers are reviewed while preparing this dissertation. This chapter has analyzed and reviewed about the past related studies which served as the basis for finding research gap as on which new visional analysis was required.

The third chapter is about research methodology which is over map of the research paper. Under this topic, research design, population and sample, nature and sources of data, data collection procedure and data analysis technique are presented. The research is designed as both descriptive and analytical type and population for this study are comprised of the entire person belonging to or associated with IT in Nepal. This research has used both secondary and primary data.

As another major step in study, data collection and presentation is done. Secondary as well as primary data were collected from various sources, which were felt to be useful for the study. Based on those collected data, a detail analysis of the income tax exemptions and deductions in Nepalese context is done in systematic manner. A detailed analysis of composition of tax revenue, contribution of various taxes to GDP, contribution of income tax in Nepal, composition and trend of income tax, exemption limit in Nepal is made under this study. After the analysis of secondary data, an attempt has also made on the analysis of primary data. A 16 question questionnaire is prepared to obtain the various dimensional views of the respondents regarding income tax regulations, sufficiency of current tax exemption limits, deductions and exempted amounts, provision regarding exemptions and deductions and suggestions. Answer of the each of the questions is analyzed by presenting and tabulating the result from respondent. The findings are also presented along with the analysis of the data.

Final chapter of this study is a conclusive chapter prepared summarizing all the study procedures and drawing conclusion about the findings along with the recommendations if any.

5.2 Conclusion

The ultimate goal of any underdeveloped countries like Nepal is to achieve economic development and ensure rapid economic growth. Sufficient funds or huge amount of investment in economic overhead and other development activities are required to meet the objectives of economic development for which taxation is undoubtedly a primary source of Inland Revenue for the government. But Nepal has not been able to collect necessary funds or revenue. Due to poor performance on internal revenue collection and its mobilization, Nepal has been heavily relying on foreign loans and grants. The dependence is increasing day by day, which is not desirable for any

economy. Thus, it is most necessary to mobilize the internal fund or revenue to the optimum level.

To increase the government internal revenue, Nepalese government is trying to extract money from people through taxation. Within tax, income tax is the most important source of government revenue, which is considered as a good remedy to cure growing resource gap in Nepal.

In Nepal, the history of income tax is not so long. It was started only on late fifties. The income tax was introduced as a trial on business profit and the remuneration income. The first elected government levied the first income tax and no specific act was made to define and treat income tax. The first income tax act was introduced only in 1959/60, since then four income tax acts have been implemented. From the very beginning the concepts of exemptions, deductions and other forms of tax relief in income tax have emerged in Nepal. All incomes of an individual can not be taxable income because the minimum cost required for subsistence can not be taxed. The exemptions, deductions and other forms of tax relief are essential to encourage an individual to work more. The tax relief works as an incentive to an individual. So, the concept of exemptions, deductions, and tax reliefs were emerged in Nepal from the very beginning of income tax.

Exemption limit and the rate of the income tax is determined according to the income level and sector wise but has not been adjusted according to the inflationary situation of the country and number of dependents. Exemption limit is not provided to corporate bodies. Income tax exemptions, rebate, relief, concession, allowance and exemption limit should be adjusted according to time and situation.

Income tax system of Nepal has been blamed as being inefficient system. It is not fully satisfactory. Revenue collection from income tax is low as compared to other developing countries like India, Sri Lanka, and Pakistan etc. Due to various problems existed in the income tax such as increasing habit of tax evasion, corruption, inefficient tax administration, defective income tax law are the reasons of lower contribution of income tax. Internal conflict of nation and political instability has also affected the economic system indirectly but very seriously. Nevertheless, if the data are analyzed relating to it, it is found that it is neither bad nor worse but it has been continuously improving. However, income tax laws and administration in Nepal are

to be deeply scrutinized and properly implemented. The provisions made on the act have to be mentioned clearly and language has to be made clear. Some reforms in tax administration are needed. The success or effectiveness of IT system entirely depends upon implementation of provision that is the major responsibility of IT administration. If the problems relating to income tax system in Nepal can be solved and resources are effectively utilized then only the prospects of revenue collection through income tax will be effective and bright and the economic development of Nepal will be achieved.

5.3 Recommendation

As earlier described, there are various problems regarding to income tax of Nepal. The existing tax assessment procedure is also unsound and inefficient. The major causes of being unsound and inefficient tax assessment procedure are weakness in government's economic policy, corruption, lack of public participation, complicated tax laws and provisions, lack of coordination within tax department etc. In the opinion survey, it was noticed that most of the respondents were dissatisfied with the government economic policy, complicated tax laws and provisions and inefficient tax administration. The study mostly focused into the problems that are related to exemptions and deductions. So, the recommendations made for other than the exemptions and deductions may have been considered as the general recommendations. Hence, the research of the study has made the following recommendations on tax exemption and deduction.

Exemption of incomes

1. To increase the income tax revenue, the present tax base must be widened by including the incomes from agricultural sector, pension amount received by Nepalese people being retired from the services by army or police of foreign country, currently exempted other sources income and by linking banking transactions above certain threshold with the PAN of each individual. Agricultural income should be taxed above certain maximum limit. A practical arrangement for taxing agriculture should be formulated.

2. The present provision of an individual and a family exemption limit are not appropriate. It should be raised to a minimum of Rs. 300,000 for an individual and Rs.4,00,000 for a family.
3. The exemption limit should be adjusted according to the inflationary situation of the country on yearly basis.
4. Most of the taxpayers are not aware about the provision of IT exemptions and deductions. General public awareness should be increased about it.
5. There are many provisions relating tax exemptions and concessions which are rarely used or which are not effective. Tax concessions encourage the establishment of industries in certain areas but no infrastructure development has been done in such place like easy transportation facilities. Some vanish or change names, ownership or place the business when the concession facility expires. Such kinds of concession do not encourage opening the industry in remote areas. For the purpose of industrial development of remote area, a separate special package should be introduced.
6. Little percentage of tax rebates should be provided to the taxpayers who submit true income statement within the specified period of time.
7. Income tax on total export amount is not appropriate because IT should be based on income not on the total amount. So, the provision of taxing on export income should be introduced. Similarly, export fee on export transaction should be eliminated or exempted.
8. Double taxation on dividend should be eliminated.
9. ITA has mentioned the organizations, which are tax free (exempt organizations). Act has exempted a social, religious, educational or charitable organization of a public character registered without having profit motive. In the case of non-transparent private business like boarding school, NGO's or other entities, where profits are earned, but for the sake of tax planning, is called retained earning or something else. So, they should be taken into tax net.
10. Retirement Contributions are nothing else than the product of sacrifice of present earnings. There are the bases for living standard of oldness of employees. So, they should be fully excluded from income tax.
11. Dearness allowance is given to meet the living standard of employees, it is not lawful to include in taxable income. So it should be fully exempted from income tax.

Deduction of Expenses

1. Donation given to a political parties registered with the election commission is allowed for deduction. But it has not been able to solve the voice of people of 'transparency of donation amount given by business men to political parties'. So, donation amount given to political parties should be transparent.
2. Deductions allowed from an employment income are not sufficient. So, the following deductions should be provided to the tax payers whose source of income is only the remuneration.
 - a. Expenses for better education of their children.
 - b. Medical expenses made by taxpayers.
 - c. Expenses made for house rent.
 - d. Educational expenses for taxpayers himself if he is still studying in an educational institution.
 - e. Life insurance premium.
 - f. Pregnant delivery expenses for certain limit.
3. Clear provisions should be made in the case of deduction. All the items of deductions should be clearly defined in the act.
4. Deductions allowed from business or investment incomes are not sufficient. So the following deductions should be provided to the taxpayers whose source of income is business or investment.
 - a. In the case of exempt controlled resident entity, full deduction of interest expense is not allowed. It is not lawful step to the businessmen who operate the business with loan or debt amount. So, it should be fully allowed for deduction within an income year.
 - b. The provision of adding any excess loss or part there of repair and improvement costs to the depreciation basis amount is not contextual and lawful provision because it shows that the repair or improvement cost of a depreciable asset has not got full approval or deduction. So it should be fully allowed for deduction within an income year.
 - c. To control pollution and protect environment, environmental protection is more essential and should be expended on it; expenses made on it should be approved and should be fully allowed for deduction within an income year. Act should not make standard limit on it.

- d. For successful industrial development, research and development is more essential and should be expended on it. Expenses made on it should be approved and should be fully allowed for deduction within an income year. Standard limit on it should not be made.
- e. There should be specific provision of depreciation of assets, which are taken on lease and installment basis. Act should not be silent on it. Provisions made on depreciation allowances should be generally understandable by all people.
- f. More deductions should be provided to the investment made in hydropower and other development sector.
- g. Carry forward of losses for 7 years is not sufficient as compared to other countries. So, it should be extended up to 9 or 10 years. The provisions of carry backward of losses should be considered because the accounting system of Nepal is not so standard to apply this provision.

Besides these recommendations, the following recommendations are made to compensate the loss of revenue due to the provision of additional exemptions and deductions recommended by the researcher:

1. The income tax policy should be formulated so as to match with the economic policy of the country.
2. The members involved in formulating income tax policies must have deep knowledge about income tax.
3. Timely revision and adjustment should be made in the matter of income tax policy.
4. Income tax policy should be formulated so as to satisfy the following criteria:
 - a. It should be progressive to ensure social justice.
 - b. It should be consistent with tax administration capacity.
 - c. It should not mitigate against national priorities and efficient resource use.
5. The success or effectiveness of any system entirely depends upon implementation of provisions, which is the major responsibility of administration. In Nepal, one of the most important reasons to be unsound income tax system is inefficient and unscientific income tax administration. The following recommendations are made for the improvement of income tax administration in Nepal:
 - a. All the tax personnel should be given comprehensive training on various aspects of taxation on regular basis. For this, a separate training section within tax department should be established.

- b. The performance, responsibilities, authorities and duties should be clearly defined.
 - c. Financial benefits and extra incentives should be provided to the personnel to decrease corruption.
 - d. Effective reward and punishment system should be established.
 - e. Working environment of the tax offices should be improved, other facilities should be provided.
 - f. The administration should try to increase effective public participation to minimize the income tax evasion.
 - g. Income tax experts/professionals should be increased in tax administration.
 - h. Coordination between staffs and departments should be established.
 - i. Delays in assessment should be reduced as soon as possible.
 - j. Fair and scientific provision of promotion and career development should be introduced.
 - k. The cost of revenue collection is one of the determinants of administrative efficiency. So, the concerned authority should pay due attention on it.
 - l. An integrated information system should be developed to prepare the list of potential taxpayers and gather information of various aspects relating to income tax.
 - m. The system of recording by computer should be developed in income tax administration.
 - n. Tax education should be provided to taxpayers on regular basis.
6. Laws relating to income tax should be clear, simple and comprehensive, it should not contain any loopholes and ambiguity; therefore it should be reviewed frequently and reformed. The following recommendations made for the reformation of existing tax laws in Nepal as;
- a. The language should be simple and clear. In spite of using the vague meaningful words, clear cut provision should be undertaken.
 - b. The definition made in ITA be further clarified and well defined.
 - c. The assessment and tax collection provisions should be made clear and simple.
 - d. The provision of fines, penalties and punishments should be made at higher rate for income tax evaders.
 - e. The assessment of time limit after the submission of income statement should be reduced.

- f. Discretionary power of the tax officers should be curtailed and their rights and duties should be clarified in ITA.
7. The rewards, prizes, incentives provisions should be introduced in the act to encourage the taxpayers to pay tax voluntarily rather than coercive measures.
8. Clear provisions should be made in the case of deductions. All the item of deductions should be clearly defined in the act.
9. There should be compulsory provisions of auditing.
10. The administration should pay great attention to bring the income from house and land rent, doctors clinic, consultancy services, tuition center etc into income tax net. In these sectors income tax has been highly evaded.
11. Unnecessary political and outsider's pressure should be avoided.
12. The provision of tax deduction at source and advance payment to tax should be extended to different source of income as far as possible.

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APPENDIX-I

Cover Letter

Dear Sir / Madam

I am Shisira Adhikari, a student of Central Department Of Management, Kirtipur, Kathmandu, Faculty of Management, M.B.S. Final Year (2067 / 070 Batch). In order to fulfill the partial requirement of the Degree in Masters of Business Studies, I am preparing a thesis named “**A Study of Income Tax Exemptions and Deductions in Nepal.**” For that, I have prepared and submitted the thesis proposal to the campus. I would be very much appreciated if you kindly spare of fens of your busy and valuable time for completing my research work in the given time. I anticipate your suggestions as far as possible.

Thank You!

.....

Your Sincerely

Shisira Adhikari

Campus Roll No.:220/067

T.U. Regd. No.: 7-2-1-1250-2006

APPENDIX-II

QUESTIONNAIRE

Name of the Respondent:

Designation:

Office/Organization:

Address:

(Please tick your answers in the following and put in order of preference from first to last number if there are more than four alternatives)

1. Do you think that contribution of income tax to national revenue is satisfactory?

a. Yes []

b. No []

2. If your answer is No, what are the major causes which are responsible for unsatisfactory contribution of income tax to national revenue? Give your answer from the following options in order of rank from 1 to 8.

- a. Defective assessment procedure []
- b. Lack of public participation []
- c. Inefficient organizational structure of tax administration []
- d. Scarce of income tax expert/professionals in tax administration []
- e. Weakness in government's economic policy []
- f. Lack of co-ordination within the tax department []
- g. Complicated tax laws and provisions []
- h. Corruptions []
- i. Others, if any []

3. What is your opinion about the current income tax rate?

- a. High []
- b. Medium []
- c. Low []

4. Do you think that the exempted items of income are sufficient?

- a. Yes []
- b. No []

5. If no, what kind of incomes should be exempted? Please give your answer in order/rank of importance.

- a. Awards, rewards and scholarship []
- b. Export earnings []
- c. Interest received from government's bank []
- d. Overtime allowance []
- e. Retirement benefits []
- f. Income from foreign employment []
- g. House rent []
- h. Others, if any []

6. Do you think that the current tax exemption limit is adequate for individual and couple or a family?

a. Yes []

b. No []

7. If no, what exemption limits do you suggest for? Please write in spaces provided below:

S.N.	Types	Existing Limit	Suggestion
a.	An individual	Rs. 2,00,000	
b.	A couple or a family	Rs. 2,50,000	

8. Do you agree that exemption limit should be adjusted according to inflationary situation of the country?

a. Yes []

b. No []

9. Do you agree that family exemption limit must be provided according to the number of dependent?

a. Yes []

b. No []

10. What is your opinion on providing exemption on agricultural income?

a. Yes, it should be exempted []

b. No, it should not be exempted []

c. It should be treated as other income []

d. Others, if any, specify []

11. Do you think that the itemized deductions are sufficient?

a. Yes []

b. No []

12. If no, what kind of other expenses should be deducted while computing taxable income? Please write your answers in order/rank of importance.

a. Educational expenses/allowances []

b. Traveling expenses/allowances []

c. House rent []

- d. Tiffin allowance []
- e. Medical expenses on the basis of bills []
- f. Full deduction of repair and maintenance expenses []
- g. Full deduction of Depreciation []
- h. Others if any []

13. Are you aware about the provision of tax exemption per the income tax act 2058 of Nepal?

- a. Yes []
- b. No []

If No, what are the causes or possible reason of it?

- a. Different provision regarding exemption []
- b. Tax office also dilemma in this regard []
- c. I don't think it necessary []
- d. If Others, Please Specify

14. In your opinion, are the provisions related to exemptions and deductions under the Nepalese ITA, 2058 B.S. sufficient in all aspect?

- a. Yes []
- b. No []

15. If no, in which aspect the improvement are needed? Please specify your answer in the order of importance.

- a. Tax laws should be simplified []
- b. Improvement in accounting system []
- c. Computerized system in all tax offices []
- d. Remove complicated provisions. []
- e. Exemption limit on the basis of market price []
- f. Tax base should be enlarged []
- g. Functional system []
- h. Others, if any []

7. Nabin Dhungina (Raj MS and Company, Dillibazar)
8. Pradeep Gragain (M. Khanal and Company, Putalisadak)
9. P.K Jha (J.V, Dillibazar))
10. Anupa Acharya (B.B Raj Bhandary and company, Dillibazar)
11. Umesh Paneru (Yeti Airlines, Tilganga)
12. Umesh Raj Paudel (N. Krishnas way and company, Kamalpokhari)
13. Keshav Kumar Pandey (RAS. Project, Lazimpat)
14. Janak Raj Pokharel (ADB, Singhadurbar)
15. Saraswati Adhikari (RBB)
16. R.M. Singh (FNCCI, Teku)
17. Badri Karki (Overall Service and Consultancy, Kalimati)
18. Basanta Gautam (Team of Business Enterpreneur, Anamnagar)
19. Milian Shrestha (Universal college, Kathmandu)
20. Sudarsan Suwal (Laxmi Bank, New Road)

Tax Administrators

1. Kamala Bhusal (Tso, Kalamati)
2. Kishwor Bhandari (Tso, Kalamati)
3. Udaya K.C (Tso, Kalimati)
4. Shom Raj Bhandari (Tso, Kalimati)
5. Prabhu Dhungal (Tso, Kalimati)
6. Hem Raj Joshi (Tso, Kalimati)
7. Janardan Tirtaphe (IRI, Kalimati)
8. Nagendra Chhaudry (Tso, Kalamati)
9. Bed Prasad Khanal (Tso, Kalimati)
10. Tek Raj Syangtari (Tso kalimati)
11. Gita Lamsal (Tso Kalimati)
12. Shanta Thapa (TSO Putalisadak)
13. Anita Bhattarai (TSO Putalisadak)
14. Anita Sharma (TSO Putalisadak)
15. Gopal Pd. Sharma (TSO Putalisadak)
16. Hariram Dhakal (TSO Putalisadak)
17. Ganesh Pd. Nepal (TSO Putalisadak)

18. Hem Chandra Sharma (TSO Putalisadak)
19. Bimal Kumar Koiral (TSO Putalisadak)
20. Yubraj Pabthee (TSO Putalisadak)
21. Janardan Tripathi (IROI, Babarmahal)
22. Shobhakar (IROI, Babarmahal)
23. D.B. Chhetri (IROI, Babarmahal)
24. Subarna Koirala (IROI, Babarmahal)
25. Prem pd. Acharya (IROI, Babarmahal)
26. Babu Kaji Karki (IRI, Babarmahal)
27. Ishwori Laxmi Bhomi (IRI, Babarmahal)
28. Govinda Subedi (IROI, Babarmahal)
29. Sharad Niraula (IROI, Babarmahal)
30. Indra Bhadur Devkota (IROI, Babarmahal)

Tax Payers

1. Prithivi Raj Sharma (Dugar Brothers and Sons)
2. Mahesh Shrestha (Bhawani plastic industry)
3. Rajendra Prasad Dahal (Rastriya Banijya Bank, Singhadurbar)
4. Bishnu paudel (Stationary, Shiphala)
5. Mamata maharjan (Bikalpa Co-operative .Pvt.Ltd)
6. Dilip Pokhrel (Samad Overseas Pvt.Ltd, Gaushala)
7. Sunny Shakya (Durable Multi Trade Pvt.Ltd, Teku)
8. Ram Chandra Pandit (Himalayan Multiplast, Balaju)
9. Subash Khitawada (Om Siddhi Poli Clinic and Medical Center, Dillibazar)
10. Narottam Dhakal (Nichandan Wala International, Balaju)
11. Jeevan Thapa (Shree polythin and plastic udyog, Balaju)
12. Susan Shakya (Kathmandu domestic appliances, Balaju)
13. Suresh Karanjeet (National ice cream industries Pvt. Ltd., Balaju)
14. Prithivi Adhikari (Gurans Engineering Pvt. Ltd, Balaju)
15. Hari Paudel (Bajra footware Industries Pvt. Ltd., Balaju)
16. Arjun Khanal (Modern Slipper Ind. Pvt ltd, Balaju)
17. Narayan Adhakari (Bottlers Nepal Ltd, Balaju)
18. Sunil Shakya (Shakya almunium Pvt.Ltd, Kalimati)

19. Ram Chandra Dhital (Shree Samuhik, Krishi Dairy Ltd., Balaju)
20. Kamal Bahadur Shrestha (Sudharshan Nirman Samagri Udhyog, Balaju)
21. Niraj Dahal (Shree Rashmi Traders and General Suppliers, putalisadak)
22. Krishna Kumar Shrestha (Nakasu Motors Pvt. Ltd., Balaju)
23. Basanta Acharya (Gorkha Nepal Placement Pvt. Ltd, Baneshwor)
24. Ritesh Jajodia (Mars Polymers Products Pvt. Ltd, Balaju)
25. Dolnath Dawadi (Shree Polythin and Plastic udhyog, Balaju)
26. Jeevan Thapa (Index Travels and Tours, New Baneshwor)
27. Shyam Sundar Shrestha (Prasanna Plastic Udhyog, Balaju)
28. Ujwal Shakya (Quality Kitchen Equipment Pvt. Ltd, Gauridhara)
29. Rajan Jung Thapa (DDC, Lainchaur)
30. Birendra Shah (Brindabasini Plasatic Udgyog, Lalitpur)