

CHAPTER I

INTRODUCTION

1.1 General Background

As Kautilya says “The launching of all programmes depends first and foremost on the treasury”, so every state needs resources. Whether to pay salary to the government employers or to do the developmental works, it needs huge amount of money called revenue.

The government of a country requires sufficient revenue to carry out development plans to handle day to day administration, to maintain peace and security and to launch various public welfare activities. The government revenue comes from different sources like tax revenues from public enterprises, special assessment, fees, fines, grants etc. Among them, tax is the main source of government revenue. Custom, excise duty, sales tax, value added tax, income tax are the examples of the sources of tax revenue. Government passes the acts for getting tax revenues and collects the taxes as per the act. Nepal collects around 80 percent of the revenue from this source.

Nepal has a predominantly agriculture base economy. The major portion of population of Nepal is in village area and most of them live below the poverty line. Wide spread poverty, rapid population growth, low income level, extreme disparity in the distribution of wealth and income, heavy dependence on agriculture, lack of industrialization, lack of needed saving and capital, dependence on foreign aid, unemployment, unexploited resources, lack of infrastructure, adverse balance are the main characteristics of Nepalese economy and it shows poor performance of economy.

Now days, the prime concern of every country is rapid economic development and Nepal is no exception to this ever continuing process, aimed at the betterment of its people. Capital plays a vital role in the rapid economic development programme to solve the various socio-economic problems.

The constitution of Nepal has clearly directed Nepalese government for a self reliant economic system, encouragement to national enterprises, prevention of economic exploitation as well as upgrading the standard of the people. For self reliant economic system and sound infrastructure for the development, the government should generate sufficient government revenue. Government revenue is the most important source of financing government expenditure. To achieve the national objectives, the government is required to make and implement various policies and planning, acts and procedure. Besides these functions revenue mobilization is one of the most important functions of the government. (Bhattarai, 1997:23)

The income of the government is called public or government revenue. Government revenue constitutes internal and external sources. Internal sources constitutes tax and non- tax revenue. Taxation is regarded as an effective instrument to monitor various economic activities in a country. The major objective of taxation is to make fund available for the economic development and economic stability. For the economic development of the country internal resource mobilization is much better than external resource mobilization because internal source are safer than external. It is better for developing countries to maximize the mobilization of domestic resources. Heavy dependence on foreign assistance and loan to strengthen the revenue structure is not favorable sign for developing countries. (Pant & Pant, 1999:12)

The dependency on foreign assistance or loan can be minimized if the country can maximize the mobilization of the domestic resources. There are lots of ways to strengthen the economy of the country by properly mobilizing the internal resources. Taxation may be very useful and major internal sources for government revenue as it is considered as safest means of capital formation.

The effectiveness of any government depends on the willingness of the people governed to surrender or exchange a measure of control over their person and property in return for protection and other services. Taxation is one form of this exchange. (Encyclopedia, 1971:54)

In the context of developing countries like Nepal, the prospect of mobilizing resources other than taxation has not been so encouraging. Taxation not only contributes in capital formation but also in equal distribution of national income of the country. It helps to reduce extreme disparity in the distribution of wealth and income.

Tax is, in simple terminology, a liability to pay an amount to the government. It is a compulsory contribution to the national revenue from the taxpayers according to law.

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.

From the definition given above, it can be said that firstly, a tax is a compulsory levy and those who are taxed have to pay it without getting corresponding benefit of services or goods from the government.

Tax can be classified into two categories Direct tax and Indirect tax. A direct tax is a tax paid by a person on whom it is legally imposed. In direct tax, the person paying and bearing tax is the same. Examples of direct taxes are Income Tax, Property Tax, Vehicle Tax, Interest Tax etc.

An indirect tax is a tax imposed on one person but partly or wholly paid by another. In indirect tax, the person paying and bearing the tax is different. Examples of indirect taxes are Value Added Tax, Excise Duty, Import and Export Duty etc.

Revenue collection from income tax is one of the major parts of taxation. Income tax is a direct tax, which enjoys a major place in the revenues of government all over the world. It is a tax levied by the government on the income of individuals and business firms. (Prasad, 1999:33)

1.2 Statement of Problem

Nepal is one of the least developed countries among the developing countries in the world. It is facing serious financial problem from the beginning of its development process.

Despite the various measures adopted by the government to boost revenue collections, there is still a substantial resource gap between expenditure and revenue. Resource constraint is appearing as a limiting factor from the beginning of development phase to present time due to increasing resource gap. Even if foreign aids are also taken into consideration the resource gap is not negligible.

There is improper internal resources mobilization, heavy foreign aid dependence, low aid absorptive capacity and misutilization of available resources in Nepal. There are not adequate internal financial resources to spend and invest on economic development activities of the country. Even after the introduction of various taxes after the advent of the democracy in Nepal in 1951 to create internal resources for economic development, the first five year economic plan (1956-1961) was implemented under cent percent foreign assistance. Considering this background, the main problem of Nepal is the lack of creation and mobilization of internal financial resources. (Guru Gharana, 1995:164)

The development of the country will be possible only when the government can collect its own internal revenue which constitutes tax and non tax revenue. Tax revenue constitutes a significant portion in government revenue. Of the total revenue collected in fiscal year 2006/07, tax revenue and non tax revenue account for 79.45 percent and 20.55 percent respectively. In fiscal year 2005/06, their contribution was 77.2 percent and 22.8 percent respectively. (Economic Survey, 2008)

Government has adopted various policies to strengthen the revenue structure of Nepal. Broad tax base is necessary to enhance the government revenue and for this purpose income tax revenue is most reliable among the different sources of revenue.

There is low collection of income tax even after the implementation of self tax assessment system, and higher tendency of income tax evasion. The revenue

administration is not effective in Nepal. There is no willingness to pay tax on the part of the taxpayers of the country. Frequent changes in tax rates and in policies would not be favorable to strengthen the revenue mobilization and economic development and this fact is to be taken into consideration by the government of Nepal. (Auditor General's Report 2053/54, Nepal, p.12)

In developed countries income tax revenue is very important and it contributes more than 40 to 50 percent of total revenue of government but in developing countries income tax contributes low per capita. In Nepal, the contribution of income tax to total revenue is only 18.2 percent in the fiscal year 2006/07.

Although the trend of income tax revenue has displayed a healthy growth rate in the more recent years it still does not constitute a significant percentage of the country's gross domestic product (GDP). In fiscal year 2006/07 total contribution of government revenue to GDP is 11.2 percent; however the contribution of income tax to total government revenue is only 18.2 percent in the same fiscal year. Above figure clarifies a very little contribution of income tax to GDP. There are many problems in Nepalese income tax collection system. The causes of low coverage of income tax in government revenue are low per capita income of the Nepalese people, inefficient income tax administrative system, lack of consciousness about income tax in part of public, widespread income tax evasion etc. (Economic Survey, July 2008).

As the investments and expenditures of the country on economic activities are increasingly yearly, the internal resources mobilization is not increasing at the same ratio which is not a good sign for national economy and it causes heavy burden of foreign loans and assistance and the country is suffering from mass poverty.

A good tax system should be structured so that it can be administered effectively and economically. Taxes that are costly or difficult to administer divert resources on non productive uses and diminish confidence in both levy and the government. (Encyclopedia, p.153)

If the government had been effective in its revenue collection by income tax and other internal resources, the amount of foreign loan would have been increased less rapidly. So, in order to create the huge internal resources, the revenue administration of the country must be systematic and the people of the country must have knowledge of income tax rules and regulations and willingness to pay income tax. Only after that, the prospect of revenue collection from income tax will be higher for internal resource mobilization.

Therefore, for the government of Nepal it is better to depend on its own revenue than foreign assistance. Among the various sources of government revenue, income tax revenue can play a significant role if the problems of Nepalese income tax collection system can be improved.

1.3 Importance of the Study

Nepal is one of the lowest taxed economies in the world as its tax/GDP as well as tax/GNP ratio are the lowest among SAARC countries and among the rest of the world as well. This indicates the poor performance of income tax management of Nepal. For the economic development of the country, contribution of direct tax is more important rather than indirect tax but the whole tax structure of Nepal is dominated by indirect tax. (Nepal, 1998:44)

In developing countries like Nepal, income tax is very crucial for reducing economic inequalities in the society and to increase the domestic resource mobilization. It may be a useful instrument to measure the economic standard of the people. But the income tax management of Nepal is suffering from various problems. The major problems are inappropriate tax policies, administrative bottlenecks of direct tax structure and existence of mass poverty. So, to identify the problems and to overcome them to improve income tax system, study in the field of income tax is essential.

1.4 Objectives of the Study

The major objectives of the present study are as follows:

1. To analyze the effectiveness of Income Tax System in Nepal.

2. To evaluate the contribution of Income Tax in National Revenue.
3. To study the effectiveness of present Income Tax Administration.
4. To examine the problems and challenges of revenue collection from income tax.
5. To suggest and recommend on the basis of major findings.

1.5 Scope of the Study

Present study will attempt to cover the major constituents of income tax collection system in Nepal as a major source of direct tax revenue. It aims to find out the major problems in revenue collection system of income tax in Nepal and prospect for its effectiveness. The major areas of this study are as follows:

1. Structure of government revenue in Nepal.
2. Contribution of income tax to government revenue and GDP.
3. Administrative aspects of income tax in Nepal.
4. Income tax assessment procedures in Nepal.
5. Existing position of income tax in Nepal.
6. Tax laws and procedures, income tax rate, exemption limit in income tax etc.

1.6 Limitations of the Study

There are some limitations in this study which are as follows:

1. The extent of this study is based on the availability of reliable data and sufficient literature.
2. Major data used in this study is secondary data, while primary information is collected from tax administrator, tax experts and tax payers.
3. For the purpose of this thesis a field survey was done in Kathmandu valley only due to the time constraint and other difficulties.
4. This study is confined to Nepalese laws, acts, rules and regulations to the income tax.

1.7 Organization of the Study

This thesis has organized in five chapters. The first chapter is about introduction. It includes General Background, Statement of Problem, Importance of Study, Objectives

of Study, Scope of study, Research methodology, Limitations of the study, Organization of Study

The second chapter is about Conceptual Framework and Review of Literature. Conceptual framework deals with Concept of tax, Gradual development of Income Tax Act and Laws, Legal Provisions of Income Tax in Nepal, Sources of Income, Appeal, Interest and Fines, Methods of Income Tax Assessment, Concept of Corporate Tax, Development of Corporate Tax in Nepal etc. In Literature Review, review of thesis, books, research reports and articles are done which are used as guideline for preparing this thesis.

The third chapter is on Research Methodology which includes research design, population and sample, nature and source of data, data and information collection procedure, data processing and analysis procedure.

The fourth chapter is Presentation and Analysis of Data. It deals with Tax structure of Nepal, Composition of total revenue, Contribution of Income Tax in Nepal, Structure of Income Tax in Nepal, Problems of resource gap in Nepal, Corporate tax structure, Corporate tax base in Nepal, Contribution of Corporate Tax on Income Tax revenue etc.

Empirical investigation regarding public awareness towards Income Tax System, Contribution of Income Tax Revenue, Reasons for tax payer wise low collection from Income Tax, Appropriateness of Income Tax Rates, Weaknesses of Income Tax Act, 2058, Situation of present Income Tax Administration, Problems of Tax payers, Motivating Factor for Tax payers, Appropriate method of Income Tax assessment in Nepal, suggestions for achieving effectiveness of Income Tax in Nepal etc.

This chapter also reveals the major findings of the study. In which the major findings from the primary as well as secondary data are organized in a systematic way.

The fifth chapter is Summary, Conclusion and Recommendation which summarizes the thesis, draws the conclusion and provides the recommendation measures for the improvement of existing situation.

CHAPTER II REVIEW OF LITERATURE

2.1 Conceptual Framework

2.1.1 Concept of Tax

Different persons have defined taxation in different ways. In this respect, it would be better to take the definition given by Seligman. In his words taxation is the "Compulsory contribution from a person to the government to defray expenses incurred in the common interest of all without references to special benefit conferred."

From the definition given above, it can be said that firstly, a tax is a compulsory levy and those who are taxed have to pay it without getting corresponding benefit of services or goods from the government. The taxpayer does not have any right to receive direct benefit from the tax paid. Due to this compulsory nature, people have expressed different views in satirical ways about the taxation. 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 it is not tax because its objective is not to collect revenue but to curb certain types of offences. Secondly, taxpayer cannot receive any quid pro quo for the payment of tax. The taxpayer does not receive equivalent benefit from the government. A tax is not a price paid by one, for which he can claim 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, in case of tax the amount is spent for common interest of the people. The tax is collected from haves and basically, spent for the interest of have-nots in the society. Fifthly, a natural as an artificial person pays the tax.

In conclusion, it can be said that a tax is a liability to pay an amount to the state. The basis for the payment is that the assessee 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 for taxation.

Taxation has been a very essential element of a government from the very beginning of the state system. However, the main objective of taxation has been different for different epochs. In ancient times, the major objective of taxation was strengthening the muscle of the state by providing resources. Till to the time of Adam smith, the chief motive of collecting the revenue was to provide resources to the government for providing security to an individual and society against violence, invasion, and injustice and maintaining public institutions.

In modern days, 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 fallows:

- a. To increase the revenue for a welfare state.
- b. To have equitable distribution of income and property.
- c. To increase the production of particular goods.
- d. To increase the employment, saving and investment.
- e. To minimize regional disparity.
- f. To implement government policy, and
- g. 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

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

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

$$y = c + s$$

Where,

y = income

c = consumption

s = saving

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

1. Agriculture
2. Industry, Business, Profession or vocation.
3. Remuneration
4. House and land rent.
5. Other sources.

The existing Income Tax Act, 2002 (2058), which has been enacted since 2058, chaitra 19 (1st April 2002) has defined income in section 2/a as "Person's" Income from any employment business as calculated in accordance with this act (ITA. 2002). It includes

all sorts of income received for the provision of labor or capital or both of whatever form or nature in the taxable income.

Income tax refers to the tax levied on the income of a person and profits of corporation for the specific time period, particularly one year. Income tax is levied on the taxable income of a person or a company after deducting allowable expenses. Accounting profits may differ from taxable profits. For the computation of taxable income, generally incomes are added and expenses are subtracted and losses, which are allowed to deduct under the provision of income tax act are also subtracted. Then, tax free incomes, allowances and common expenses are also deducted to get taxable income. After giving the exemption limit as per law, the amount at tax to be levied on this computed income is the income tax.

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 and 1816, which is known as Napoleonic war.

The 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. Since this was levied as a war tax it was repealed on April 5, 1802 after the end of the war with France. However, the income tax was reinstated in 1803 after the outbreak of war again with France on May 18, 1803. The new Income Tax Act was enacted on August 1, 1803. As a war tax, it was abolished on March 18, 1816, after the end of the Napoleonic wars.

Income tax was proposed again on March 11, 1842, as a 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 of its yield accepted as a permanent tax by the 1840s.

In the USA also income tax was introduced in 1862 to generate revenue to finance civil war. The federal corporation income tax was introduced in 1909.

In Japan, income tax was introduced in 1887 through the enactment of the Income Tax law on March 23, 1887. It was a general individual income tax and extended to the corporate income in 1899.

Although the income tax had been levied in different form before the unification of Germany in 1871, income tax became an effective instrument since the Prussian Reform of 1891. In India, while income tax in its modern form was adopted in 1860, several experiments were made from 1860 to 1886 and finally the systematic income tax legislation was enacted in 1886.

Income tax was introduced in Switzerland in 1840, Austria in 1849, Italy 1864, New Zealand in 1891, Canada in 1892, Holland in 1892-93, Australia in 1895, Denmark in 1903, France in 1909, Sri Lanka in 1932, Venezuela in 1943, South Korea in 1948, and Nepal in 1959.

Similarly, this tax 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 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. This 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.

While the history of income tax is tumultuous, the situation is different now. Income tax has been an important element of the modern tax system. This tax has been adopted by all sorts of countries as an important instrument to generate revenue required to finance state activities. This tax is also considered as a fairest tax since it can be tied with the taxable capacity of the taxpayers.

2.1.4 Taxation in Ancient Nepal

Reliable records about taxation in ancient and medieval Nepal are not available; however, tax has been one of the major sources of government's revenue from the ancient time in Nepal. Taxes were then levied on the merchants, travelers and farmers in the form of cash, kind and labor. On some occasion gold and agricultural products were also paid as taxes; but the nature of these taxes was temporary. In the Lichhavis regime, income taxes from agriculture and business were introduced as a direct tax for the first time in Nepal. Agricultural income tax was called "Bhaga". The 1/6, 1/8, and 1/12 quality of the land that they owned. Income tax, which was levied on business income, was called 'Kara'. There did also exist irrigation and religious tax during the regime of king Ansubarma of Nepal. (Shaun, 1995:236)

2.1.5 Taxation in Unified Nepal (1768-1846)

After unification of kingdom of Nepal, expenses for administration, military and other operational activities were increased significantly. During that period, taxation has been taken as main source of revenue and different types of taxes like land tax, transit tax, market duties, various levies and fines, forest product tax and mining tax were levied.

Local administrations were directed "To take whatever is paid willingly by the people."

Taxes were collected from the three levels. (Agrawal, 1980)

- a) Royal Palace: To finance occasional and ceremonial needs. The taxes were broad based and progressive.
- b) Government: To finance administrative, military and other purposes assessed on official functionaries, occupational groups and other people.
- c) Local: Prerequisites of local officials, functionaries and mendicants.

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

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

2.1.6 Taxation in Rana Regime (1846-1950 A.D.)

Imposition and collection of taxes during 104 years oligarchic rule of the Rana family in Nepal prior to 1951 was the prerogative of the feudal rulers only those taxes, which suited the objectives, needs and whims of the ruling prime minister, were imposed.

No budget was framed during the Rana regime. Taxes were collected at the time of requirement due to lack of Income Tax Act and Finance Act. The collected taxes were directly deposited into the prime minister's Account.

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

collected on a contractual basis and 'Salami' which the government employees used to pay out of their salaries at a very small percentage.

Rana prime minister levied taxes for meeting specific expenditure of the royal household or extra ordinary expenditure necessitated by war or other crisis rather than mobilizing revenue in the nation. During Nepal-Tibet war (1955-56), the first Rana Prime Minister Jung Bahadur Rana had imposed a tax on the income of selected groups. Similarly, Bir Shamsheer imposed a levy of 1% in the official value of Jagir assignment of government employees in 1891, to finance the transportation of water pipe supply in the capital. Ranoddip Singh imposed a 50% tax in the income made by fisherman in Deukhuri from the sale of fish in 1882.

2.1.7 Income Tax in Modern Nepal

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

2.1.8 Gradual Development of Income Tax Act and Laws

2.1.8.1 Business profit and Remuneration Tax Act, 1960 (2017 B.S.)

The finance act, 1960, made provisions for the taxation of business profits and remunerations. An ordinance was issued by the king to collect the tax. In 1960, parliament of Nepal, enacted, "Business Profit and Remuneration Tax Act, 1960 (2017 B.S.)", which consisted of 22 sections. With the enactment of that act, the salary tax or personnel income tax was levied upon those individuals whose personal income exceeded Rs. 6000 per year. In the first three years, the exemption was Rs. 7000. An examination of tax files in the Kathmandu District office disclosed 577 personal income tax files of individuals who had paid taxes in one or more year.

Main feature of Income Tax Act 1960 were as follows:

1. Only remuneration and business profit were subject to tax. Deductions were not specified for the purpose of calculating the income.
2. Tax on remuneration was to be deducted at source.
3. The basis for calculating the tax liability for remuneration was the income of the current year and for the business profit, it was the profit of preceding year.
4. In case of default, fines up to Rs. 5000 were prescribed.
5. The tax payer was given the right to appeal against the tax assessment to local "Badahakim". There after appeal could be lodged at revenue court. Every appeal could be accompanied by security deposit for the amount of tax payable.
6. The tax officers were empowered to assess tax on the basis of best judgment estimates.
7. Profits from industries were granted a rebate of 25% and profits from small industries were granted a rebate of 50%.

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

2.1.8.2 Income Tax Act, 1962 (2019 B.S.)

The main purpose of the imposition of this act was not only to raise government revenue but also to reduce inequality of income and wealth distribution with social justice and to create regular tax paying habit of the taxpayer. The Income Tax Act,

1962 had 29 sections and it was amended in 1972 (2029 B.S.). It had provision of imposition of income tax in agriculture income, but this provision was abolished by the finance Act, 1966 (2023 B.S.). The additional features of this act were as follows:

1. Income was defined as kinds of income including income derived from business, remuneration, profession and occupation, house and land rent, investment in cash or kinds, agriculture, insurance business, agency and any other sources.
2. The personal as well as residential status of the tax payer for the tax purposes was defined.
3. The income tax assessment and collection procedure were specified along with the method of computing net income. Certain deductions were allowed to calculate net income.
4. The basis was specified for assessing tax on the best judgment estimates of the tax offices.
5. Provision was made for the installment as well as advance payment of the tax for the first time.
6. Carry forward of losses was allowed for two years.
7. Provision was made for the exemption of income tax for the new industries for a period of not exceeding ten years.
8. The act granted power to constitute net income assessment committee.

The changing socio-economic environment of the nation had for to change the Income Tax Act, As a result, Income Tax Act, 1974 (2031) came into existence.

2.1.8.3 Income Tax Act, 1974 (2031 B.S.)

The Income Tax Act, 1974 can be said to be the defined form of Income Tax Act, 1962 (Dhakal, 2057). It had 66 sections. This act has explained various aspects of taxes, containing many provisions for taxation. This act was amended for eight times i.e. 1977 (2034), 1979 (2036), 1980 (2037), 1984 (2041), 1985 (2042), 1986 (2043), 1989 (2046) and 1992 (2049) to make it more practical and to eliminate confusing terms. His majesty's Government enacted the income Tax Rule, 1982 (2039) in 1982 (2039-1-27) in accordance with the authority given under sections 65 of Income Tax Rule 1982, the

financial act is also equally applicable for the proper administration of income tax in Nepal. Some of the features are as follows:

1. This act had clearly defined about income tax, taxpayer, year of income, personal status of taxpayer, non-resident taxpayer, net income and so on.
2. Five heads of income sources were specified Viz.
 - a) Agriculture,
 - b) Industry, Business, profession or vocation,
 - c) Remuneration,
 - d) House and land rent and
 - e) other sources.
3. Method of computing the taxable income from each head had been specified with deductions allowable.
4. The act had made it obligatory for taxpayer to register their industries, business, profession or vocation in the tax office and any changes should be notified.
5. Carry forward of losses is allowed for within subsequent three years.
6. Provision was made for self assessment of tax for the first time in Nepal.
7. Provision was made relating to deduction for life insurance premium and contribution made for philanthropic purpose.
8. Taxpayer was required to keep accounts and records of the income and to be preserved for six years.
9. Provision was made to make agreement for avoidance of double taxation with foreign government.
10. Provision was made relating to reassessment or additional assessment of tax.

2.1.8.4 Income Tax Act, 2002 (2058 B.S.)

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 Income Tax Act, 2002 (2058), since first April 2002. (19th chaitra, 2058).

This act was brought in Nepal to avoid the following defects of Income Tax Act, 2031 (Kandel, 2003)

- a) Narrow base of tax.
- b) Levying tax only on the income originated in Nepal.

- c) Dispersion of tax related acts, i.e. income tax related provisions were given in different acts.
- d) Low penalty rate to tax evader.
- e) Incompatible to self-assessment, and
- f) Unsuitable to modern economy.

The main objectives of ITA, 2058 are presented below:

1. To levy tax on all income sources and income earning transactions.
2. To impose uniform tax to all people and all sources.
3. To make income tax revenue more productive and elastic.
4. To develop the tax system by means of extended scope, clear-cut, transparent and simple procedure.
5. To make accountable and improved tax administration.
6. To reduce economic cost neutralizing income tax.
7. To emphasize statement based an accounting system.
8. To make the taxpayers responsible by introducing the process of self-assessment system.

2.1.8.4.1 The key Features of Income Tax Act, 2058 are:

1. All income tax related matters are confined within the act by abolishing all tax related concessions, rebates and exemption provided by different acts.
2. 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.
3. The act has introduced a pool system of charging depreciation. Intangible assets are also depreciated.
4. The act has firstly introduced taxation on capital gains.
5. The act has provided liberal set-off and carry forward/backward provisions and inter head adjustments of losses are clearly specified.
6. The act has provided a stringent fine and penalty for the defaulters.
7. The act has introduced a provision for administrative reviews to allow the tax administration to correct mistakes made by tax administration internally.

8. Global income of a resident are made taxable. Non-resident are also taxed on their income with source in Nepal.
9. List of expenses is inclusive. All expenses relating to income have been made admissible.
10. The act has made provision of international taxation. Foreign tax credit has been introduced for the first time.
11. The act has separated administrative and judicial responsibilities by distinguishing civil liabilities of the taxpayers from criminal liabilities (Bhattarai and Koirala, 2061).

2.1.9 Legal Provisions of Income Taxation in Nepal

The function of revenue collection has remained one of the key activities of the government from ancient time in Nepal. During that time, very few economic activities were operated in the country. Hence, government could not collect huge amount of money in the form of taxation. At that time, taxes were levied to the merchant travelers and farmers in the form of cash, kind of 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 (Regmi, 1971:55).

In the Lichhavis regime, income taxes from agriculture income and business were introduced as a direct tax for the first time in Nepal. Tax on agriculture income was called 'Bhaga' and tax on business was called "Kara". Irrigation tax and religious monuments preservation taxes also existed at the time of king Ansubarma of 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 mints and the export of forest products, birds, animals and various levies and fines. Taxes were collected at three levels: Royal Palace levies, government levies and local levies. The various taxes levied during that period were narrow in base and were imposed primarily on occupations and economic activities, not in income or property. There was no taxation of income in the modern sense of income tax.

During the period of Rana regime, there was not 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 not provision of separating the personal income of prime minister and state treasury. There was not system of preparing government budget. The surplus of revenue over expenditure was considered as the personal income of the Rana prime minister.

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

There was no direct tax in the country except land tax collected 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 administrative system. After the advent of democracy in the country in 1951, no taxes are levied and collected in Nepal except in accordance with law.

2.1.10 Sources of Income

Income is the accretion of wealth or Purchasing capacity of a person or entity. According to Income Tax Act, 2058 it 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, Income Tax Act, 2058 has specified sources of income into three heads.

1. Income from a business (Section 7)
2. Income from employment (Section 8)
3. Income from investment (Section 9)

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

2.1.11 Method of Income Tax Assessment

Income Tax Act, 2058 has specified three types of assessments. They are as follows.

1. Self Assessment (Sec. 99)
2. Jeopardy Assessment (Sec. 100)
3. Amended Assessment (Sec. 101)

Self-assessment is done by the taxpayer himself. He submits a return of income for an income year under section 97.

As per the income tax act, 2058 jeopardy assessment is done under the following circumstances:

- a. The person becomes bankrupt, is wound-up, or goes into liquidation.
- b. The person is about to leave Nepal indefinitely.
- c. The person is otherwise about to cease activity in Nepal or.
- d. The department otherwise considers it appropriate.

The section 101 of Income Tax Act, 2058 also empowers tax officials to make amended assessments to adjust the assessed person's liability to tax in such a manner as, according to the departments best judgment, is consistent with the intention of this Act. The department may amend an assessment according to its best judgment for as many times as it thinks appropriate within a period of four years.

2.1.12 Appeal

Income Tax Act, 2058 had the provision of two alternatives to the taxpayer who thinks the tax assessment of tax offices is unfair. He could either go to the director general of the Income Tax Department or to revenue tribunal. Income Tax Act, 2031 has not such provision. Instead, it has managed taxpayers first to go to Director General of Inland Revenue Department for review of decisions and then if unsatisfied with the decision of Director General, he/she can go to Revenue Tribunal.

Sec 115 of the Act has stated that a person who is aggrieved by a reviewable decision of the Director General of the Inland Revenue Department may file an objection in writing. While filing the objection, he should specify the grounds in detail upon which it is made such objection should be made within 30 days after the decision is made. In case of the time over for applying to show objection to a reviewable decision, the taxpayer can apply for extending the period within 7 days of the time lapse. In this case, if the department finds reasonable cause, it can extend the period, not exceeding 30 days, by which an objection must be filed. A reviewable decision may not be stayed or affected if more than 50 percent of tax that is otherwise payable is not paid. After consideration of a person's objection, the department may allow the objection in whole or part by amending the decision or disallow the objection and a notice in this respect is served to the concerned person. If the tax department fails to serve a person with an objection decision within 90 days of an objection being filed, the person may, by notice in writing filed with the Department, take the Department as having made a decision to disallow the objection.

Sec 116 of the Act has specified that a person who is aggrieved by an objection decision may appeal to the Revenue Tribunal in accordance with the Revenue Tribunal Act, 2031. If the person has appealed, he should file a copy of the notice of appeal with the department within fifteen days. However, the operation and enforcement of an objection decision is not stayed or otherwise affected by an appeal. If Director General of the Department has made the decision relating to administrative review the appeal to Revenue Tribunal would be effective.

2.1.13 Interest and Fines

The Act has provided rights to tax officers to impose interest and fines. The circumstances in which a tax officer imposes interest and fine are pointed out below.

1. Interest for understating estimated tax payable by installment (sec 118):

When an installment payer's estimate of tax payable in each installment is less than 80% of the correct amount 15% p.a. for each month and part of month from the date of due until the date of tax payable on assessment.

2. Interest for failure to pay tax (sec. 119):
15% p.a. for each month and part of a month on the amount of tax outstanding.
3. Fine for failure to maintain documentation or file statements or returns of income (sec. 117):
0.1% p.a. on assessable income without any deduction or Rs. 1000 p.a. whichever ever is higher.
Withholding agent failing to file statement:
1.5% p.a. for each month or part of a month from the month of tax required to be withheld.
4. Fine for making false or misleading statements (sec. 120):
50% of the underpayment of tax if it happens to be without knowingly or recklessly.
100% of the underpayment of tax where it is made knowingly or recklessly.
5. Fine for aiding or abetting another person to commit an offence or counsels or induces another person to commit such an offence (sec 121):
100% of the underpayment of tax.

2.1.14 Corporate Tax and its Development in Nepal

2.1.14.1 Concept of Corporate Tax

A corporate body or company is an artificial person created by law. A company is a legal person just as much as individual. It is separate and distinct from its individual members. A company like a natural person can do everything. It can conduct a lawful business and enter into contracts with others in its own name. A company or corporate body is legal organization that is voluntarily created, organized or chartered under law. It is artificial people which can own property execute contracts, raise debts and generate profits. Corporate tax, therefore, is a tax. Levied on companies or corporate bodies in contrast to unincorporated enterprise. It is the tax on capital income that occurs in the form of profit and originates in the corporate sector i.e. company. The history of tax was started from 1909 in USA when 1% excise was levied on corporation

i.e. companies in the ground of the privilege they enjoy. Since then, corporate tax is contributing a substantial amount of revenue to the state treasury of the most of the developed and developing countries. The statutory rate percent, however, was very low in initial period, increased vehemently later on after First World War and again started to be sown turned since 1980's (Kandel, 2000:186).

2.1.14.2 Development of Corporate Tax in Nepal

The history of corporate tax is not so long. This tax was introduced only in 1960 with the Business profit and Remuneration tax Act, 1960 for the first time. Initially, corporate income tax was not differentiated from personal income tax. All the taxpayer persons, companies and private firms were imposed at the same rate with progressive and exemption limit prescribed by finance Act of 1960 to 1964. The tax exemption given to companies are similar to personal taxpayer, was withdrawn from the financial year 1965/66. A separate tax system to companies was introduced by the finance Act, 1976.

The third income tax act was introduced in 1974 with new changes and provisions than old one. A separate tax system to companies was introduced by the finance Act, 1976. Finance Act, 1985 made a provision of giving 5% tax rebate from highest marginal rate of 55% to listed public companies and government enterprises. Fiscal year 1986/87 was the year when the corporate tax was really recognized by imposing a flat rate of 40% tax on taxable income of the listed companies. The same finance Act imposed tax on dividend also to be deducted at source at the rate of 20% which after the filing of return by shareholders was to be reconciled. But the dividend tax system was changed exempting dividend to a level of 85% in 1987/88 and cent percent in 1990/91. Compulsory self tax for public and private limited company was enacted from the financial year 1994/95. This change support to end the discrimination between private company and public company. Another major changes was carried out in the fiscal year 1998/99, was the inclusion of dividend of non industrial companies within the tax net.

Nepal originally combined corporate income tax with individual income tax. The same rate structure was designed for corporate income and other income for many years. In

1986/87, a flat rate corporate tax was introduced for government corporations and public limited corporations listed with security exchange center. Corporate tax was extended to private limited companies in 1993/94 and partnership firms in 1995/96 (Khadka, 1997)

After enactment of Income Tax Act 2002, the corporate tax levied upon general industries is 25%, 30% for insurance company and financial institutions. Trading companies are levied tax at the rate at 25%, manufacturing industry at 20% and specials Sector Company at 20%. Export profit was taxed at a level of 8% or 0.5% of sales as per finance Act, 2057 was changed by the fiscal Act, 2058 has recommend, export profit from industry sector and trading sector are taxed at 20% and 25% respectively.

2.1.14.3 Corporate Tax Base in Nepal

There are controversies as regards to the choosing of corporate tax base since there may be various bases of taxation. For instance, these bases may be income, cash flow, turnover, total assets and added value etc. Among there, two base income and cash flow are mostly considered by the tax expert (Kandel, 2005:65)

The standard tax base is corporate income, which is the difference between revenues from the sale of goods and services plus financial income on the one hand, and wages, depreciation, inventory costs plus interest on the other. Such costs are revenue expenses incurred in the ordinary course of conducting day to day operation, and amortization of capital costs. Under the income-based tax system, many developing countries provide substantial tax incentives in the form of exemptions and deduction such as accelerated depreciation, Investment tax credits or allowances, tax holiday etc.

Tax base may depend on the relation between corporate tax rates and personal tax rates. Different countries of the world have different choice of base for corporate tax. Most of the countries prefer corporate-profits or book profits as the tax base. For, book profits as a tax base are stronger and superior than other types of tax bases. (Khadka, 1994:212)

If income is taken as the base of taxation, it is called income basis or net profit basis. It means deduction of interest on debt and depreciation of fixed assets from gross profit and adjustment of capital gain, stock appreciation or depreciation etc. Since, calculating tax base is adding up all the incomes of the company and deducting expenses incurred in earning the income. However, because of its cumbersomeness in finding out taxable income, modern tax experts are in favor of replacing it. The main causes of cumbersomeness are treatment of revenue and expenses on accrual basis, treatment of depreciation under historical cost, measurement of capital gain and effect of inflation either interest or valuation of stock. The cash flow tax, on the other hand, is the alternative, considered by economists and tax experts to replace income based taxation. (Kandel, 2000:116)

Like other countries of the world, Nepal is also following the method of making income as base for corporate taxation. The procedure of finding out taxable income is adding up the all items of revenues and deducting all expenses which are allowable.

2.2 Review of Related Study

2.2.1 Review of Thesis

Mr. Shakya (1995) had presented his thesis entitled "Income Tax in Tax Structure of Nepal" and had tried to give origin and meaning of income tax with its historical review, structure of government revenue in Nepal, importance of income tax, contribution of income tax to total tax revenue and total revenue.

In his study, he stated that the structure of the government revenue in Nepal is a composition of the tax and non-tax revenue. The Tax revenue is the most important source of government revenue which occupies 80% share in the total government revenue in the year 1993/94. The ratios of income tax to GDP, total revenue, total tax revenue and direct tax revenue had an increasing trend. But the increasing rate was low in comparison to other countries. He further added that the change in tax rate and exemption limit had made the assessment of income tax more complicated which had given plenty of opportunities to evade income tax which exist as a major problem.

Lastly, he had recommended many suggestions for the sound and effective income tax such as honest and effective tax administration, scientific method in tax collection and encouragement to self-assessments of tax.

Mr. Tripathee (1995) had presented a thesis entitled "Income Tax System in Nepal and Some Potential Areas for Reform". Deficit annual budget and deficit financing of the nation were his main concern of the study where he had tried to show the tax structure in Nepal, rule of income tax in Nepalese economy, income tax administration and tax evasion in Nepal along with reforms.

Mr. Tripathee had conducted his research using the 15 years data since 1974/75 to 1989/90. Primary data were also used which were collected through opinion survey within Kathmandu Valley. Simple statistical tool such as mean and time series were used to analyze the data, graphs, charts and diagrams were also used as necessary.

From that research, he had concluded that tax from individual sector had provided maximum contribution in income tax structure and above 80% of total revenue was collected through taxation. Tax evasion had increased due to poor tax administration and delay in the process of tax assessment. Lastly, he had recommended levying tax on agriculture income. Tax holiday should be given to the firms and administration should be sound and efficient.

Mr. Shauh (1995) had conducted a research on the topic, "Contribution of Income Tax in National Revenue of Nepal". His research problems were increasing resource gap and how income tax can be the means for resource mobilization. The main objective of this research were; to show the contribution of income tax in government revenue, to show the resource gap in Nepalese Finance, to highlight the importance of income tax as a source to avoid financial deficit, to find out the rate and per capital burden of income tax and trend and structure of income tax in Nepal.

His research design was historical and descriptive. He had used only secondary data of 21 years from 1974/75 to 1994/95. Data collection and analysis procedures were,

consulting the required government and non-government offices, and simple arithmetic rule chart and diagrams were applied to analyze data. From that research he had found out and concluded that income tax can be the vital source for internal resource mobilization to fulfill resource gap. Only 0.35% of total population came under the categories of tax payers in Nepal during his research period. He found that collection of income tax was gradually growing and the contribution of income tax in total tax revenue and total national revenue were 9.95% and 7.94% respectively. Similarly, he also concluded that individual tax payer had higher contribution in income tax than salaried tax payer.

Mr. Panta (1996) had presented a thesis entitled, "A study on Income Tax Management in Nepal." The main objectives of his research were to find out the share of income tax to government revenue, to review the income tax system and to identify the problem of income tax management. His research was based upon secondary as well as primary data. The primary data were collected within Kathmandu valley through interview, questionnaire etc.

He had concluded that income tax was a major source of internal resource mobilization, the income tax system was not efficient and income tax assessment was not efficient. Evasion of income tax was major constraint for resource mobilization. He also added that corporate tax rate was found high and exemption limit was not sufficient.

Lastly, he had recommended that income tax net should be widened, assessment procedure must be improved and income from agriculture and capital gain should be taxed.

Mr. Poudyal "Kshetry" (1998) had submitted a Ph. D. thesis entitled, "Corporate Tax Planning in Nepal". This thesis report was aimed to examine the implications of tax factors in strategic planning, project planning and operational planning in Nepalese companies. He had found that the majority (90%) of the companies (Sample size of the study) considered tax factor while selecting the business. He also found the positive correlation (+0.8) between tax rate and the debt equity ratio because of interest paid on

debt is a tax-deductible item. Similarly the correlation coefficient between average fixed assets and corporate tax was (0.75) in large 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 in fixed assets in large companies resulted in decrease in the corporate tax. He addressed that the tax planning should be considered while making corporate planning and companies should set up separate tax section to get maximum benefit of provisions, provided by the law. However, tax assessment under the best judgment blocked the application of tax planning in corporate planning. He had recommended that tax incentives should be given to non-industrial companies too, and tax rate should be differentiated for resident and non-resident companies.

Mr. Kandel (2000) also presented the Ph. D. thesis entitled "Corporate Tax System and Investment Behaviour in Nepal". He undertook the research work to find out the problems relating to corporate tax, which blocks the development of the private investments. The main objectives of his study were 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. He showed the relationship of private investments with average effective tax rate, marginal effective tax rate and tax incentives in Nepal. He found that debt-financed project are almost negative i.e. -17% and positive for equity financed project and debt-equity project by 27% and 19% respectively. He had also found the impact of inflation to the marginal effective tax rate. According to him, the statutory tax rate deduction had impact on private investments by 60% to 20%. In this regard, he had showed the adjusted value 0.87 at 5% level of significance. He had concluded that the statutory tax rate was in moderate level under the financing options: debt, mix and equity i.e. it was not much destructive. The relationship between inflation rate and effective tax burden in Nepal was Negative.

Mr. Lamsal (2001) had also presented a thesis entitled "A Study on Contribution of Income Tax on Government Revenue". His research had mainly focused on the removing and controlling income tax evasion for better resource mobilization. As his main objective was to analyze the impact of income tax evasion in government revenue

of Nepal, he set further objectives which were to identify the ways and causes of income tax evasion, to estimate the volume and tendency of income tax evasion in small trade sectors and to examine the role of income tax in utilizing the resources in Nepal.

Mr. Lamsal had conducted the research following analytical as well as descriptive research design. Most of the data were from secondary sources and some were from primary sources. Primary data were collected through opinion survey, field visit and interview. Simple statistical analysis such as average and percentage were used for data analyzing tools; Graphs, Charts, and tables were used to interpret visually the findings of the research.

From the research, he had concluded that there was widespread evasion of income tax in Nepal and income tax is a suitable means for raising government revenue. He had recommended measures for controlling tax evasion by controlling illegal business activities, increasing penalties and fines to tax evader, compulsory maintenance of accounts etc.

Mr. Serchan (2003) had covered tax structure, role of income tax and legal provision of income tax in his thesis. He had specially focused on provision of fines and penalties of income tax Act. He found the dominating role of tax revenue to the total government revenue. Income tax had occupied third position during his study period and it was in increasing trend. The tax/GDP ratio was not found satisfactory. There was dominating role of corporate income tax but it was in decreasing trend and contribution of individual income tax was in second position with increasing trend.

He had recommended measures for revising the provision of fees and penalties, introduction of reward, prize to the tax payer, clear act, rules and regulation regarding Income tax, timely revision of income tax policy, and computerized system for payment of income tax. This study was done with the objective of analyzing tax structure of Nepal, analyzing the provision of fines and penalties under income tax law, Awareness of taxpayer towards fines and penalties etc.

Mr. Paudel (2006), conducted a research entitled “Role of Income Tax in National Revenue of Nepal” in order to fulfill partial requirement of Masters of Public Administration (MPA). The major objectives of his study were to study role of income tax in revenue of Nepal, evaluate prevailing income tax system, and examine issues relating to income tax. The major findings of study were as follows:

There was dominant contribution of tax revenue over non tax revenue to the total revenue of Nepal. Contribution of tax revenue was in increasing trend.

The Tax- GDP ratio of Nepal was not found satisfactory compare to other developing countries.

Nepalese income tax system is facing problems during tax collection such as: lengthy assessment process, lack of sufficient incentives to employees, inadequate power to income tax administrators, and lack of experts in the tax management, more tax evasion etc.

Tax payers were facing problems while paying tax because of misconduct of tax personnel, administrative harassment and complex tax laws and rules.

Reforming and controlling present taxation system, controlling open boarder with India, preventing illegal business, making effective administration, increasing tax coverage can contribute positively to the present tax system of Nepal.

Mr. Pokhrel (2007), in his thesis “Contribution of Income Tax on Tax Structure of Nepal” has conducted an empirical investigation. According to his investigation, income tax is a suitable means of raising government and tax education is necessary in Nepal for which 91.67% and 98.33% respondents have supported respectively. He found that inefficient tax administration, tax evasion and inappropriate objectives of income tax were the main causes of low collection of income tax in Nepal. Self assessment method of assessing income tax is most appropriate in Nepal. 70% of the respondents were in favor of fees, fines and penalties whereas remaining 30% were against it. The recommended measures of the respondents are effective tax management, training and development programs to tax personnel, development of check and balance system can bring efficiency in income tax system in Nepal.

2.2.2 Review of Books

A senior researcher in the field of Nepalese taxation, Dr. Agrawal (1978) had conducted a research entitled, "Resource Mobilization for Development: The Reform of Income Tax in Nepal". The main objective of his study were to examine the problem of growing resource gap in Nepalese finance in the context of the role of income tax, to examine the buoyancy and elasticity of income tax in Nepal including projection of income tax, to examine the ways and means for increasing tax consciousness in Nepalese people etc.

Dr. Agrawal (1980) had written a book entitled "Resource 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.

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 constraints in the effective functioning of tax system seem to be administrative deficiencies, poor tax paying habits, lack of taxpayer's education, complicated procedures and defective tax information system.

Dr. Khadka (1994) had written a book entitled, "Nepalese Taxation: A path for Reform". The book deals with both national and international taxes. The writer had described the scenario of Nepalese tax system from origin of income tax, adoption of quasi-global or a limited scheduler system, segregation of corporate income tax from individual income tax, increasing dependence an the presumptive basis, basic allowance and progressive rate structure, move from joint taxation to individual taxation and shift from itemized to flat system of standard expenses, experiment with

an advance tax on impacts and the existing structures, commodity taxes and poverty taxes. He had evaluated the Nepalese tax system base on conventional, theoretical concepts and suggested various measures for its improvement. The book had not been directly focused on corporate tax only but explains the whole Nepalese taxation system and structure for its reform.

Adhikari (2002) has discussed the legal provision of new Income Tax Act, 2002. His book is analytical rather than informative. Writer has not included administrative aspect, role and structure of income tax in his book. The book has only focused on the legal aspect of income tax. Agreement and protocol relating to avoidance of double taxation and the prevention of fiscal evasions with respect to taxes on income between different countries had also included in his book. (Adhikari, 2002)

Mr. Mallik (2003) had written a book entitled "Nepalko Adhunik Aayakor Pranali". This book especially deals with the thorough analysis of Income Tax Act, 2058 with examples. Every section of income tax act has been clarified with suitable examples. He had written about the development of existing income tax and need and importance of income tax system in Nepal. The new provision made by Income Tax Act 2058, about tax base, Computation of income, tax exempt amount, allowable deduction, Accounting of tax, capital gain, retirement saving and tax, dividend tax, Intonation tax auditing have been clarified precisely in his book. Similarly, the book had also explained about tax administration, documentation, information collection, payment of tax, installment tax, income statements, tax-assessment, tax collection, review and appeal, fees and interest, fine and penalties, tax rates and determination of provision of depreciation etc.

Mr. Aryal and Mr. Poudel (2004) had written a book entitled, "Taxation in Nepal". They had explained about the income tax system in Nepal along with house and land tax and value added tax. This book has been designed on the basis of the curriculum of B.B.S. It has been divided into three parts. In the first part of the book introduction and development of income tax, capital and revenue nature expenses and income items, entity and retirements saving, dividend tax, computation of income from business,

remuneration and investment have been explained in the second and third part respectively. The book also included proper bibliography and adequate appendix where various income tax, house and land rent and VAT related forms, schedules and format had been described. Lastly, he had recommended mobilizing additional domestic resources through taxation, redesigning the tax structure in order to increase the role of direct tax and reformation of income tax in Nepal.

2.2.3 Review of Research Reports and Articles

United Nation (1977) published a journal on public finance entitled, "Guidelines for improving tax administration in developing countries". The study was divided into your 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 taxpayer, taxpayer's education, information provider and assistance etc. The study had detail explained there functions and recommended some valuable suggestions to the developing countries.

Mr. Pant (2004) had written an article entitled, "Problems in Tax Administration and their Remedies" Published in Journal of Finance and development 'Rajaswa' 2004, April Vol. 1. He had comprehensively explained about the problems and their remedies related with tax revenue and major types of practical problems and challenges, in tax administration. He had highlighted on the major problems like showing limited amount of transaction at low selling price, low practice of issuing and taking bills, Hiding the real factory cost, Commercial fraud, lack of co-operation in tax auditing, legal ambiguity and complexity in implementation and lock of co-operation between Inland Revenue Department and Revenue Investigation unit. Meanwhile, he had recommended some valuable suggestions to solve the problems and to overcome the challenges. Such as managing statistical and information system, Using of fixed norms and standards for assessing selling price and factory costs, compulsory use of billing system, proper co-ordination of Inland Revenue office with various entities of HMG, Revenue Investigation Department and its related units.

Dr. Kandel (2004) had written an article entitled, "Are Tax Incentives Useful? If so, which one?" Published in journal of Finance and Development, 'Rajaswa', Volume. 1, 2004, April. In that article, he had tried to seek the answer from the survey of various empirical studies done in Nepal, India, Pakistan and Other western countries. He found that the tax incentives are still the controversial matter whether they promote the investments or not but he argued that most of the developing countries need tax incentives. The empirical study concluded that among different types of tax incentives, investment allowance or investment tax credit and accelerated depreciation is 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 within Nepal and outside Nepal.

He further added that the survey of the studies indicate that accelerated depreciation system had positive impact on investment. Reducing tax rate, especially followed after 1990s to the lowest rate was not a proper decision. That is why, if Nepal wants to go to tax incentives again, it should adopt investment allowance or investment tax credit, not the full tax holiday in future.

The Institute of Chartered Accountants of Nepal (ICAN) published a monthly journal on December 2005. Sinha presented an article named "Taxation-legal illegality"? He had described the taxpayer have been encouraged by the tax officials themselves to go courts over the complaints of their wrong doing because the authority is totally convinced that no immediately solution can be expected from the court of tribunal on short-span of time as long as they are in position. The Tribunal court reviews the decision of Inland Revenue department's director.

In 2005, The Kantipur daily published news about Income tax and VAT. The news presented the terms used in Income tax and VAT which is not clear. There is not friendly business environment between taxpayers and government. Similarly, the vocabularies used in tax act are very ambiguous and difficult.

In 2007, Mr. Neupane has published an article in economic bulletin 'Rajaswa', which shows the contribution of income tax to total tax revenue, has decreased from 23.93% to 20.83% in the FY056/057 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 of instable political condition.

In 2007, The Kantipur daily has published news about tax paying behaviors in Nepal and European countries. The news presented that 95% of taxpayer in European countries were willing to pay tax but in Nepal 95% taxpayer want to hide the income and they did not pay tax as per rules and regulation.

2.3 Resource Gap

The role of revenue is crucial for the overall development of the country. Since more than 80 percent of the total revenue is collected from the tax source, efficient tax system has to be developed and strengthened. In recent years, the government has taken several measures to reduce tax-induced distortions strengthening tax administration, simplifying tax laws and procedures to make them more precise and transparent. Since the government's main concentration is always on increasing revenue, it's very important for us to know about the pros and cons of activities taken by government as we all are directly or indirectly involved in this subject matter.

Nepalese corporate sector is small and stagnant in nature. The performance of public sector, private and even government sector is poor. Contribution of income tax from corporate sector plays vital role in Nepalese economy. Despite of the fact that the considerable contribution of corporate sector in the economy of developing countries, I found very few studies are done in this subject matter which is not sufficient as per its importance. So, this study has been undertaken analytically and intensively to analyze the structural composition of income tax in Nepal, to find about the condition of problem in income tax collection, efficiency of income tax administration and to

analyze corporate income tax contribution to government revenue and fulfilling the resource gap from an internal source.

CHAPTER III RESEARCH METHODOLOGY

This chapter is concerned with detail discussion of the methodology used in this study by covering the procedure of getting research problems answers as per the objectives. There are five parts as Research Design, Population and Sampling, Nature and source of data, Data collection procedure and Data processing and Analysis procedures.

3.1 Research Design

This study includes three types of research as descriptive, analytical as well as empirical. The study of income tax act, the role of income tax, indirect tax and direct tax in total tax revenue etc. is done as a part of descriptive research. Analytical research is conducted to analyze the trend and contribution of income tax in government revenue of Nepal, the effectiveness of income tax administration, effectiveness of income tax revenue collection in Nepal etc. It is mainly done through the secondary source of data for empirical research, the opinion of the 75 respondents associated with distinct denomination i.e. tax experts, tax administrators and taxpayers were collected through structured questionnaire. The questionnaire included the role of income tax to national revenue; major weakness of income tax act, effectiveness of tax administration, problems of tax payers, loopholes at income tax act 2058, poor income tax collection etc. In this way, research design of this research is descriptive, analytical and empirical.

3.2 Population and Sample

The targeted whole area relating to government revenue or national revenue is set for the research population. In order to fulfill the objectives, the 75 sample size from Kathmandu is selected. The total number of questionnaire distributed were 90 among which only 75 were properly filled up and used. The sample size was selected from three different groups of respondents with the consultation of supervisor and best judgment of the researcher. The following table shows the group of respondents and sample size

S.N.	Group of Respondents	Total Sample	Respondents
1	Tax Administrator	30	25
2	Tax Expert	30	25
3	Tax Payer	30	25
Total		90	75

3.3 Nature and Source of Data

Necessary data and information to describe this study has been collected from primary as well as secondary sources.

A. Primary Data

Primary data were collected through administering structured questionnaire to sample population. The same questionnaires were distributed to all respondents. Tax administrators are selected from Inland Revenue department related offices situated in Kathmandu. Tax experts are the chartered Accountants, Registered Auditors. Tax payers are selected representing various sectors i.e. manufacturing company, trading company, industries, private banks, finance company, travel and tours, consultancy firms etc.

B. Secondary Data

Secondary data and information are obtained from various sources specifies a below.

1. Budget speech of various years, Ministry of Finance, Government of Nepal.
2. Economic survey of various years, Ministry of Finance, Government of Nepal.
3. Books related to income tax and public finance.
4. Dissertation related to income tax.

5. National and international news papers, journals and news magazines.
6. Official website of Inland Revenue Department: www.ird.gov.np
7. Official website of Ministry of Finance: www.mof.gov.np
8. Reports and records of Inland Revenue Department,
9. Other relevant records and data.

3.4 Data and Information Collection Procedure

Data and information used in this study is collected from primary and secondary sources. To get accurate and actual information in time all questionnaires were distributed and collected personally through field visit. The numerical data or secondary data are collected from the annual reports of IRD/N (Inland Revenue Dept, Nepal) economic survey of ministry of finance, publication of CEDA/TU, budget speeches etc.

3.5 Data Processing and Analysis Procedures

For the analysis, all collected data and information of various aspects of income tax was arranged in order and processed. Then, the descriptive tools and statistical tools such as simple percentage, simple average, graphs, charts, diagrams, Table time series analysis etc, have been applied in the way of analysis so that the findings could be presented and interpreted precisely and properly in order.

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

4.1 Tax Structure of Nepal

Modern economic planning of Nepal had started with the initiation of first economic planning in 1956. Since then, taxes have been used for the achievement of national economic goals. So, taxes play vital role to the economic development of Nepal. Tax structure of any country comprises both direct and indirect taxes.

4.1.1 Composition of Total Revenue

Total Revenue of Nepal is composed of both tax and non-tax revenue since the presentation of first national budget in 1951/52 by HMG.

Table 4.1 shows the composition of total revenue of government, which includes tax and non-tax revenue from FY 2000/01 to 2007/08. It seems that the share of tax revenue has always been greater than the share of non-tax revenue. In FY 2000/01 share of tax and non-tax revenue is 77.19% and 22.81% respectively, however it is 79.45% and 20.55% in FY 2007/08. It indicates that tax revenue plays the significant role in financing government expenditure. Tax revenue has been placed as a major source of government revenue in Nepal.

The composition of total revenue from fiscal year 2000/01 to 2076/08 is given below.

**Table No. 4.1
Composition of Total Revenue**

(Rs. in

Million)

Fiscal Year	Total Revenue	Tax Revenue	% of Tax Revenue	Non-Tax Revenue	% of NTR on TR
2000/01	37251	28752.90	77.19	8498.10	22.81
2001/02	42893.70	33152.10	77.29	9741.60	22.71
2002/03	48893.90	38865.10	79.49	10028.80	20.51
2003/04	50445.60	39330.60	77.97	11115	22.03
2004/05	56229.70	42587	75.74	13642.70	24.26
2005/06	62331	48173	77.29	14158	22.71
2006/07	70122.70	54104.70	77.16	16018	22.84
2007/08	72282.10	57430.40	79.45	14851.70	20.55

Source: Economic Survey, 2009

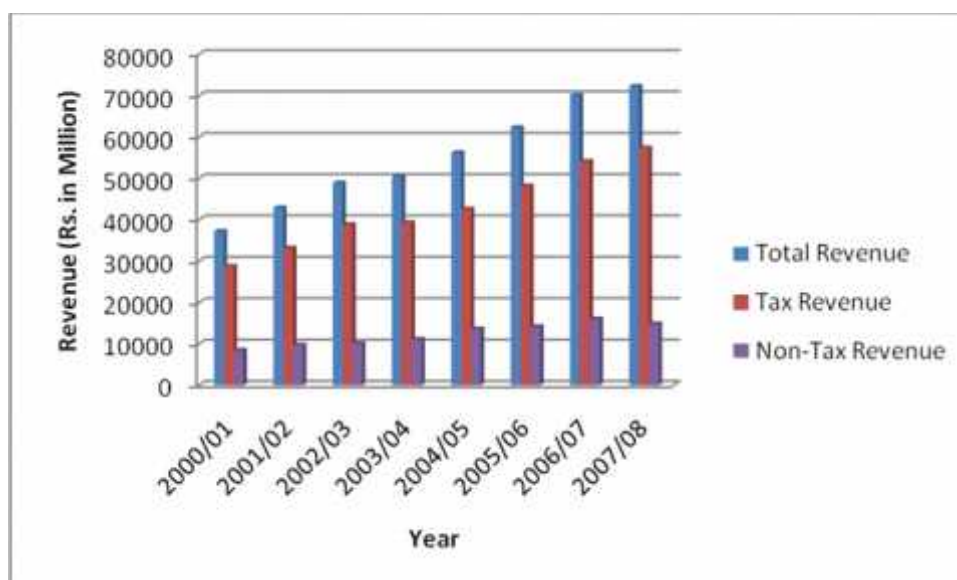
The above table reflects the increasing trend of tax revenue from the fiscal year 2000/01 to 2006/07. It was Rs. 28752.90 million in FY 2000/01 and increased to Rs. 57430.40 million in FY 2007/08. But the percentage contribution of tax revenue seems to be fluctuating in different years. The contribution of tax revenue to total revenue was maximum i.e. 79.49% in FY 2001/02 and minimum 75.74% in FY 2004/05 during the study period. The non-tax revenue is also in increasing trend for the first 7 years but it is decreased from Rs. 16018 million to Rs. 1485.70 in last year i.e. FY 2007/08.

The percentage contribution of non-tax revenue to total revenue is also fluctuating during the study period. It was decreased to 20.51% in FY 2002/03 and increased up to 24.26% in FY 2004/05. During the FY 2007/08 the contribution of non-tax revenue to total revenue is only 20.55% however the contribution of tax-revenue to total revenue is

79.45% in the same year from the above figure it is clear that the tax-revenue has covered the major portion of government revenue.

The contribution of tax and non-tax revenue on total revenue is shown in the following bar diagram.

Figure No.4.1
The Contribution of Tax and Non-Tax Revenue on Total Revenue



4.1.2 Composition of Tax Revenue

Tax revenue is composed of direct tax and indirect tax. Income Tax, property tax, Tax and interest are included in direct tax. Indirect tax includes customs, Excise duty, VAT etc. The composition of Nepalese tax revenue is presented in Table 4.2 in terms of direct and indirect tax revenue from FY 2000/01 to 2007/08.

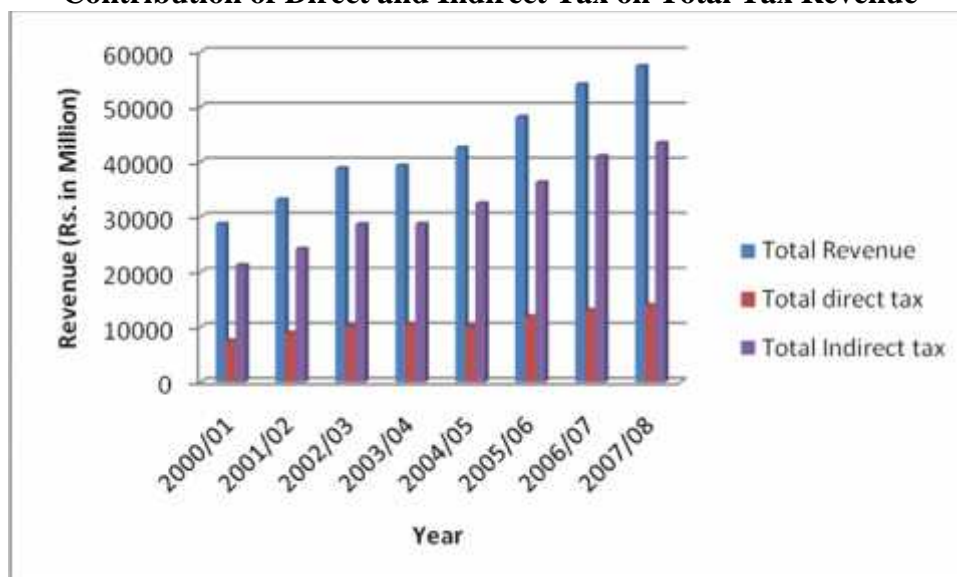
Table No. 4.2
Contribution of Direct and Indirect Tax on Total Tax Revenue

Rs. in Million

Fiscal Year	Total tax Revenue	Total direct tax	% share of direct tax	Total Indirect tax	% share of Indirect tax
2000/01	28752.90	7516.10	26.14	21236.8	73.86
2001/02	33152.10	8951.5	27	24200.6	73
2002/03	38865.10	10159.4	26.14	28705.7	73.86
2003/04	39330.60	10597.5	26.94	28733.1	73.06
2004/05	42587	10105.8	23.73	32481.2	76.27
2005/06	48173	11912.6	24.73	36260.4	75.27
2006/07	54104.70	13071.8	24.16	41032.9	75.84
2007/08	57430.40	13968.10	24.32	43462.3	75.68

Source: Economic Survey, 2009

Figure No.4.2
Contribution of Direct and Indirect Tax on Total Tax Revenue



The above table shows the increasing trend of total tax revenue thereby increasing its contributing factor i.e. direct and indirect tax. In FY 2000/01 the amount of direct and indirect tax is Rs. 7516.10 million and 21236.8 million respectively. The indirect tax is in sharp increasing trend however the direct tax is decreased in FY 2004/05 from Rs. 10597.5 in FY 2003/04 to Rs. 10105.8, in spite of its increasing trend. The share of direct and indirect tax in FY 2007/08 is Rs. 13968.10 and Rs. 43462.3 respectively.

The % share of direct and indirect tax to total tax revenue is 26.14% and 73.86% respectively in FY 2000/01. But in FY 2007/08 this portion is changed into 24.32% and 75.68% respectively. The contribution of direct tax to total tax revenue is decreased to

23.73% in FY 2004/05 which is lowest among other years. But it increased gradually and covered 24.73% in FY 2005/06. Similarly, the share of indirect tax also decreased to 73% of total tax revenue. And gradually increases to 73.86% in FY 2002/03. The share of indirect tax is maximum i.e. 76.27% in FY 2004/05. This means that the share of direct tax is minimum and share of indirect tax is maximum in the same fiscal year i.e. 2004/05. It may be due to unfavorable economic environment in the country.

Above table makes us clear that major portion of tax revenue is covered by indirect tax. And it is also in increasing trend. The share of indirect tax has increased from 73.86% in FY 2000/01 to 75.68% in FY 2007/08. But direct tax is 26.14% in 2000/01 and decreased to 24.32% of total tax revenue in FY 2007/08. It indicates that the income level of people is in decreasing trend in one hand and promotion of importing goods from other countries on the other. To direct the economy in the channel of development, it is necessary to increase the share of direct tax, ultimately decreasing the share of indirect tax. Therefore attention should be paid on the sufficient resource mobilization through internal sources.

4.1.3 Composition of Indirect Tax

Nepalese tax structure is heavily dependent on indirect taxes which constitutes the major portion of total tax revenue. Nepalese tax revenue is dependent mainly on international trade and VAT on goods and services supplemented by taxes on income and property to some extent. The major components of indirect tax in Nepalese tax structure constitutes custom duty, excise duty, VAT etc. Custom duty has been classified mainly into import duty and export duty. Following table shows the composition of indirect tax:

Table No. 4.3
Major Sources of Indirect Tax and Their Relative Percentage to Indirect Tax
Rs. in

Million							
Fiscal Year	Indirect tax revenue	Customs	As % of IDT	Excise Duties	As % of IDT	VAT	AS % of IDT
2000/01	21236.8	9517.7	44.82	2953.2	14	8765.9	41.28
2001/02	24200.6	10813.3	44.68	3127.6	13	10259.7	42.41

2002/03	28705.7	12552.1	43.73	3771.2	13.14	12382.4	43.13
2003/04	28733.1	12658.8	44.06	3807	13.25	12267.3	42.7
2004/05	32481.2	14236.4	43.83	4785.1	14.73	13459.7	41.44
2005/06	36260.4	15554.8	42.9	6226.7	17.17	14478.9	39.93
2006/07	41032.9	15701.6	38.27	6445.9	15.71	18885.4	46.02
2007/08	43462.3	15344	35.30	6507.6	14.97	21610.7	49.72

Source: Economic Survey,

2009

Note:

) Value Added Tax includes sales Tax, Entertainment Tax, Hotel Tax, Air Flight Tax and contract Tax.

) Customs includes Imports, Exports, Indian Excise Refund, others.

The table reflects that the custom duty and VAT occupies major portion in Indirect tax. The total indirect tax revenue collected in FY 2000/01 is Rs. 21236.8 million of which Rs. 9517.7 million i.e. 44.82 percent is contributed by customs, 41.28% i.e. Rs. 6765.9 is covered by VAT and Rs. 2953.2 i.e. 14% is covered by Excise duty. The share of customs is continuously increasing from FY 2000/01 to FY 2006/07. But it is decreased in FY 2007/08. In this year customs amounted to Rs 15344 million which is only 35.30% of indirect tax revenue. The collection of VAT is decreased in FY 2003/04 from Rs. 12382.4 to Rs. 12267.3 million and their respective share is 43.13% to 42.7%. After that there is improvement in collection from VAT. In FY 2007/08 the total collection from VAT amounted to Rs. 21610.7 million representing 49.72% of total indirect tax revenue which is the highest collection from VAT during the study period. Such significant increase in VAT shows the improving consumption pattern of Nepalese market. The share of excise duty is also continuously increasing from FY 2000/01 to 2007/08. However, its percentage share in indirect tax is fluctuating during the study period. In FY 2000/01 its percentage contribution is 14% and increased to 14.97% in FY 2007/08. The highest contribution of excise duty is 17.17% in FY 2005/06 representing Rs. 6226.7 million. From the above table we can clearly see that the percentage contribution of excise duty to indirect tax revenue is not significantly changed although total collection from excise duty is increased.

4.1.4 Composition of Direct Tax

The major components of direct tax are income tax, land Revenue and Registration, Urban house and Land tax, vehicle tax and others.

Table No. 4.4
Components of Direct Tax and Their Percent to Direct Tax

Rs. in

Million

Fiscal Year	Direct Tax	Income Tax	IT as % of DT	Land Revenue & Registration tax	As % of DT	Urban house & land Tax	As % of DT	Vehicle tax	As% of DT	Others	As % of DT
2000/01	7516.10	6170.2	82.09	1003.1	13.35	123.3	1.64	219.4	3	0	-
2001/02	8951.5	7420.6	82.9	1015.9	11.35	118.5	1.32	396.5	4.43	0	-
2002/03	10159.4	9114	89.71	612.9	6.03	2.9	0.03	429.6	4.23	0	-
2003/04	10597.5	8903.7	84.01	1131.8	10.68	2.3	0.02	559.7	5.28	0	-
2004/05	10105.8	7966.2	78.84	1414.3	14	0	-	559.5	5.54	165.8	1.64
2005/06	11912.6	9245.9	77.62	1697.5	14.25	0	-	700.6	5.88	268.6	2.25
2006/07	13071.8	10159.4	77.72	1799.2	13.76	0	-	806.5	6.17	306.7	2.35
2007/08	13968.1	10373.7	74.27	2181.1	15.61	0	-	847.6	6.07	565.7	4.05

Source: Economic Survey, 2009

Above table shows that contribution of income tax to direct tax is higher than other tax and it occupies the largest share in the direct tax. The percent share of income tax to direct tax in FY 2000/01 is 82.09 percent amounting Rs. 6170.2 million. This gradually increases to 89.71% in FY 2002/03 amounting Rs. 9114 million. After the FY 2002/03 the percentage contribution of income tax is continuously decreased in FY 2003/04. its contribution to direct tax is 84.01 percent and in FY 2007/08 this share is decreased to 74.27 percent amounting Rs. 10373.7 million, so, this regular decrease in contribution percent of income tax to direct tax is not satisfactory. It needs to increase by widening the tax net.

The land revenue and registration has covered 13.35% of direct tax in FY 2000/01 amounting Rs. 1003.10 million. But in FY 2002/03 its share is decreased to 6.03 percent only. Afterwards it started to increase and its maximum contribution is 15.61% in FY 2007/08. The urban house and land tax has contributed 1.64 percent of direct tax in FY 2000/01 amounting Rs. 123.3 million, which has decreased gradually and reached to Zero percent since 2004/05 and thereafter.

Another major component of direct tax is vehicle tax which has covered 3% of direct tax in FY 2000/01 amounting Rs. 219.4 million. Its share to direct tax is continuously increasing thereafter. Its maximum share is Rs. 806.5 million which is 6.17% of direct tax. In FY 2007/08 the percent share of vehicle tax to direct tax is 6.07 % amounting Rs. 847.6 million.

The contribution of other sources to direct tax is also in increasing trend from FY 2004/05 and 2007/08 respectively.

4.1.5 Contribution of Direct Tax as Percent to GDP, Total Revenue and Total Tax Revenue

The contribution of direct tax as percent of GDP, total revenue and total tax revenue is shown below:

Table No. 4.5
Contribution of Direct Tax as Percent to GDP, Total Revenue and Total Tax Revenue

Rs. in				
million				
Fiscal Year	Direct Tax	Direct Tax as % of Total Tax	Direct Tax as % of GDP	Direct Tax as % of Total Revenue
2000/01	7516.10	26.14	2.28	20.18
2001/02	8951.5	27	2.44	20.87
2002/03	10159.4	26.14	2.58	20.78
2003/04	10597.5	26.94	2.61	21
2004/05	10105.8	23.73	2.31	17.97
2005/06	11912.6	24.73	2.51	19.11
2006/07	13071.8	24.16	2.38	18.64
2007/08	13968.10	24.32	2.31	19.32

Source: Economic Survey,
2009

From the table, it is clear that percentage share of direct tax to total tax revenue is 26.14 percent in FY 2000/01. Then it has increased to 27% in FY 2001/02 which is maximum contribution during the study period. In FY 2004/05 direct tax share to total tax revenue has decreased to 23.73 percent which is its lowest contribution. Afterwards its share is 24.73%, 24.16% and 24.32% in FY 2005/06, 2006/07 and 2007/08 respectively. The share of direct tax to GDP seems to be very low. It is only 2.28% in FY 2000/01 which is gradually increased to 2.61% in 2003/04. But the share is only 2.31% in FY 2007/08. From the above figures, we can conclude that there is not any significant improvement in contribution of direct tax to GDP in the last 8 years. In the other hand, the share of direct tax on total revenue was fluctuated. Its contribution is 20.18% in FY 2000/01 and its share is increased to 21% in FY 2003/04 and decreased to 17.97% in FY 2004/05. In FY 2007/08 its share is only 19.32% which is 1.32% higher than FY 2006/07.

4.1.6 Contribution of Various Taxes as % to GDP

The contribution of various taxes as % to GDP is given in the following table:

Table No. 4.6
Contribution of Various Taxes as % to GDP

Rs. in									
million									
Fiscal Year	Total Revenue as % of GDP	Total Tax Revenue as % of GDP	Direct Tax as % of GDP	Indirect tax as % of GDP	Income tax as % of GDP	Custom duty as % of GDP	Excise duty as % of GDP	VAT as % of GDP	Land Revenue & Reg. as % of GDP
2000/01	11.29	8.71	2.28	6.43	1.87	2.88	0.89	2.66	0.30
2001/02	11.71	9.05	2.44	6.61	2.02	2.95	0.85	2.80	0.28
2002/03	12.41	9.86	2.58	7.28	2.31	3.18	0.95	3.14	0.15
2003/04	12.42	9.68	2.61	7.07	2.19	3.12	0.94	3.02	0.28
2004/05	12.85	9.73	2.31	7.42	1.82	3.25	1.09	3.08	0.32
2005/06	13.12	10.14	2.51	7.63	1.95	3.27	1.31	3.05	0.36
2006/07	12.78	9.86	2.38	7.48	1.85	2.86	1.17	3.44	0.33
2007/08	11.97	9.51	2.31	7.20	1.72	2.54	1.08	3.58	0.36

Source: Economic Survey, 2009

From the table, we can find out that the contribution of total revenue on GDP is in increasing trend up to FY 2005/06. In FY 2000/01 it is 11.29% which is gradually increased and reached to 13.12% in FY 2005/06. But after that, it is decreased to

12.78% and 11.97% in FY 2005/06 and 2007/08 respectively. The contribution of total tax revenue on GDP is fluctuating in past 8 years. It is 8.71% in FY 2000/01, and increased to 10.14% in FY 2005/06. In FY 2006/07 its share to GDP is decreased to 9.86% and it further decreased to 9.51% in FY 2007/08. There is significant role of indirect tax in the tax structure of Nepal, which has contributed about three times more than direct tax. In FY 2000/01, the contribution of indirect tax and direct tax 6.43% and 2.23% respectively, this is increased to 7.20% and 2.31% in FY 2007/08. The contribution of income tax on GDP is also increasing gradually in the beginning years. Its contribution is 1.87% in FY 2000/01 which is increased to 2.31% in FY 2002/03 at maximum level during the period of 8 years. Then after, it is decrease to 2.19% in FY 2003/04 and further decreased to 1.82% in FY 2004/05 but it seems same improvement in FY 2003/04 by increasing up to 1.95%. In FY 2007/08 the share of income tax to GDP is only 1.72%. The contribution of land revenue and Registration tax is 0.30% in FY 2000/01. And it is slightly increased to 0.36% in FY 2007/08 within the direct tax, the contribution from income tax on GDP is higher than other tax.

The custom duty, which is composed of import and export duty, has contributed the largest part in GDP within the indirect tax. It has contributed 2.88% on GDP in FY 2000/01. After that, it is gradually increased and covered the share of 3.27% in FY 2005/06. But it is again decreased to 2.86% and 2.54% in FY 2006/07 and 2007/08 respectively. The contribution of VAT in GDP is increased to 3.58% in 2007/08 as compared with 2.66% in FY 2000/01. The contribution of VAT to GDP is maximum in FY 2007/08. The contribution of excise duty is maximum i.e. 1.17% in FY 2006/07. But it is decreased to 1.08% in FY 2007/08. The government has target to increase the VAT at 4% of GDP. But it will not be fulfilled unless the VAT is implemented properly. For that government should stimulate the consumer's awareness program for taking bills and control the practice of evading VAT.

4.1.7 Contribution of Income Tax in Nepal

Nepal has late started the practice of income tax. The idea of introducing income tax in Nepal was originated along with the first budget in 1951. Finally, in 1959, Business profit and Remuneration Tax Act 1960 was introduced. At that time income tax was

levied only on business profits and salaries. After about three year of experiencing income tax, the government replaced the prevailing tax by Income Tax Act, 1962. In 1974, Income Tax Act, 1974 (2031) was enacted, However, this act is replaced by Income Tax Act, 2002 (2058). The Contribution of income tax on various revenues is given in the following table.

Table No. 4.7
Contributions of Income Tax to GDP, Total Revenue,
Total Tax Revenue and Direct Tax Revenue

Rs. in

million

Fiscal Year	GDP	Total Revenue	Total Tax Revenue	Direct Tax Revenue	Income Tax	% of IT on GDP	% of IT on TTR	% of IT on TR	% of IT on Direct tax
2000/01	330018	37251	28752.90	7516.10	6170.2	1.87	21.46	16.56	82.09
2001/02	366251	42893.70	33152.10	8951.5	7420.6	2.02	22.38	17.30	82.89
2002/03	394052	48893.90	38865.10	10159.4	9114	2.31	23.45	18.64	89.71
2003/04	406138	50445.60	39330.60	10597.5	8903.7	2.19	22.64	17.65	84.02
2004/05	437546	56229.70	42587	10105.8	7966.2	1.82	18.70	14.17	78.83
2005/06	474919	62331	48173	11912.6	9245.9	1.95	19.19	14.83	77.61
2006/07	548485	70122.70	54104.70	13071.8	10159.4	1.85	18.77	14.49	77.72
2007/08	603673	72282.10	57430.40	13968.10	10373.7	1.72	18.06	14.35	74.27

Source: Economic Survey, 2009

Table reflects that the income tax is increased in 2007/08 as compared with 2000/01. Total income Tax is Rs. 6170.2 million for the FY 2000/01 and it is increased to Rs. 10373.7 million for the FY 2007/08. The share of income tax on GDP of Nepal is very low. It lied between 1.87% to 1.72% during the study period. It is 1.87% in FY 2000/01 and decreased to 1.72% in FY 2007/08. In FY 2002/03 the share of income tax on GDP is maximum i.e. 2.31%.

The share of income tax to total tax revenue is fluctuated from 21.46% to 18.06%. It is 21.46% in FY 2000/01, increased to 23.45 in FY 2002/03. Thereafter, it is decreased to 18.77 in FY 2006/07 and further decreased to 18.06 in FY 2007/08. Similarly, contribution of income tax to total revenue is 16.56% in FY 2000/01. And it is decreased to 14.35% in FY 2007/08. Its contribution is highest in FY 2002/03 which is 18.64% of total revenue. The contribution of income tax on direct tax is maximum; it is 82.09% in FY 2000/01. It reached to the maximum contribution of 89.71% in FY 2002/03. But its contribution is sharply decreased to 74.27% in FY 2007/08. Such decreasing trend of contribution of income tax to direct tax structure is not fruitful for the tax structure of developing country like Nepal.

4.1.8 Structure of Income Tax in Nepal

Income tax revenue is divided into corporate tax, individual income tax and remuneration tax until 1993/94. After that, the income tax revenue is divided into four group i.e. corporate income tax, individual income tax, house and land rent tax and interest tax. Corporate tax is collected from government, public and private limited companies and partnership firms, and individual income tax is collected from remuneration and industry, business profession or vocation, Interest tax is paid from banks and financial institution that pay interest for all types of deposits and the house rent tax is levied on income obtained from renting house and land in urban areas. The structural composition of income tax is presented below.

Table No. 4.8
Composition of Income Tax

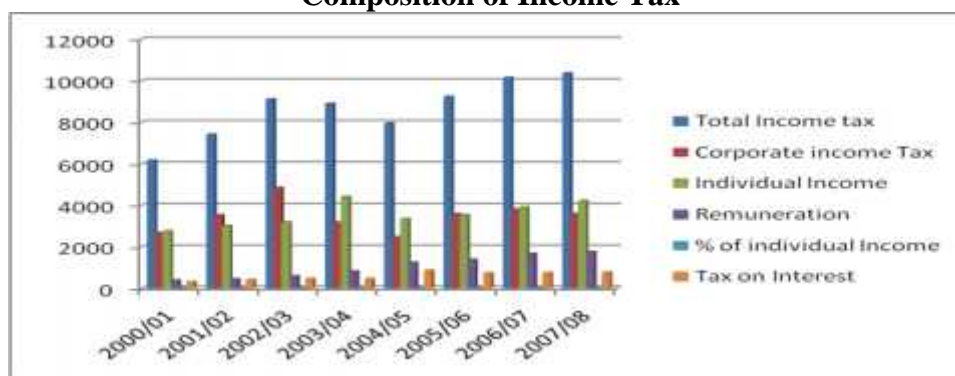
Rs. in

million

Fiscal Year	Total Income tax	Corporate income Tax	% of Corporate tax	Individual Income	% of individual Income	Remuneration	% of Remuneration	Tax on Interest	% of tax on interest
2000/01	6170.2	2681.5	43.46	2772.7	44.94	396.5	6.45	319.5	5.18
2001/02	7420.6	3538.3	47.68	3016.4	40.65	451.5	6.08	414.4	5.58
2002/03	9114	4852.3	53.24	3200.5	35.17	597.3	6.55	463.9	5.09
2003/04	8903.7	3181.3	35.73	4419.1	49.63	835.6	9.38	467.7	5.25
2004/05	7966.2	2487.3	31.22	3362.3	42.2	1252.6	15.72	864	10.84
2005/06	9245.9	3587.9	38.80	3533.4	38.22	1391.2	15.05	733.4	7.93
2006/07	10159.4	3800.2	37.4	3926.3	38.65	1675.9	16.49	757	7.45
2007/08	10373.7	3600	34.7	4234.7	40.82	1764.1	17	774.9	7.47

Source: Economic Survey, 2009

Figure No. 4.3
Composition of Income Tax



The table shows that the share of corporate income tax was 43.46% in FY 2000/01, which was increased to 47.68% in FY 2001/02. And it gradually increased to 53.24% in FY 2002/03. But it sharply decreased to 35.73% in FY 2003/04. Among these ups and downs the share of corporate income tax is decreased to 34.7% in FY 2007/08. Tax collection from corporate sector is found to be highly fluctuated during the study period, which is the red signal for the corporate sector.

Contribution of individual income seem to be gradually increasing from Rs. 2772.7 million to Rs. 3016.4 million in FY 2000/01 and 2007/08 respectively, but in percentage the figure is in diminishing trend i.e. 44.94% and 40.82% in FY 2000/01 and 2007/08 respectively. Individual income tax collection is highest in FY 2003/04 which is 49.63% of total income tax amounting to Rs. 4419.10 million.

Contribution from Remuneration and tax an interest is Rs. 396.5 million and Rs. 319.5 million which is 6.45% and 5.18% of total income tax respectively in FY 2000/01. The share of remuneration is continuously increasing during the study period. Its share is 6.45% in 2000/01 and reached to 17% in FY 2007/08 amounting Rs. 1764% million. Tax an interest is also in increasing trend during the first five years. It is Rs. 864 million in FY 2004/05, but decreased to Rs. 733.4, 757 and 774.9 million in FY 2005/06, 2006/07 and 2007/08 respectively.

4.2 Problem of Resource Gap in Nepal

The resource mobilization is the main challenge in the economic development of the country. The internal resource plays vital role in economic development of the country. Government collects the resources from different ways. The tax structure is major source of revenue for the government. Government has imposed two types of tax like direct and indirect tax. In the present tax structure, the government collects higher revenue from indirect taxes rather than direct tax. Tax policy has to be made a part of the instrument of the development goals.

The resource mobilization has been a major problem in financing of growing government expenditure. Since the beginning of planned development of Nepal, there has been tremendous increment in the size of government expenditure. The development works have to be carried out by the government in the initial stage. An increase in government expenditure creates additional demand in the economy through multiplier effects and thereby induces rise in aggregate output. The government resources have been concentrated more on expanding economic overhead in the form of transport, power and communication which will stimulate agriculture, industry and transport in the private sectors.

The government expenditure is the main source of gross national investment and capital formation. Many studies have been attempted to examine the problem of resource gap and prospect of internal resource gap. Domestic resource gap is the amount of excluding net foreign grants and loans. But the overall resources gap includes the contributions made by foreign grants and loans in financing public expenditure.

The problem of resource gap has increased from one year to another which has been recovered through massive inflow of external capital. Regular expenditure is fulfilled by internal resources whereas development expenditure is mostly depending on external resources. The dependence on foreign aid and deficit finance has not shown any declining trend. If the resource gap is minimized through the over dependence on foreign loans, it can further create the resource problem in the near future.

The problem of resource mobilization and resource gap is related to the saving and investment. The level of income and the rate of interest influence the saving structure. The low rate of saving is prevailing in the country as a result of low level of income of the people. The low level of income creates the problem of resource mobilization for undertaking investment programmes on a large scale by both government and private sector.

Table No. 4.9
Domestic Resource Gap Pattern in Nepal

Rs. in

million

Fiscal Year	Total Govt. Expenditure (A)	Total Govt. Revenue (B)	Resource Gap (A-B)	Resource gap as % of Total Expenditure
2000/01	59579	37251	22328	37
2001/02	66272.5	42893.8	23378.7	35
2002/03	79835.1	48893.6	30941.5	38
2003/04	80072.2	50445.5	29626.7	37
2004/05	84006.1	56229.8	27776.3	33
2005/06	89442.6	62331	27111.6	30
2006/07	102560.4	70122.7	32437.7	31
2007/08	110889.2	72282.1	38607.1	35

Source: Economic Survey, 2009

From the above table, we can see that the Resource Gap is increasing every year. It was Rs. 22328 million in FY 2000/01 and reached to Rs. 38067.10 million in FY 2007/08. This amount of resource gap is decreased in year 2003/04, 2004/05 and 2005/06 respectively. But it sharply increased from Rs. 27111.6 million to Rs. 32437.7 million in FY 2006/07. Percentage of resource of gap on total expenditure is maximum i.e. 38% in FY 2002/03 amounting to Rs. 30941.50 million. Total Government revenue and expenditure is increasing every year. But the rate of increase in expenditure is higher than increasing revenue which leads to the rising resource gap.

Figure No.4.4 (A)
Bar Diagram Showing resource Gap

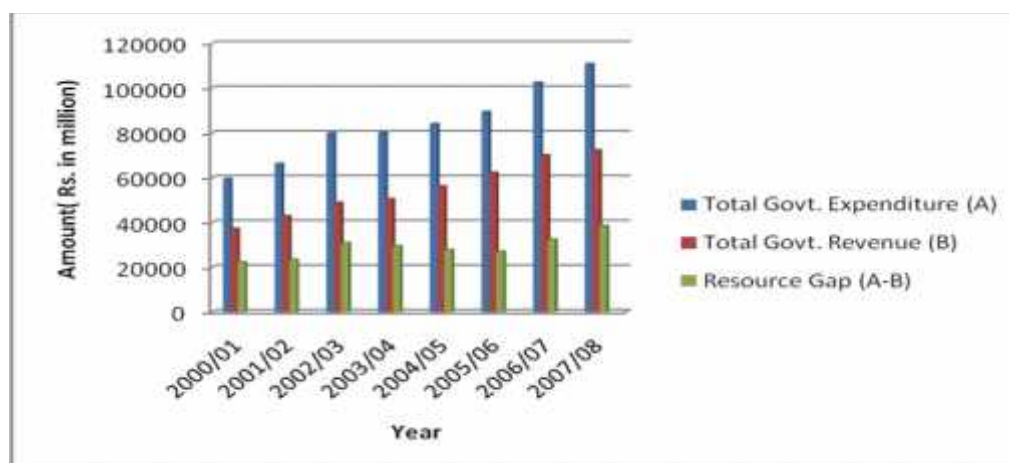
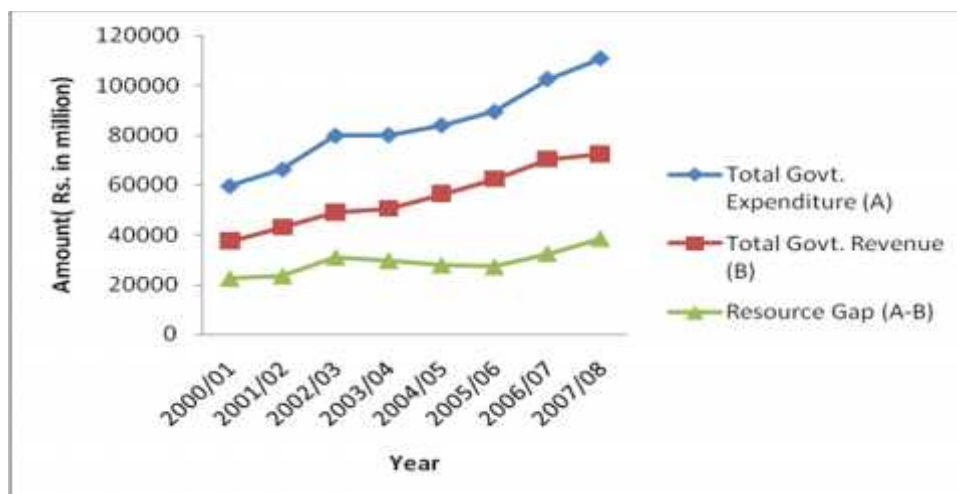


Figure No.4.4 (B)
Trend Line Showing resource Gap



4.2.1 Revenue Expenditure

Revenue expenditure gap is known as resource gap. In this context, three types of gaps are measured and used in the analysis of resource gap.

Table No. 4.10
Overall Resource Gap pattern of Nepal

Fiscal Year	Total Govt. Expenditure (A)	Total Govt. Revenue (B)	Resource Gap (A-B)	Foreign Grants (C)	Rs. in million		
					Resource Gap 2 A-(B+C)	Foreign Loan (D)	Resource Gap 3 A-(B+C+D)
2000/01	59579	37251	22328	4336.6	17991.4	11852.4	6139
2001/02	66272.5	42893.8	23378.7	5711.7	17667	11812.2	5854.8
2002/03	79835.1	48893.6	30941.5	6753.4	24188.1	12044	12144.10
2003/04	80072.2	50445.5	29626.7	6686.1	22940.6	7698.7	15241.9
2004/05	84006.1	56229.8	27776.3	11339.1	16437.2	4546.4	11890.8
2005/06	89442.6	62331	27111.6	11283.4	15828.2	7629	8199.2
2006/07	102560.4	70122.7	32437.7	14391.2	18046.5	9266.1	8780.4
2007/08	110889.2	72282.1	38607.1	13827.5	24779.6	8214.3	16565.3

Source: Economic Survey, 2009

) Resource Gap¹ (A-B)

The gap between government revenue and expenditure has risen from Rs. 22328 million to Rs. 38607.10 million in FY 2000/01 and 2007/08 respectively. This figure shows the poor performance of domestic resource mobilization.

) Resource Gap² A – (B + C)

This type of resource gap is Rs. 17991.4 million in FY 2000/01, which is gradually increased to Rs. 24188.10 million in FY 2002/03. And decreased to 22940.60 million in FY 2003/04. It further decreased to Rs. 16737.2 million and 15828.2 million in FY, 2004/05 and 2005/06 respectively. However, this figure is Rs. 24779.6 million in FY 2006/07. The above data suggests that foreign grants should be encouraged to minimize the resource gap.

) Resource Gap³ A – (B + C + D)

This resource gap is taken as the difference between total expenditure and total revenue plus foreign grants plus foreign loan. In FY 2000/01 the gap was Rs. 6139 million which was increased to Rs. 12144.10 million and 15241.90 million in FY, 2002/03 and 2003/04 respectively. And it was started to decrease gradually. It was Rs. 8199.2 million and 8780.4 million in FY 2005/06 and 2006/07 respectively. Then it was rapidly increased and reached to Rs. 16565.3 million in FY 2007/08 which is nearly two times higher than previous year. It measures the internal indebtedness of the government. The above data reflects the decreasing resource gap when foreign loan is increased and vice versa. As the loan taken amount will decrease simultaneously, the resource gap will increase consequently. Moreover, foreign loan largely depends on the fiscal policy adopted by the nation.

Fiscal deficit (resource gap) is continuously increasing due to lack of proper income management to meet the increasing trend of government expenditure (Economic Survey). Thus this increasing resource gap indicates that it is necessary to mobilize

additional domestic resources. Ultimate and best measure to fill up the resource gap is to increase public revenue through effective tax system.

If any government has a resource gap, it has to resort a deficit budget. There was a large portion of foreign grants to meet the budget deficit in the early year's budgets in Nepal. But in recent years, the percentage of foreign loans is rising and percentage of grants is decreasing. It is not a desirable direction for our economy. Moreover, foreign loan creates extra burden to the economy because debt servicing charge increases every year. The foreign loan should be taken as a complementary resource to mobilize internal resource properly.

4.2.2 Problems in Public Expenditure

Government expenditure is increasing along with its expanding activities in development and social activities. The increasing trend of government expenditure can be fulfilled either by internal resources or through inflow of foreign aid. The increasing rate of growth in government expenditure creates many problems in public expenditure management. As a result, deficit financing takes place in the economy. On the one hand, the resource gap problem is increasing and on the other hand it has grown the inflation and price unstabilization in the economy. There is two way relationships between resource mobilization and expansion in budgetary size in developing country. Government policy should be reformed for maximum resource mobilization in accordance with the expansion in economy that has taken place through the investment of public sector in development activities.

Development expenditure is mostly prepared in accordance with commitment of the donor agencies. But the disbursement of foreign aid has not been as per the commitment. The lack of funding compels to delay the completion of the projects. In the same way, the donor agencies are too much involved in the decision making which creates many problems in implementation and for the completed project by the funding agencies the problem stands to the government on the operation and maintenance of the project.

Table No. 4.11

Share of Government Revenue, Foreign Aid and CITER in Public Expenditure
Rs. in
million

Fiscal Year	Total Govt. Expenditure	Total Govt. Revenue	TR as % of TE	Foreign Aid	Foreign Aid as % of TE	CITER	CITER as % of TE
2000/01	59579	37251	62.52	16189	27.17	2681.5	4.5
2001/02	66272.5	42893.8	64.72	17523.9	26.44	3538.3	5.34
2002/03	79835.1	48893.6	61.24	18797.4	23.54	4852.3	6.08
2003/04	80072.2	50445.5	63	14384.8	17.96	3181.3	3.97
2004/05	84006.1	56229.8	66.93	15885.5	18.91	2487.3	2.96
2005/06	89442.6	62331	69.69	18912.4	21.14	3587.9	4.01
2006/07	102560.4	70122.7	68.37	23657.3	23.07	3800.2	3.70
2007/08	110889.2	72282.1	65.18	22041.8	19.88	3600	3.25

Source: Economic Survey, 2009

The above table shows the total government expenditure, government revenue, foreign aid and CITER. The contribution of government revenue is only 62.52% of government expenditure in FY 2000/01. This share has increased to 64.72% in FY 2001/02 amounting to Rs. 42893.8 million. And it decreased to 61.24% in FY 2002/03. The share of government revenue is maximum in FY 2005/06 contributing 69.69% of government expenditure. This share is only 65.18% in FY 2007/08.

The share of CITER is 4.5% in FY 2000/01. This share is maximum in FY 2002/03 which represents 6.08% of total government expenditure. This share is 4.5% in FY 2000/01. The share of CITER is only 2.96% in FY 2004/05. However it is increased to 4.01% in FY 2005/06. And decreased to 3.25% in FY 2007/08 amounting to Rs. 3600 million.

Similarly, the contribution made by foreign aid comprising both foreign grants and loans is 27.17% in FY 2000/01 amounting Rs. 16189 million. After this year, its share is on decreasing trend. Its contribution is minimum in FY 2002/03 i.e. 17.96 amounting Rs. 14384.8 million. In FY 2006/07 it has contributed 19.88% of government expenditure amounting to Rs. 22041.8 million.

Conclusion from the above analysis is that government dissaving is increasing every year. Government's expenditure is increasing at a higher rate than the growth of government revenue. The growth rate of domestic saving has not increased

substantially even the external capital inflow has been increasing with higher rate. As a consequence of which the resource gap is highly increasing instead of diminishing. In this context, the certain percentage increase in the share of CITR will play a significant role to fulfill resource gap from the internal sources. So, more emphasis should be given on raising revenue through corporate sectors.

4.3 Corporate Tax Structure

This deals with the corporate tax rate and tax base. It has divided into two sections. The first section presents the structure of corporate income tax while the second reveals the present corporate tax base followed by the corporate sector.

4.3.1 Corporate Tax Rate Structure in Nepal

Tax rate is the base of measurement of tax liability. Tax should not be so high only for minimum revenue realization but should be an activator for private investment. Developing countries like Nepal need to boost up their economic conditions by developing industries and trade within the country. For this, the corporate tax rate also plays a crucial role. Imposition of tax on corporate profit was started with the enactment of the Business Profit and Remuneration Tax Act, 1960. The starting corporate tax rate was 25% and it was levied on a progressive way. The tax amount was calculated on different slabs before FY 1985/86. The corporate tax rate structure was combined with individual tax rate structure. The reason was the numbers of companies were limited and private companies were generally managed by family. In the year 1985/86 the progressive tax rate structure was abolished in the case of government enterprise and used to split into different units to take advantage of lower rates. The progressive rate of tax to private companies was abolished in the fiscal year 1995/96. This flat rate system has been continued for all corporate bodies since the FY 1995/96.

The corporate tax rate structure was increased up to 60% the maximum rate in the FY 1995/96 from 25%. During 1960/61 to 1975/76, the tax rate again decreased up to 51% and 50%. This rate was again increased to 55% and remains continued from FY 1982/83 till 1987/88. In the year 1987/88, the listed public limited companies

were levied 10% less than others. This concession was given to such companies by only 5% in the year 1985/86. After the FY 1987/88, the tax rate was continuously decreasing. Now it is 20% to industry (except cigarette and alcohol), 25% to general companies and 30% to banks and finance companies. Special fee of 3% of taxable income was levied to all corporate bodies. The corporate tax rate structure of different years is presented as below:

Table No. 4.12
Corporate Tax Rate Structure in Nepal

Fiscal Year	Maximum Marginal Tax Rate		Nature of tax rate Progressive
	Private Co.	Public Co.	
1960/61-1962/63	25	25	"
1963/64-1964/65	30	30	"
1965/66-1966/67	40	40	"
1967/68	55	55	"
1968/69-1974/75	55	55	"
1975/76	60	60	"
1976/77-1978/79	51	51	"
1979/80	50	50	"
1980/81-1981/82	50	50	"
1982/83	55	55	"
1983/84-1984/85	55	55	"
1985/86	55p	55f	Progressive(P) & Flat(F)
1986/87-1987/88	55p	50f	"
1988/89-1989/90	50p	50f	"
1990/91-1991/92	40p	40f	"
1992/93-1994/95	35p	35f	"
1995/96	33	33	Flat
1996/97	30	33	"
1997/98-2006/07	20,25 & 30	20,25 & 30	"

Source:

1. Kandel, P. R. (2000), Corporate Tax System & Investment Behavior in Nepal
2. Budget Speech, 2005/06 & 2006/07
3. Finance Acts

Notes:

- 20% tax rate for special industries.
- 25% tax rate for general industries producing cigarette, bidi, liquor and industries uses as raw material.
- 30% tax rate for non industries for banking and insurance business.

4.3.2 Corporate Tax Base in Nepal

Under the Income Tax Act, 2058 of Nepal, corporate tax is levied on the total taxable income of the previous year. It has assumed the global or total as well as scheduler income tax. This act has divided the source of income into three major heads they are: income from business, income from investment and income from employment. The third amendment of Income Tax Act, 2058 has further clarified about calculating the adjusted taxable income and net taxable income from business, investment and employment. All the taxable income are added as per law and deduction allowable expenses such as general deduction, cost of trading stock, interest expenses, repair and maintenance expenses, depreciation, reserve and rise-bearing fund and expenses related with business and investment were deducted as per the law, which occurs adjusted taxable income. Then, incase of business income, pollution control and R & D expenses should be deducted taking the adjusted taxable income as base, after that we get assessable income from business before loss adjustment. Then, loss from business in current year and previous year are deducted to get the net assessable income from business. Likewise, loss in business and investment of current year and business loss of previous year are deducted to get the net assessable income from investment.

Total assessable income is calculated by adding the net income from business and investment from where common expenses and donation expenses can be deducted as per law to get total taxable income. No exemption Limit is provided to the companies. Special additional fee of 15% of taxable income is charged to the second slab where 25% tax rate is charged.

4.3.3 Contribution of Corporate Income Tax

Contribution of corporate income tax on Income Tax revenue, total government revenue, its composition and trend line for 8 years has been drawn in this sub-chapter. The relationship of CITR with other taxes and total revenue and its coverage portion has been examined.

4.3.3.1 Structural composition of corporate Income Tax

The corporate income tax structure comprises of government sector, public and private sector. Corporate taxable income is calculated by adding all the taxable income and deducting all the allowable expenses. After the enactment of Income Tax Act 2058, the books of account of corporate sector have been kept a little bit differently. From the FY 2003/04, the total corporate sector income tax is computed by adding public and private sector including individual and sole trading concern. The, following table has been drawn to show the structural composition of corporate income tax from the FY 2000/01 to 2007/08.

Table No. 4.13
Structural Composition of Corporate Income Tax

**Rs. in
million**

Fiscal Year	CITR	Public Sector	% share of CITR	Private Sector	% share of CITR
2000/01	2681.5	1526.5	56.93	1155	43.07
2001/02	3538.3	2198.8	62.14	1339.5	37.86
2002/03	4852.3	2928	60.34	1924.3	39.66
2003/04	3181.3	1769.3	55.61	1412	44.39
2004/05	2487.3	1251	50.30	1236.3	49.70
2005/06	3587.9	2056.6	57.32	1531.3	42.68
2006/07	3800.2	1332.4	35.06	2467.8	64.94
2007/08	3600	195.7	5.43	3404.3	94.57

Source: Economic Survey, 2009

The above structural composition of corporate tax shows that major portion is covered by public sector in the beginning. It is 56.93% in FY 2000/01 while the private sector contributed only 43.07%. The share of public sector increased to 62.14% in FY 2001/02 where as the private sector contribution is decreased to 37.86%. From the FY 2002/03, the share of public sector is gradually decreasing and the share of private sector is increasing. In FY 2004/04 the public sector contribution is 50.30% where as the share of private sector is 49.70%. There is a huge decrease in share of public sector is FY 2007/08 in comparison to FY 2006/07. Its share is decreased from 35.06% to 5.43% in FY 2007/08. On the other side, the share of private sector is highly increased in FY 2007/08 in comparison to previous fiscal year. It has increased to 94.57% in FY 2007/08 from 64.94% in FY 2006/07. The above figure shows the growth and

diversification of private sectors in the country. The structural composition of CITR can be presented in bar graph and chart as follows:

Figure No.4.5 (A)
Bar Graph Showing CITR and its Composition

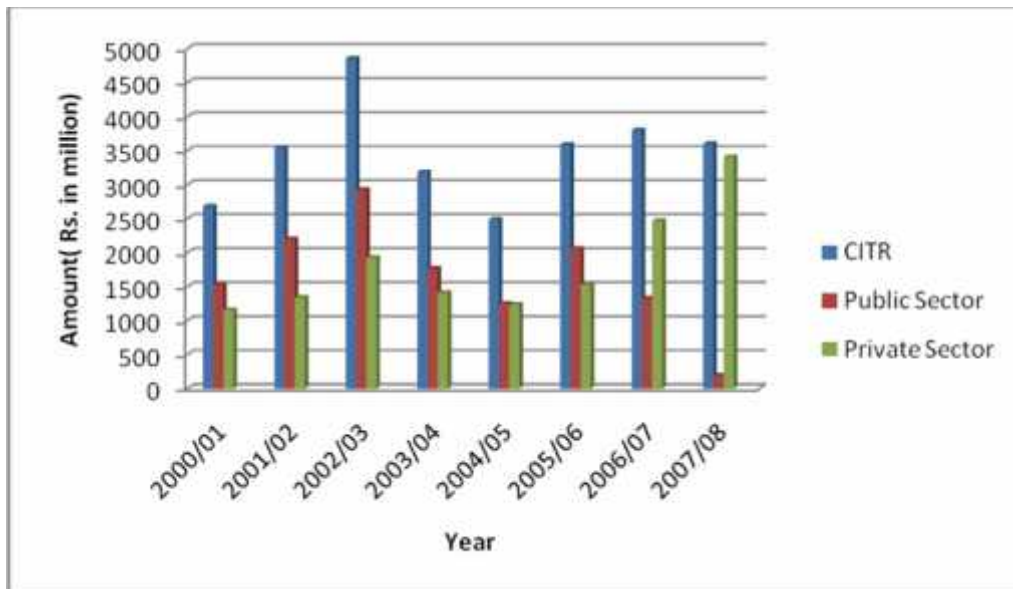
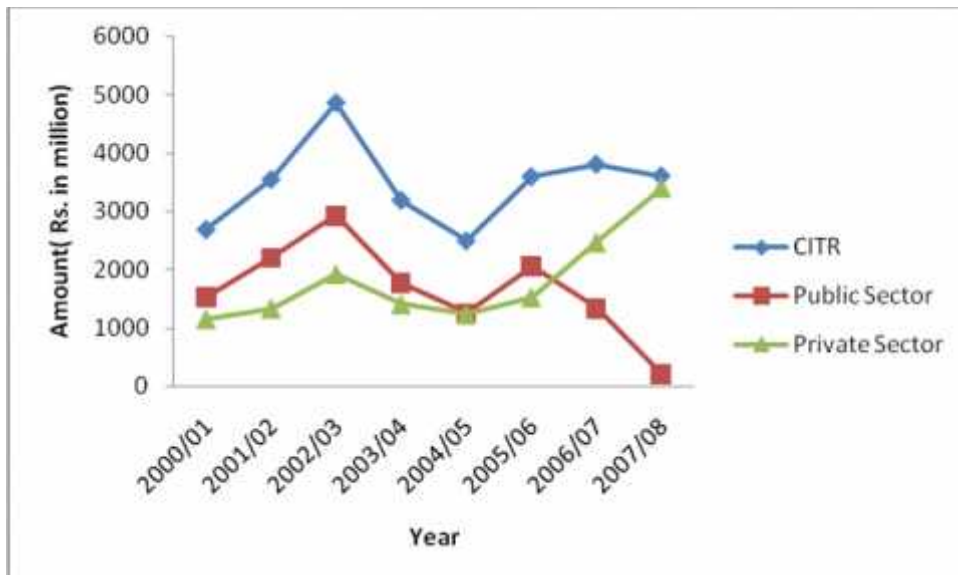


Figure No. 4.5 (B)
Trend Line Showing CITR and its Composition



4.3.3.2 Contribution of Corporate Income Tax Revenue on Income Tax Revenue

Income tax revenue comprises of corporate income tax, individual income tax, remuneration tax and interest tax. The size of income tax revenue largely depends upon the size of corporate sector. Greater the size of corporate sector, higher will be the CITR and total tax revenue and vice versa. So CITR in Nepal has played a crucial role in income tax revenue which has been presented in the following table:

Table No. 4.14
Contribution of CITR on Income Tax Revenue

**Rs. in
million**

Fiscal Year	Income Tax	Corporate Income Tax				Total CITR	%
		Public Sector	%	Private Sector	%		
2000/01	6170.2	1526.5	24.73	1155	18.72	2681.5	43.45
2001/02	7420.6	2198.8	29.63	1339.5	18.05	3538.3	47.68
2002/03	9114	2928	32.13	1924.3	20.11	4852.3	53.24
2003/04	8903.7	1769.3	19.87	1412	15.86	3181.3	35.73
2004/05	7966.2	1251	15.70	1236.3	15.52	2487.9	31.22
2005/06	9245.9	2056.6	22.24	1531.3	15.56	3587.9	37.40
2006/07	10159.4	1332.4	13.11	2467.8	24.29	3800.2	37.40
2007/08	10373.7	195.7	1.88	3404.3	32.81	3600	34.69

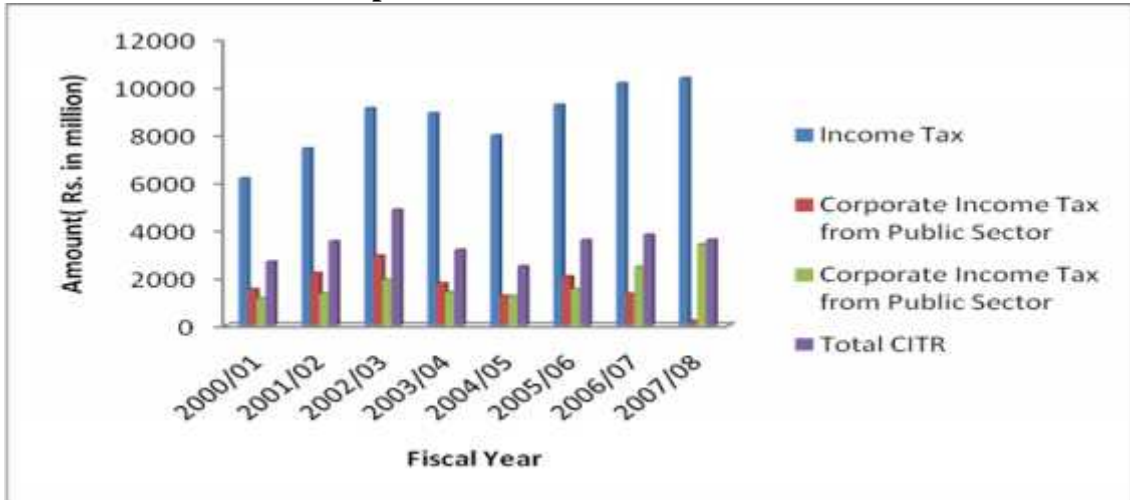
Source: Economic Survey, 2009

Above table reflects that the contribution of CITR to income tax seems to be in decreasing trend during the study period. It is 43.45% amounting Rs. 2681.5 million in The FY 2000/01, which is increased to 47.68% amounting Rs. 3538.3 million. In FY 2002/03 it is increased to 53.24% amounting 4852.3 million. But its contribution is started to decrease and reached to 31.22% in FY 2004/05 amounting Rs. 2487.30 million. After that it is increased to 37.80% and decreased to 37.40% in FY 2005/06 and 2006/07 amounting Rs. 3587.9 million and 3800.2 million respectively. In FY 2007/08 the contribution of CITR is only 34.69% amounting Rs. 3600 million.

The Structural composition of corporate sector seemed to be changed during the study period. In FY 2000/01, 24.73% and 18.72% contribution is made by public and private sectors. This figure is 15.70% and 15.52% respectively in FY 2004/05. And this figure is changed to 1.88% and 32.81% in FY 2007/08. The above figure clarifies that the contribution of public sector is decreasing and private sector is in increasing trend.

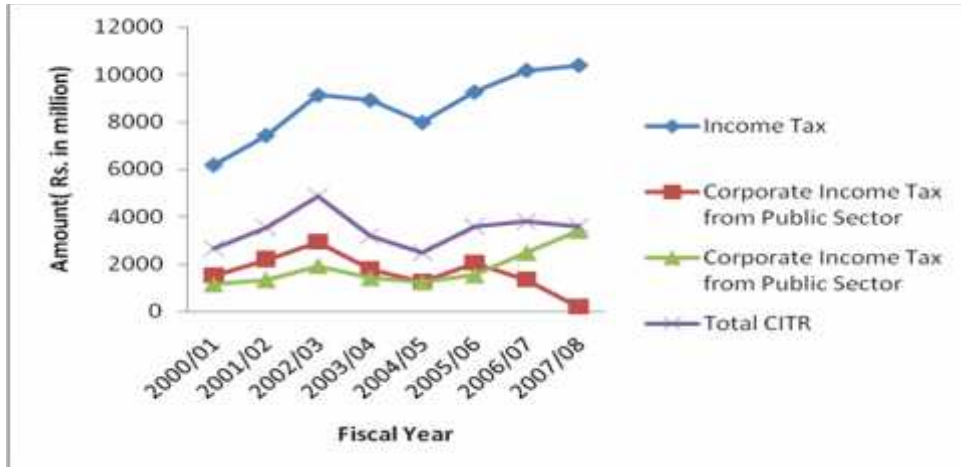
The CITR and income tax revenue position has been shown in the following bar diagram and chart:

Figure No.4.6 (A)
Bar Graph of CITR and Income Tax Revenue



In the above bar diagram, different years are shown in x-axis and total Income Tax Revenue is shown in Y-axis. In which we can see the maximum contribution of CITR to income tax revenue in FY 2003/04.

Figure No.4.6 (B)
Trend Line of CITR and Income Tax Revenue



The above trend line shows that income tax revenue is increasing regularly up to FY 2002/03 and it started to decrease regularly for two years. And again it is continuously increasing up to FY 2007/08. Total CITR is maximum in FY 2002/03 and it is in decreasing trend except FY 2005/06.

4.3.3.3 Contribution of Corporate Income Tax on Total Revenue

Corporate income tax plays an important role in Nepalese government revenue. The composition of national revenue/government revenue has been shown in master table in appendix and the composition of corporate tax revenue as well. As per the master table, the following table has been drawn to show the contribution portion of CITR in different time periods in percentage and amounts also.

Table No. 4.15
Contribution of Corporate Income Tax on Total Revenue

Rs. in million

Fiscal Year	Total revenue	Corporate Income Tax				Total CITR	%
		Public Sector	%	Private Sector	%		
2000/01	37251	1526.5	4.10	1155	3.10	2681.5	7.20
2001/02	42893.7	2198.8	5.13	1339.5	3.12	3538.3	8.25
2002/03	48893.9	2928	5.98	1924.3	3.93	4852.3	9.91
2003/04	50445.6	1769.3	3.51	1412	2.80	3181.3	6.31
2004/05	56229.9	1251	2.22	1236.3	2.20	2487.3	4.42
2005/06	62331	2056.6	3.30	1531.3	2.46	3587.9	5.76
2006/07	70122.7	1332.4	1.90	2467.8	3.52	3800.2	5.42
2007/08	72282.1	195.7	0.27	3404.3	4.71	3600	4.98

Source: Economic Survey, 2009

Above table reflects the contribution percentage of corporate income tax to total government revenue during the study period is fluctuating from 4% to 7%. The share of corporate income tax revenue is 7.2% amounting Rs. 2681.5 million in the FY 2000/01, in which 4.10% is covered by public sector and rest by private sector. Later on, the share of CITR to total revenue has slowly increased up to 9.91% of maximum in FY 2002/03 amounting Rs. 4852.3 million. Where intra-structural composition of corporate sector is dominated by government sector contributing 5.98% of maximum percentage of amounting Rs. 2928 million during the study period. But these situations continue no longer. Political instability, unfriendly economic environment for smooth operation of business is some of the main reason for Nepalese corporate sector unable in improving its competency. As a result, contribution of CITR on total revenue is sharply decreased from 9.91% amounting Rs. 4852.3 million in 2002/03 to 5.42% in 2006/07 amounting Rs. 3800.2 million which is 4.98% amounting Rs. 3600 million in FY 2007/08.

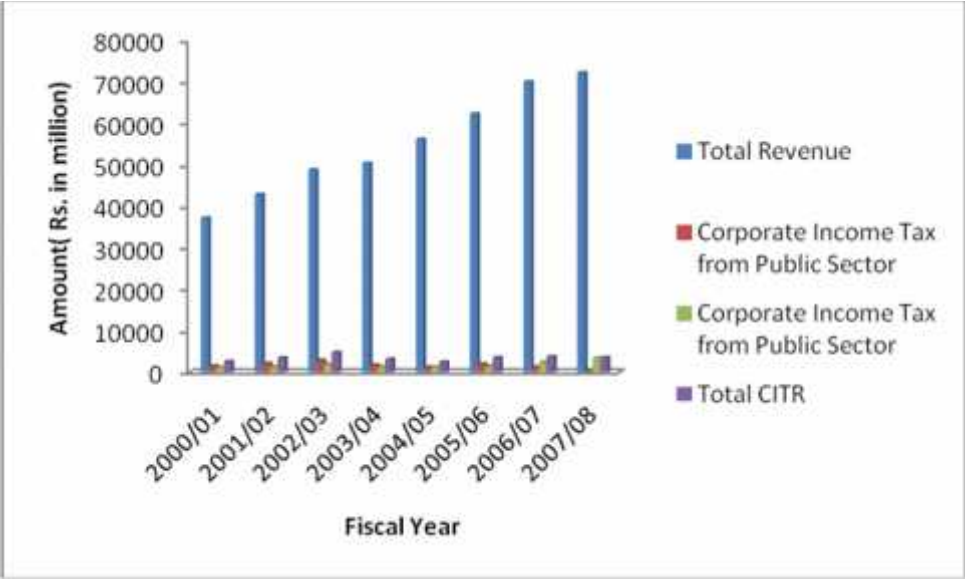
Total revenue is also in increasing trend which is not only the cause of better implementation of fiscal policy and positive macro-economic indicator but it was also

due to the expansion of taxation and revenue net. This table also shows that the private sector's tax collection is fluctuating but it is around 2% to 4% since last 8 years although Nepal has liberalized the economy and privatized about 24 public enterprises and companies during the last decade. Likewise, tax collection from public enterprises seemed to be increasing up to 2002/03 but later on it was decreased to 0.27% in FY 2007/08. We can find out from the above table that, the contribution from public sector is decreasing gradually and from private sector is in increasing trend.

Nevertheless, Nepalese corporate sector is contributing to total revenue only about 6% on average which seems to be very small portion comparing to other developing countries.

The contribution pattern of corporate income tax to total revenue has been shown in the following bar diagram:

Figure No.4.7
Contribution of Corporate Income Tax on Total Revenue



In this bar diagram, total revenue is shown in Y-axis and fiscal year in X-axis. Comparing with total revenue, corporate income tax revenue seems to be very low. The intra-structural composition of corporate tax seems to be changed. In the beginning, the public sector is covering the major portion but later on the major portion of the corporate income tax is covered by private sectors during the study period.

4.4 Empirical Investigation

An empirical investigation has been conducted in order to find out various aspects of income tax imposition in Nepal. This chapter analyzes information collected from primary sources i.e. through questionnaire. The questionnaire was distributed to the Tax administrators, Tax experts/Auditors and Tax payers. The responses received from various respondents have been arranged, tabulated and analyzed in order to facilitate the descriptive analysis of the study. The respondents were requested to response on questionnaire by four ways.

- They were requested to response simply by yes or no response.
- They could response by selecting one or more options.
- They could response by ranking the choices starting from 1 to 10, starting from most important to least.
- Respondents had also option to put their views by writing wherever necessary.

Table 4.16
Groups of Respondents and Number from Each Group

S.N.	Groups of Respondents	Sample Size	Code Used
1	Income Tax Administrators	25	A
2	Income Tax Experts/Auditors	25	B
3	Income Tax Payers	25	C
	Total	75	

4.4.1 Public Awareness towards Income Tax System in Nepal

In order to know whether the people are well informed about income tax system in Nepal, a question was asked "Do you think people are well informed about the income tax system in Nepal?" The respondent's response was presented in the table 4.17

Table No. 4.17
Information about Income Tax System in Nepal

Respondents	Yes		No		Total	
	No	%	No	%	No	%
A	-	-	25	100	25	100
B	2	8	23	92	25	100
C	1	4	24	96	25	100
Total	3	4	72	96	75	100

Source: Opinion Survey

From the opinion survey, it is found that cent percent Tax Administrators believe that people are not informed about income tax system in Nepal. Only 8% of tax experts/auditors said that people are well informed about income tax system where as 92% claim that people are not properly informed. And 96% of tax payers believe that people are not well informed about income tax system in Nepal. In total, 96% of respondents believe that people are not well informed about income tax system in Nepal.

Above survey approved that public awareness program is necessary in Nepal for making people well informed about income tax system. Awareness should be given through local newspaper and mass media in order to make the people conscious.

4.4.2 Contribution of Income Tax Revenue

To know whether the contribution of income tax revenue is satisfactory or not, a question was asked to respondents "In your opinion is contribution of Income tax to national revenue is satisfactory?" opinion result is presented in the table 4.18.

Table No. 4.18
Contribution of Income Tax Revenue Satisfactory or not

Respondents	Yes		No		Total	
	No	%	No	%	No	%
A	5	20	20	80	25	100
B	8	32	17	68	25	100
C	5	20	20	80	25	100
Total	18	24	57	76	75	100

Source: Opinion Survey

Only 20% tax administrators, 32% tax experts/auditors and 20% tax payers believe that contribution of income tax to national revenue is satisfactory. And rest 80% tax administrator, 68% tax experts and 80% tax payers reacts adversely. In total, 76% of total respondents believe that contribution of income tax to national revenue is not satisfactory.

4.4.2.1 Reasons for Low Revenue Collection from Income Tax

76% of the total respondents believed that contribution of income tax on national revenue is not satisfactory. So in order to find out the major causes of low collection from income tax, the respondents are asked to rank among ten options as per their priority. The ranking result is as follows:

Table 4.19
Main Causes of Low Revenue Collection from Income Tax in Nepal

S.N.	Major Cause	Total Points Received			Total	Percent %	Ranks
		A	B	C			
(i)	Inconsistent tax acts, rules and regulation	81	92	81	254	8.12	2
(ii)	Loopholes in income tax act	122	68	77	267	8.53	3
(iii)	Inefficient tax administration	127	103	103	333	10.64	6
(iv)	Existence of Smuggling	114	132	129	375	11.98	9
(v)	Improper billing system	84	63	133	280	8.59	4
(vi)	Lack of tax education	105	55	44	204	6.52	1
(vii)	Income tax returns not filing on time	140	70	150	360	11.5	7
(viii)	Instable political Condition	108	89	110	307	9.81	5
(ix)	Increasing tendency of tax evasion.	105	136	130	371	11.86	8
(x)	Mass Poverty and low income level	114	119	145	378	12.1	10
Total					3129		

Source: Opinion Survey

In table 4.19 rank 1 is given to the lowest percentage and 10 to the highest. Here, lowest percentage is obtained by the cause, which is treated as the most important cause by the respondents.

From the above table, the major causes of low collection of income tax in Nepal are ranked in order of the preference of the respondents are as follows:

1. Lack of tax education.
2. In consistent tax acts, rules and regulations
3. Loopholes in income tax act.
4. Improper billing system.

5. Instable political condition.
6. Inefficient tax administration.
7. Income tax returns not filing on time.
8. Increasing tendency of tax evasion.
9. Existence of smuggling.
10. Mass poverty and low income level.

From the above table, it can be concluded that, in the opinion of the respondents, the major causes of tax payer wise low calculation of income tax is lack of tax education, Inconsistent tax acts, rules and regulations, loopholes in income tax act etc. So major emphasis should be given on creating public awareness and modifying the difficulties of present income tax act.

4.4.3 Appropriateness of Income Tax Rates

To know the respondents view towards income tax rates, the question was put is present income tax rates in Nepal High? Opinion result is summarized in the table below.

Table No. 4.20
Appropriateness of Income Tax Rates

S.N.	Respondents	Yes		No		Total	
		No	%	No	%	No	%
1	A	2	8	23	92	25	100
2	B	11	44	14	56	25	100
3	C	20	80	5	20	25	100
Total		33	44	42	56	75	100

Source: Opinion Survey

From the above survey, 92% of tax administrators and 56% of Tax Experts/auditors believed that income tax rate is not high in Nepal. They are in favor of present income tax rate. But 80% of the tax payers claimed that present income tax rate is high. It means they are against the present income tax rates. And their recommendation is as follows:

Table No. 4.21
Suggested Income Tax Rates

S.N.	Tax	Respondents Answer	Total	%
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	Rate	A	%	B	%	C	%		
1	20%	2	100	2	18.18	7	35	11	33.33
2	18%	-	-	-	-	-	-	-	-
3	15%	-	-	9	81.81	3	15	12	36.36
4	10%	-	-	-	-	10	50	10	30.36
Total		2	100	11	100	20	100	33	100

Source: Opinion Survey

From the above survey, cent percent tax administrators prefer income tax rate 20%, 18.18% tax experts and 35% tax payers prefer tax rate 20%. Whereas 81.81% tax experts and 15% tax payers prefer tax rate at 15% and 50% tax payers prefer income tax rate at 10%. So it can be concluded that major portion of tax payers found present tax rate high and they recommend the income tax rate at comparatively lower rate.

4.4.4 Weaknesses of Income Tax Act 2058

In order to know the weakness of income tax act, 2058 for the low collection from income tax a question was asked to respondents "Do you believe that the contribution of income tax is not satisfactory because of income tax act 2058"? Opinion result is as follows:

Table No. 4.22
Low Income Tax Collection Because of Income Tax Act 2058

S.N	Respondents	Yes		No		Total	
		No	%	No	%	No	%
1	A	12	48	13	52	25	100
2	B	16	64	9	36	25	100
3	C	12	48	13	52	25	100
Total		40	53.33	35	46.67	75	100

Source: Opinion Survey

As 53.33% of total respondents believed that contribution of income tax is not satisfactory because of income tax act 2058, the major weakness of the act is assumed as follows:

Table No. 4.23
Major Weakness of Income Tax Act, 2058

S.N.	Major Weakness	Respondents						Total	
		A	%	B	%	C	%	No	%
1	Fully based on self-Assessment	5	41.67	3	18.75	0		8	20

2	Amended assessment is not in practice	2	16.67	2	12.5	0		4	10
3	Assessment of income tax is not based on best judgement	1	8.33	6	37.5	5	41.67	12	30
4	Complication due to the merging of tax and VAT administration	3	25	4	25	4	33.33	11	27.5
5	No Harmony between VAT and income tax act	1	8.33	0	0	3	25	4	10
Total		12	100	16	100	12	100	40	100

Source: Opinion Survey

From the above table, 41.67% of tax administrators believed that the major weakness of income tax act, 2058 is that it is fully based on self assessment. And 25% said that complication had arise due to the merging of tax and VAT offices. 37.5% of tax experts/auditors said that income tax assessment is not based on best judgement. And 25% of tax experts agreed with the opinion of tax administrators i.e. Complication due to the merging of tax and VAT administration. 41.67% of tax payers agreed that income tax assessment is not based on best judgement. 33.33% agreed with the opinion of tax administrators and tax experts whereas 25% said that problem arised due to the disharmony between VAT and income Tax Act. It means the common view of all the respondents is that complication arised due to the merging of tax and VAT administration.

4.4.5 Soundness of Income Tax Administration

In order to know the view of respondents towards soundness of income tax administration a question was asked "Do you believe that the income tax administration is not sound after merging of tax and VAT office?" If yes, what is the main reason? And they are requested choose the best option among five. The responses received are tabulated as below:

Table No. 4.24
The Soundness of Income Tax Administration After Merging Tax and VAT office

S.N	Respondents	Yes		No		Total	
		No	%	No	%	No	%
1	A	14	56	11	44	25	100

2	B	11	44	14	56	25	100
3	C	18	72	7	28	25	100
Total		43	57.33	32	42.67	75	100

Source: Opinion Survey

Since 57.33% of the respondents believed that the tax administration is not sound after merging of tax and VAT offices, the reasons for such in the opinion of respondents are as follows:

Table No. 4.25
Reasons for Inefficient Tax Administration

S.N.	Main Reason	Respondents						Total	
		A	%	B	%	C	%	No	%
1	Difficulty in management due to the large numbers of tax payers.	5	37.71	2	18.18	8	44.44	15	34.88
2	Inefficient tax officials	0	0	4	36.36	1	5.55	5	11.63
3	Disharmony between income tax and VAT	3	21.43	3	27.27	0	0	6	13.95
4	Increasing habit of tax evasion after registering in VAT.	6	42.86	2	18.18	9	50	17	39.53
Total		14	100	11	100	18	100	43	100

Source: Opinion Survey

From the above survey, 42.86% of tax administrator believed that income tax administration is not sound after merging tax and VAT office because there is increasing tendency of tax evasion by tax payers once they are registered in VAT. 18.18% tax experts and 50% of the tax payers also accepted the same reason. 36.36% of the tax experts/auditors said that Income tax administration is not sound because of inefficient tax officials. And 27.27% tax experts said that problem is arised due to the disharmony between income tax and VAT. Among the tax payers 44.44% said that income tax administration is not sound after merging tax and VAT office because there are large numbers of tax payers which is difficult to manage. But in total, highest percentage is received by the option 4 i.e. Income Tax administration is not sound because there is increasing habit of tax evasion after tax payers are registered in VAT. Another major reason is difficulty in management due to the large numbers of tax payers.

4.4.6 Situation of Present Income Tax Administration

To know the situation of present income tax administration, the respondents are asked "What do you feel about present income tax administration of Nepal?" Whether it is efficient, inefficient or satisfactory their responses is tabulated as below:

Table No. 4.26
Situation of Present Income Tax Administration

S.N.	Responses	Respondents						Total	%
		A	%	B	%	C	%		
1	Efficient	3	12	0	0	0	0	3	4
2	Inefficient	9	36	10	40	11	44	30	40
3	Satisfactory	13	52	15	60	14	56	42	56
Total		25	100	25	100	25	100	75	100

Source: Opinion Survey

Above table shows that 4% respondents believed that present income administration is efficient, 40% for inefficient, 56% for satisfactory. Since, 40% of the respondents said the present income tax administration is inefficient, they are asked to rank among 8 major causes of such inefficiency. The ranking table is as below:

Table No. 4.26
Major Causes of Inefficient Income Tax Administration

S.N	Major Causes	Respondents			Total Score	Percent	Rank
		A	B	C			
1	Lack of trained and competent tax officials	37	19	26	82	7.61	1
2	Lack of delegation of authority among tax personnel	50	31	43	124	11.51	2
3	Lack of proper direction	40	53	56	149	13.83	6
4	Lack of effective communication	40	62	37	139	12.90	5
5	Unnecessary outside pressure	46	43	79	168	15.60	8
6	Undue delay in making Assessment	45	29	51	125	11.61	3
7	Lack of co-ordination among tax departments	30	52	46	128	11.88	4
8	Complicated tax laws	36	71	55	162	15.04	7
Total					1077	100	

Source: Opinion Survey

The major causes of inefficient tax administration in Nepal were ranked in order of the preference of the respondents are as follows:

1. Lack of trained and competent tax officials.

2. Lack of delegation of authority among tax personnel.
3. Undue delay in making assessment.
4. Lack of coordination among tax related departments.
5. Lack of effective communication.
6. Lack of proper direction.
7. Complicated tax laws.
8. Unnecessary outside pressure.

4.4.7 Problems of Tax Payers

To know the problems facing by the taxpayers while paying income tax, the respondents were requested to choose the most appropriate options among four. The question was "In your opinion, what types of problems are facing by the tax payers while paying income tax"? Responses received from respondents are tabulated as below:

Table No. 4.27
Problem Faced by the Tax Payers while Paying Tax

S.N.	Problem Type	Respondents						Total	%
		A	%	B	%	C	%		
1	Time consuming process	7	28	4	16	11	44	22	29.33
2	Expectation of illegal incentives by tax personnel	2	8	6	24	5	20	13	17.33
3	Vague provisions in income tax laws	12	48	12	48	7	28	31	41.33
4	Lack of cooperation by tax administrators	4	16	3	12	2	8	9	12
Total		25	100	25	100	25	100	75	100

Source: Opinion Survey

From the above survey 41.33% of the total respondents believed that their main problem is vague provisions in income tax laws 29.33% of the respondents found their main problem in time consuming process. It means that the major problem is the vague provisions in income tax laws. People are not fully aware about the procedures to be followed while paying tax. There are so many provisions such as installment payment, installment statement and others. And tax payers are often penalized for making mistakes so people generally hesitate to go to the tax office. Such hesitation of tax payers has further doubled the problem.

4.4.8 Submission of Income Tax Returns

It is found that each year only about 60 percent of the total tax payers submits income tax return to the revenue office. We had asked the respondent that is this main cause of low collection from income tax. Their opinion is as below:

Table No. 4.28
Belief on Few Submission of Income Tax Return, the Main Cause of Decreasing Income tax

S.N	Respondents	Yes		No		Total	
		No	%	No	%	No	%
1	A	14	56	11	44	25	100
2	B	21	84	4	16	25	100
3	C	19	76	6	24	25	100
Total		54	72	21	28	75	100

Source: Opinion Survey

Since 72% of the total respondents believed that few submission of income tax return is the main cause of low collection from income tax, we further asked them for the measures to increase the submission of income tax returns. Their recommended measures among the four options are as below:

Table No. 4.29
Measures to be Followed to Increase the Income Tax Returns

S.N.	Recommended Measures	Respondents						Total	%
		A	%	B	%	C	%	No	%
1	Heavy fines and penalties should be levied.	5	35.71	3	14.28	2	10.53	10	18.52
2	Awareness should be given through news paper and mass media	4	28.57	14	66.67	11	57.89	29	53.70
3	Certain exemption for timely submission of income tax returns	5	35.71	2	9.52	4	21.05	11	20.37
4	Provision of reward	0	0	2	9.52	2	10.53	4	7.40
Total		14	100	21	100	19	100	54	100

Source: Opinion Survey

From the above analysis, 53.7% of the total respondents believed that public awareness should be created through newspaper and mass media in order to increase the timely submission of income tax returns. Presently, we have the problem of information dissemination. When people are timely informed, they will submit their returns which

ultimately will help to increase the income tax collection. Respondents were also in favor of giving certain exemption to those who submits the returns on time.

4.4.9 Loopholes in Income Tax Act, 2058

To know the main loopholes of income tax act, 2058 in the view of the respondents, we had asked them 'what do you think is the main loopholes in income tax act 2058'? We put 6 options and asked to rank them. Table no. 4.30 gives the breakdown of responses.

Table No. 4.30
Main Loopholes in Income Tax Act 2058

S.N.	Main Loopholes	Respondents Score			Total Score	%	Rank
		A	B	C			
1	High rate of depreciation	127	99	109	335	21.23	5
2	Complicated income tax act, rules and regulation	45	45	33	123	7.79	1
3	Based on Self-Assessment	66	75	71	212	13.43	2
4	Inappropriate rate and exemption limit	115	108	89	312	19.77	4
5	Lack of accuracy on submitted bills and vouchers	75	86	98	259	16.41	3
6	Less provision of fines and penalties	97	115	125	337	21.36	6
Total		525	528	525	1578	100	

Source: Opinion Survey

The main loopholes of income tax act, 2058 ranked in order of preference of the respondents are as follows:

1. Complicated income tax act, rules and regulation
2. Based on self assessment
3. Lack of accuracy an submitted bills and vouchers
4. Inappropriate rate and exemption limit
5. High rate of depreciation
6. Less provision of fines and penalties

From the above survey, we can say that the main loopholes of income tax act 2058 are complicated income tax act, rules and regulation, based on self assessment, lack of accuracy on submitted bills and vouchers etc.

4.4.10 Motivating Factor for the Tax Payers

In Nepal, people are not fully aware about the tax practices. Moreover there is a practice of tax evasion. People take tax as a burden. But government should motivate them to pay the tax so as to increase the revenue. We hap asked a question to the respondents regarding this matter. The question was "What should government do for the tax payers who pay more tax in order to motivate them?" The response received from the respondents was as follows:

Table No. 4.31
Motivating Factor for the Highest Tax Payers

S.N.	Motivating factor	Respondents						Total	%
		A	%	B	%	C	%		
1	The should be honored as CIP	6	24	1	4	8	32	15	20
2	Government Should provide facilities like free medical Service, free education etc.	16	64	13	52	13	52	42	56
3	Certain percent tax refund in upcoming years.	3	12	11	44	4	16	18	24
Total		25	100	25	100	25	100	75	100

Source: Opinion Survey

From the above survey, 56% of the respondents preferred different facilities from government like those in developed countries such as free medical service, free education etc. 24% respondents went for certain percent tax refund in upcoming years and rest 20% preferred the honors of CIP (Commercially Important Person). So, the government should put more emphasis on providing different facilities to the highest tax payers in order to encourage them.

4.4.11 Appropriate Method of Income Tax Assessment

Method of Income Tax assessment is very important in the assessment of income tax. Sound and appropriate assessment procedure is essential for the collection of the large amount in the form of income tax. It is very important in managing the income tax because the amount of income tax is realized through the assessment. To find out an appropriate method of income tax assessment a question was forwarded to the respondents what method is most appropriate in Nepal for assessing income tax?" The response received is tabulated below.

Table No. 4.32
Appropriate Method While Assessing Income Tax

S.N.	Methods	Respondents						Total	%
		A	%	B	%	C	%		
1	Assessment on the basis of accounts submitted by the tax payers.	7	28	5	20	12	48	24	32
2	Self Assessment	8	32	19	76	11	44	38	50.66
3	Assessment on the best judgement	10	40	1	4	2	8	13	17.33
4	Assessment by the committee	0	0	0	0	0	0	0	0
Total		25	100	25	100	25	100	75	100

Source: Opinion Survey

From the opinion survey, it has been clear that self assessment method is most appropriate for Nepal while assessing income tax 50.66% of the respondents are in favor of self assessment while 32% of respondents prefer assessment on the basis of account submitted by tax payers.

4.4.12 Most Important Factor for Effectiveness of Income Tax in Nepal

In order to know the most important factor for effectiveness of income tax in Nepal respondents were requested to rank their responses on given choices. The question was, "What is the most important factor for effectiveness of income tax in Nepal?" Table No. 4.33 gives a break down of responses:

Table No. 4.33
Most Important Factor for Effectiveness of Income Tax in Nepal

S.N.	Factor	Respondents			Total Score	%	Rank
		A	B	C			
1	Honest tax officers	87	53	60	200	27.32	3
2	Honest tax payers	52	52	59	163	22.26	2
3	Clear act, rules and regulation	46	67	32	145	19.81	1
4	Effective income tax administration	65	75	84	224	30.60	4
Total		210	247	235	732	100	

Source: Opinion Survey

The most important factors for effectiveness of income tax were ranked in order of the preference of the respondents were as follows:

1. Clear acts, rules and regulation
2. Honest tax payers

3. Honest tax officers
4. Effective income tax administration

It can be concluded that clear act, rules and regulation is needed for the effectiveness of income tax in Nepal.

4.4.13 Suggestions for Achieving Effectiveness of Income Tax in Nepal

To know the other important factors for effectiveness of income tax, a question was asked "Do you have any others suggestions for achieving effectiveness of income tax in Nepal?" The responses are as follows:

1. Tax system should be simple, transparent and clearly understandable to the general public.
2. Training programs should be organized to the tax personnel in order to make them up-to-date and to develop effective tax management system.
3. Public awareness is necessary for successful application of income tax. So, tax education should be given from the school level, it should be included in school curriculum.
4. There should be proper co-ordination among tax related departments such as Department of Revenue Investigation, Custom Department, and Inland Revenue Department. And networking of information system should be developed accordingly.
5. 'Tax Payers friendly' environment should be created in tax offices.
6. Government should have ability to convince the tax payers about the proper utilization of money, which they have paid as tax.

4.5 Major Findings of the Study

On the basis of data presentation and analysis in above mention sub-chapter some important findings of the study are summarized below:

1. The study shows that the contribution of tax revenue to total revenue is 79.45% and of non-tax revenue to total revenue is 20.55% in FY 2007/08. The share of tax revenue is in increasing trend.

2. Nepalese tax revenue is composed of both direct and indirect tax revenue. There is a dominant role of indirect tax revenue in Nepalese tax structure. The contribution of direct tax and indirect tax to total tax revenue was 26.14% and 73.86% in FY 2000/01 which become 24.32% and 75.68% in FY 2007/08. Although the total amount of both taxes is increasing, there is not satisfactory growth in collection of both taxes.
3. The contribution of customs, excise duty and VAT on indirect tax revenue were 44.82%, 14% and 41.28% respectively in FY 2000/01 and contribution of each taxes were reached to 35.30%, 14.97% and 49.72% respectively in FY 2007/08. It shows that the custom duty is in decreasing trend where as excise duties and VAT is in increasing trend.
4. The contribution of income tax, land revenue and registration, urban house and land tax, vehicle tax an direct tax revenue were 82.09%, 13.35%, 1.64% and 3% respectively in FY 2000/01. The contribution from other taxes was nil during that period. This was reached to 74.27%, 15.61%, 0%, and 6.07% in FY 2007/08. The contribution from other taxes was 4.05% during this year. In the composition of direct tax, income tax was the giant one which contribution seems to be fluctuating every year. The percentage contribution from land revenue and registration is in increasing trends and from urban souse and land tax come to nil in the proceeding years.
5. Income Tax has been considered as suitable source for mobilizing internal resources. It can be used as a positive instrument to boost up government revenue collection, to develop the economic condition of Nepalese people, to promote distributive justice and to eliminate the resource gap problem.
6. Total tax revenue covered only 8.71% of GDP in FY 2000/01. This increased to 10.14% in FY 2005/06. In FY 2007/08 this ratio was only 9.51%. There is no significant increment in total tax revenue/GDP ratio in last eight fiscal years.
7. The indirect tax /GDP ratio, custom duty/GDP ratio, excise duty/ GDP ratio and VAT /GDP ratio was 6.43%, 2.88%, 0.89% and 2.66% respectively. These were reached to 7.20%, 2.54%, 1.08% and 3.58% respectively in FY 2007/08. It shows that the contribution of indirect tax to GDP is not satisfactory in last 8 years however the ratio is in increasing trend.

8. The direct tax/GDP ratio, contribution of direct tax to total tax revenue and total revenue in FY 2000/01 was 2.28%, 26.14% and 20.18% respectively, which were 2.31%, 24.32% and 19.32% respectively in FY 2007/08. It means there is not substantial growth in the collection of direct tax.
9. The income tax/GDP, income tax/total revenue, income tax/total tax revenue and income tax/direct tax revenue ratio were 1.87%, 16.56%, 21.46% and 82.09% respectively in FY 2000/01 which had been changed to 1.72%, 14.35%, 18.06% and 74.27% respectively in FY 2007/08. It shows that there is decrease in every ratio for the last eight years.
10. Total income tax is the composition of corporate income tax, individual income tax, remuneration tax and tax on interest. Corporate tax and individual income tax which are the major components of income tax is in decreasing trend. But the remuneration tax and interest tax is in increasing trend. The contribution of remuneration tax has doubled in last eight years.
11. The resource gap is increasing every year. It was Rs. 22328 million in FY 2000/01 and increased to Rs. 38607.10 million in FY 2006/07. It shows the poor performance of domestic resource mobilization. The amount of foreign grants is slightly increasing and amount of foreign loan is in decreasing trend. The resource gap as % of total expenditure was 37% in FY 2000/01 and 35% in FY 2006/07.
12. Total government revenue has contributed 62.52% in financing govt. expenditure in FY 2000/01. Similarly foreign aid and CITER had contributed 27.17% and 4.5% respectively. In FY 2007/08 the contribution of government revenue, foreign aid and CITER to total govt. expenditure is 65.18%, 19.88% and 3.25% respectively. There is a drastic reduction in the contribution made by foreign aid and CITER. Foreign aid is declined due to the lack of funding by donor agencies. Similarly, the contribution % of corporate sector is declined mainly because of the unfriendly business environment created by unstable political and economic situation of the country.
13. The corporate tax rates have been revised for several times. Now days, special industries, general industries and non-industries banking and insurance business

are taxed at a flat rate of 20%, 25% and 30% respectively in spite of the progressive, progressive & flat tax rate in previous years.

14. The contribution of CITR on income tax revenue was 43.45% in FY 2000/01, of which public sector and private sector contributed 24.73% and 18.72% respectively. In FY 2007/08 CITR has contributed 34.69% of which public and private sector share was 1.88% and 32.81% respectively. CITR has decreased due to the unfavorable business environment. The CITR from public sector has drastically reduced in last eight year. This may be due to the inefficiency of public enterprises. Most of the public enterprises are suffering from heavy losses due to their inefficient operation. But private sector is flourishing day by day so their share in CITR is also increasing, this may be due to the globalization and economic liberalization in the country.
15. Contribution of CITR on total government revenue was 7.20% in FY 2000/01. In which public and private sector contributed 4.10% and 3.10% respectively. The share of CITR to total revenue was maximum i.e. 9.91% in FY 2002/03. After that it is in diminishing trend. In FY 2007/08, the share of CITR is only 4.98% of total government revenue in which the share of public and private sector is only 0.27% and 4.71% respectively.
16. In the structural composition of corporate income tax, public sector had played a dominating role in the initial years. In FY 2000/01 share of public and private sector was 56.93% and 43.07% respectively. But in FY 2007/08 the share of public sector has decreased to 5.43% and that of private sector has increased to 94.57%. It shows the flourishing trend of private sector in the economy.

On the basis of empirical analytical analysis some major findings can be drawn which are summarized as given below:

1. 96 percent of the total respondents believe that people are not well informed about the income tax system in Nepal.
2. 76 percent of the total respondents believe that the contribution of income tax is not satisfactory in national revenue. The low collection from income tax is due to the lack of tax education.

3. 56% of the total respondents believe that present income tax rate is appropriate in Nepal. However, 44% of the respondents think that present income tax rate is high, out of which 36.36% of respondents prefer 15% income tax rate.
4. 53.33% of the total respondents believe that contribution of income tax is not satisfactory because of income tax act, 2058. The major weakness of income tax act, 2058 is that the assessment of income tax is not based on best judgement.
5. 57.33% of the respondents think that income tax administration is not sound after merging of tax and VAT office. The main reason for this is increasing habit of tax evasion by taxpayer after registering in VAT.
6. 56% of total respondents believe that present income tax administration is satisfactory. Whereas 40% of respondents believe it is inefficient and 4% of respondents go for efficient. Since 40% of the respondents believe present income tax administration is inefficient, the main reason for inefficient income tax administration is lack of trained and competent tax officials.
7. 41.33% of the total respondents believe that the main problem facing by tax payers while paying tax is vague provision in income tax laws. Where as 29.33%, 17.33% and 12% are in favor of time consuming process, expectation of illegal incentives by tax personnel and lack of co-operation by tax administrators respectively.
8. 72% of the total respondents believe that few submission of income tax return is the main cause of low collection from income tax, out of which 53.70% respondents think that awareness should be given through newspaper and mass media in order to increase the submission of income tax return.
9. The main loopholes in income tax act, 2058 is complicated income tax act, rules and regulation.
10. 56% of the total respondents believe that highest tax payer can be motivated by providing different services such as free health service, free education etc. whereas 24% of the respondents believe that they can be motivated by refunding certain percent tax in upcoming years. And 20% of the respondents believe that they can be motivated by recognizing them as commercially important person.

11. 50.66% of the total respondents believe that self-assessment method is appropriate while assessing income tax in Nepal. 32% of the respondents go for assessment on the basis of accounts submitted by the tax payers and rest 17.33% respondents are in favor of assessment on the best judgement.
12. Clear act, rules and regulation is the most important factor for effectiveness of income tax in Nepal.

CHAPTER V

SUMMARY, CONCLUSION & RECOMMENDATIONS

5.1 Summary

In our country, there is lack of the financial resources and a lot funds are required to do the development activities. Nepal has been suffering from the shortage of capital to accelerate the economic growth. There is so much resource gap so in order to fulfill the shortage, government is depending on the foreign grants and loans. So to fulfill the resource gap income tax, a direct tax is most important sources of internal revenue. Due to the low economic activities and lesser development of the corporate sector, the contribution of income tax to the total revenue is very low.

The study shows that the percentage of tax revenue and non tax revenue to total revenue was 79.45% and 20.55% respectively in fiscal year 2007/08, the ratio of total tax revenue to GDP was only 9.51% in the fiscal year 2007/08. The total tax revenue was very few. This may be because of the low economic activities, mass poverty and low income level of people. The percentage of total tax revenue to GDP of about 13% is regarded satisfactory in case of the developing country.

In Nepalese economy, the percentage of indirect tax to total tax revenue is 75.68% and direct tax to total tax revenue is 24.32% in the FY 2007/08. So the direct tax revenue portion to tax revenue is low which may be due to the low income level and loss improvements of the private sectors as well as public enterprises.

The composition of the corporate income tax seems to be dominated by private sector in the FY 2007/08. The average contribution of Public sector and private sector are 5.42 and 94.58% respectively. Similarly the percentage of corporate income tax to income tax revenue was 34.69%.

During the study period, the resource gap has been increasing every year. It was Rs. 22328 million in the FY 2000/01 and increased to 38607.1 millions in the FY 2007/08. This shows the poor performance of the domestic resource mobilization. It was found that the contribution of government revenue, foreign aid and corporate income tax to total government expenditure was 65.18%, 19.88% and 3.25% respectively in FY 2007/08.

In order to find out the problems in the income tax administration, a set of questionnaires were distributed among tax administrators, tax experts and tax payers. On the opinion survey empirical investigation has found the weaknesses of the income tax act as well as the income tax administration which follows as below.

According to survey 96% of the total respondents believed that taxpayers were not well informed about the income tax system in Nepal. So awareness programmes and tax education were to be given to the tax payers. 56% of the total respondents were in favor that the present income tax rate appropriate in Nepal. 44% preferred that the rate was high and among them 36.36% recommended the 15% tax rate was appropriate to increase the income tax collection.

53.33 of total respondents believed that the contribution from income tax was not satisfactory because of the income tax act 2058 in which assessment system is not based on the best judgment.

57.33% of total respondents believed that after merging VAT and income tax administration the administration was not sound and lot of tax evasion were recorded after a taxpayer registered on VAT.

56% of total respondents believed that the income tax administration was satisfactory. 41.33% of the total respondents believed that the vague provision in income tax laws was the main problem facing by tax payers while paying income tax.

72% of the total respondents believed that the few submission of income tax returns was the main cause for low collection from income tax and awareness should be given

through mass media to increase the returns rather than levying the fines and penalties. The main loopholes of the income tax act 2058 were found to be the complicated income tax acts, rules and regulations. So the provisions like installment returns, installment payment, and submission process of the income tax returns should be simplified.

In order to motivate the highest tax paying firm and person 56% of total respondents believed that the highest payers should be motivated by providing the services like free health service, free education facilities as provided by developed countries.

The appropriate method of assessment system was found to be the self assessment system as 50.66% of total respondents supported because a genuine taxpayer knows his transactions and expenses if recorded properly. So, clear acts rules and regulation is necessary for the effectiveness of the income tax administration and income tax laws should be simplified because it is vague.

5.2 Conclusion

The economy of a nation largely depends on the well developed private sector. The private sector can be developed through corporate friendly laws, rules and regulations as well as the process of industrialization. A good corporate culture is very important to develop corporate sector.

As Nepal is adopting the mixed economy for last five decades and have been liberalized from 1990's. By constitution, Nepal has encouraged the foreign investments. Various corporate friendly, laws rules has been formulated. Many public enterprises has been privatized and liquidated, some are in the process of privatization. Nepal has entered to WTO from 23rd April 2004 and has given emphasis to foreign trade and foreign direct investments. Also the rate of custom duties has been lowered and relief in other trade barriers. Due to liberalized economy number of multinational companies has been established. Though there is establishment of multinational companies, they are facing various challenges. The challenges are open boarder, smuggling of goods

and services, improper billing, tax evasion, political instability, strike, insecurity and unhealthy relation between labor union and the management.

The resource gap has been increasing every year. The internal source of revenue cannot meet the regular expenditure so for the development activities depend on the foreign grants and loan. There is always trade loss in foreign trade. The trade deficits have been increasing every year.

Income tax is very important source of tax for the generation revenue from internal sources. We can see the status of a country with the contribution of income tax to national revenue. If the ratio of contribution is high then the status of development is more. So in developed countries the contribution from income tax to national revenue is very high.

In order to increase the contribution from income tax, Nepal has adopted the new income tax act 2058 from 19th chaitra 2058 B.S. This act has been formulated so as to encourage the foreign investors. This act has the feature of self assessment system with broad tax base.

The corporate sectors are in the initial stage of development. The role of industrial sector is very poor. We have to depend on the foreign countries for raw materials as well as technologies. Due to land locked nature the carriage cost of the industrial raw materials is very high. Also our economy is more or less depended on the Indian economy. So most of the profits are diverted to foreign countries.

These days after the restoration of democracy in 2063 B.S., due to the peaceful nature and feeling of security there is chances for good business environment. The hotel and tourism sector are progressing these days and is the future for Nepalese economy.

The income tax act 2058 has encouraged developing the corporate culture in the country. It has transformed the ad-hoc based accounts to account based self assessment. The strength of the act are broad base, appropriate rate of tax, appropriate method of

calculation of depreciation provision for loss carry forward for consecutive year, provision of installment and use of the information technology.

Though the act have good aspects, in the implementation there are following challenges, the acts, rules and regulation are not consistent, the tax education part is very poor, there is problem of under invoicing, improper billing and after registration to VAT, taxpayers use to evade the tax by showing less transaction. Also there is smuggling of goods due to the open boarder and inefficiency of the administration. Though the tax department is applying IT, it is not well educated to tax payers as well as the tax personnel. The tax personnel don't get appropriate training. The manpower development planning is desired for the efficiency of tax personnel so as to improve the tax administration and tax compliance. Hence tax compliance can be improved with the remedy of the above challenges.

5.3 Recommendations

On the basis of this research, following recommendations are recommended by researcher in order to increase the contribution of income tax in revenue collection as well as for the effectiveness of the income tax act in Nepal.

1. The rate of total tax to GDP is 9.51 % which is very low. The ratio can be increased by levying tax on education, public transport etc and broadening the tax net.
2. The VAT is regarded as good source of indirect tax. The government should encourage the entrepreneur to join VAT, take PAN and systematize the custom.
3. Consumer awareness lottery is good method for proper billing in VAT. So this type of awareness programme should be continued and simplified.
4. There should be good policy so as to control under invoicing. This can be controlled only through application of ASYCUDA, proper declaration of goods value in custom point and proper billing in manufacturing level.
5. The under invoiced goods should be bought by the government.
6. The transaction record between tax payers more than one lakh should be exchanged among Inland Revenue offices.

7. Proper tax incentives should be given to sick industrial units like Hotel and Tourism.
8. The foreign grants and loans should be invested on the projects with high return ratio.
9. The sick public enterprises should be privatized and the sectors which are interested by private sectors should be handed to the private sectors.
10. There should be tax facilities to attract the foreign investment. Different tax facilities should be given to multinational companies and export based industries.
11. There should be good monitoring policy. The tax officers should have access to the taxpayer's premises which can be met by reorganizing the existing Inland Revenue offices.
12. The service sectors should be properly defined and they should be covered in tax net.
13. Tax education should be given to general public. For this purpose, tax education should be included in the syllabus of the secondary education.
14. Highest tax paying person should be motivated by giving different facilities and by honoring him.
15. The income tax act should be very simple. Tax laws, rules and regulations should be consistent.
16. Heavy fines and penalties should be strictly levied so as to harass the tax evaders.
17. There should be effective coordination among the different tax related departments.
18. Tax deduction at source should be simplified by use of IT. The new programme E-tds should be encouraged to tax payers.
19. The services given by revenue offices should be simplified and all the tasks should not be paper based but IT based.
20. Provision of reward, prize and incentives should be introduced to encourage the tax payers to pay tax voluntarily rather than through coercive measures.

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Appendix I

Tax Revenue

Headings	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
Customs	10813.3	12552.1	12658.8	14236.4	15554.8	15701.6	15344
Imports	8959.9	10391.9	9678.4	10567.7	10666.9	12299.1	11744.6
Exports	432.5	492.6	917.4	855.6	527.1	697.9	625.6
Indian Excise Refund	1331.7	1456.2	1700.9	2370.6	3882.7	2188.3	2314.4
Others	89.2	211.4	362.1	442.5	478.1	516.3	659.4
Tax on Consumption and Product of Goods and Services	13387.3	16153.6	16074.3	18244.8	20705.6	25331.3	28118.3
Excise on Industrial Products	3127.6	3771.2	3807	4785.1	6226.7	6445.9	6507.6
Value Added Tax	10259.7	12382.4	12267.3	13459.7	14478.9	18885.4	21610.7
Land Revenue and Registration	1015.9	612.9	1131.8	1414.3	1697.5	1799.2	2181.1
Land Revenue	4.6	5.1	0.8	0	0	0	0
House and Land Registration Fees	1011.3	607.8	1131	1414.3	1697.5	1799.2	2181.1
Tax on Property, Profit & Income	7935.6	9546.5	9465.7	8691.5	10215.1	11272.6	11787
Income Tax from Public Enterprises	2198.8	2928	1769.3	1251	2056.6	1332.4	195.7
Income Tax from Semi-Public Enterprises	0	0	0	0	0	0	0
Income Tax from Private Corporate Bodies	1339.5	1924.3	1412	1236.3	1531.3	2467.8	3404.3
Income Tax from Individuals	3016.4	3200.5	4419.1	3362.3	3533.4	3926.3	4234.7
Income Tax from Remunerations	451.5	597.3	835.6	1252.6	1391.2	1675.9	1764.1
Urban House and Land Tax	118.5	2.9	2.3	0	0	0	0
Vehicle Tax	396.5	429.6	559.7	559.5	700.6	806.5	847.6
Tax on Interest	414.4	463.9	467.7	864	733.4	757	774.9

Other Taxes	0	0	0	165.8	268.6	306.7	565.7
Total	33152.1	38865.1	39330.6	42587	48173	54104.7	57430.4

Note: Value Added Tax includes Sales Tax, Entertainment Tax, Hotel Tax, Air Flight Tax, and Contract Tax

Source: Financial Comptroller General Office

Appendix II

Non-Tax Revenue

Headings	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
1. Charges, Fees, Fines and Forfeiture	386.3	386.7	518.8	579.6	1202.5	1202.5	1927.7
Firm Registration	65.8	60	71.9	78.7	85.1	85.1	147
Arms Registration	2.4	1.5	1.4	1.6	2.4	2.4	3.6
Vehicle License	106	95	111.1	119.5	635.4	635.4	677.4
Judiciary	95.8	106.8	192.2	104.3	102.1	102.1	506.8
Administration, Penalty & Forfeiture	116.3	123.4	142.2	275.5	377.5	377.5	592.9
2. Receipts from sales of Commodities and Services	2428.9	2728	2611.1	3063	3497	3497	3932.4
Drinking Water	14.1	9.1	6.5	5.6	5.3	5.3	3.7
Irrigation	1.5	1.1	1.3	1.4	0.6	0.6	1.3
Electricity	0.3	0	0	0	0	0	0
Postal Service	226.6	229.6	230.3	219.9	247	247	246.3
Food and Agriculture	43.4	50.6	45.9	42.3	42.8	42.8	57.2
Education	83.5	94	128	112.3	128.7	128.7	143.1
Forest	525.2	602.6	546.2	683.6	674.1	674.1	410.2
Transport	86	86.3	99.9	93.5	131.6	131.6	116.8
Others	1448.3	1654.7	1553	1904.4	2266.9	2266.9	2953.8
3. Dividend	2507.5	2336.5	2512.9	2497.6	2661.1	2661.1	3394.8
Financial Institutions	2135.5	2076.3	2281.8	1904.3	1103.1	1103.1	1313.9

Trading Concerns	9.7	13.4	8.8	11	9.1	9.1	4.7
Industrial Undertakings	103.2	0	0	6.1	3	3	3.2
Services Sector	138	226.6	161.8	576.2	1510.3	1510.3	2073
Others	121.1	20.2	60.5	0	35.6	35.6	0
4. Royalty and Sale of Fixed Assests	563.3	949.6	723.9	1945.4	1465	1465	1196.8
Royalty from Mining	11.7	5.4	15.3	11.9	9.8	9.8	13.6
Other Royalties	370.9	483.1	637.2	1142.1	1002.2	1002.2	933.6
Other Sales	180.7	461.1	71.4	791.4	453	453	249.6
Mint	0	0	0	0	0	0	0
Others	0	0	0	0	0	0	0
5. Principal and Interest Payment	3751	3497.2	3109.5	2464.3	3507.1	3507.1	3251.3
Loan Corporations	2176	2050.6	1880.7	1516.7	1826.7	1826.7	1510.5
Interest from Loan to Companies & Corporations	1565.1	1437.1	1206.8	911.2	1654	1654	1732.9
Others	9.9	9.5	22	36.4	26.4	26.4	7.9
6. Miscellaneous Items	104.6	130.8	1638.8	3092.8	1825.3	1825.3	1148.7
Miscellaneous	104.6	130.8	1638.8	3092.8	1825.3	1825.3	1148.7
Total	9741.6	10028.8	11115.0	13642.7	14158.0	16018.0	14851.7

Source: Financial Comptroller General Office

Appendix III

GDP, GDP Growth Rate, Deflators and Composition by Broad Industry Group

(Rs.
in Million)

Fiscal Year	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
GDP at basic prices(current)	413429	430397	460325	500699	548485	603673	670589
Primary Sector	157442	168239	175113	188632	202116	214071	231983
Secondary Sector	71744	75712	81228	86902	94311	101781	109603
Tertiary Sector	196269	200101	217205	242460	270152	307233	349973
FISIM	12026	13655	13221	17294	18094	19412	20971
GDP at basic price (constant)	413429	414091	429699	448654	461452	475953	486842
Primary Sector	157442	162398	167801	175765	181979	81003	185475
Secondary Sector	71744	72220	74452	75557	77756	184145	82671
Tertiary Sector	196269	192782	199874	213504	218896	229236	238608
FISIM	12026	13309	12428	16173	17180	18431	19912
Annual Growth Rates of GDP (in percentage)		0.16	3.77	4.41	2.85	3.14	2.29
Primary Sector		3.15	3.33	4.75	3.54	1.19	0.72
Secondary Sector		0.66	3.09	1.48	2.91	4.18	2.06
Tertiary Sector		-1.78	3.68	6.82	2.53	4.72	4.09
Implicit GDP Deflator	100.0	103.94	107.13	111.60	118.86	126.83	137.74
Primary Sector	100.00	103.60	104.36	107.32	111.07	116.25	125.08
Secondary Sector	100.00	104.83	109.10	115.02	121.29	125.65	132.58

Tertiary Sector	100.00	103.80	108.67	113.56	123.42	134.02	146.67
Composition of GDP (in percentage)							
Primary Sector	37.01	37.89	39.98	36.42	35.67	34.35	32.19
Secondary Sector	16.86	17.05	17.15	16.78	16.65	16.35	16.09
Tertiary Sector	46.13	45.06	45.87	46.81	47.68	49.30	51.71
FISIM	-2.91	-3.17	-2.87	-3.45	-3.30	-3.22	-3.13

Source: Central Bureau of Statistics

Questionnaire

Name.....

Designation.....

Office/Organization.....

Occupation.....

Please you are requested to tick (v) the suitable answers of your choice from the following questions or wherever appropriate **please rank** them in order of preference from I to last number. Number 1 stands for the most important and the last number for least.

1. Do you think that people are well informed about the income tax system in Nepal?

(i) Yes ()

(ii) No ()

2. In your opinion is contribution of income tax to national revenue is satisfactory?

(i) Yes ()

(ii) No ()

If no, what are the main causes of tax payer wise low collection from income tax in Nepal? (**Please rank according to the priority**)

(i) Inconsistent tax acts, rules and regulation ()

(ii) Loopholes in income tax act ()

(iii) Inefficient tax administration ()

(iv) Existence of smuggling ()

(v) Improper billing system ()

(vi) Lack of tax education ()

(vii) Income tax returns not filing on time ()

(viii) Instable political condition ()

(ix) Increasing tendency of tax evasion ()

(x) Mass poverty and low income level ()

(xi) Other, Please specify.....

3. Is present income tax rates in Nepal high?

(i) Yes ()

(ii) No ()

If yes, what should be the maximum rate of income tax?

(i) 20% ()

(ii) 18% ()

(iii) 15% ()

(iv) 10% ()

(v) Others ()

4. Do you believe that the contribution of income tax is not satisfactory because of income tax act 2058?

(i) Yes ()

(ii) No ()

If yes, what is the major weakness in income tax act 2058, for low contribution from income tax?

(i) It is fully based on self assessment ()

(ii) Amended assessment is not in practice ()

(iii) Assessment of income tax is not based on best judgment ()

(iv) Complication due to the merging of tax and VAT administration ()

(v) No harmony between VAT and income tax act. ()

(vi) Others, please specify.....

5. Do you believe that the income tax administration is not sound after merging of tax and VAT office?

(i) Yes ()

(ii) No ()

If yes, what is the main reason?

(i) Difficulty in management due to the large numbers of tax payers ()

(ii) Inefficient tax officials ()

(iii) Complication due to disharmony between income tax and VAT ()

(iv) Increasing habit of tax evasion by tax payers once they are registered in VAT ()

(v) Others, if any please specify.....

6. What do you feel about the present income tax administration of Nepal?

(i) Efficient ()

- (ii) Inefficient ()
- (iii) Satisfactory ()

If inefficient, what are the major causes? **(Please rank)**

- (i) Lack of trained and competent tax officials ()
- (ii) Lack of delegation of authority among tax personnel ()
- (iii) Lack of proper direction ()
- (iv) Lack of effective communication ()
- (v) Unnecessary outside pressure ()
- (vi) Undue delay in making assessment ()
- (vii) Lack of coordination among tax related departments ()
- (viii) Complicated tax laws ()
- (ix) Others, if any please specify.....

7. In your opinion, what types of problems are facing by the tax payers while paying income tax?

- (i) Time consuming process ()
- (ii) Expectation of illegal incentives by tax personnel ()
- (iii) Vague provisions in income tax laws ()
- (vi) Lack of cooperation by tax administrator ()
- (vii) Others, if any please specify.....

8. Each year only about 60 percent of the total tax payers submits income tax return to the revenue office. Do you believe that it is the main reason of decreasing income tax?

- (i) Yes ()
- (ii) No ()

If yes, what should be done to increase the submission of income tax return?

- (i) Heavy fines and penalties should be levied ()
- (ii) Awareness should be given through newspaper and mass media ()
- (iii) Certain exemption should be given for timely submission of income tax returns()
- (iv) Provision of reward ()
- (v) Others, Please specify.....

9. What do you think is the main loopholes in income tax act 2058? **Please rank.**

- (i) High rate of depreciation ()

- (ii) Complicated income tax act, rules and regulation ()
- (iii) Based on self assessment ()
- (iv) Inappropriate rate and exemption limit ()
- (vi) Lack of accuracy on submitted bills and vouchers ()
- (vii) Less provision of fines and penalties ()
- (viii) Others, please specify.....

10. What should government do for the tax payers who pays more tax in order to motivate them?

- (i) They should be honored as CIP (commercially important person) ()
- (ii) Government should provide different facilities like those in developed countries such as free medical service, free education etc. ()
- (iii) Certain percent of tax refund in upcoming years ()
- (iv) Others, please specify

11. What method is more appropriate for in Nepal for assessing income tax?

- (i) Assessment on the basis of accounts submitted by the tax payers ()
- (ii) Self Assessment ()
- (iii) Assessment on the best judgment ()
- (iv) Assessment by the committee ()
- (vii) Others, please specify.....

12. What is the most important factor for effectiveness of income tax in Nepal? **Please rank.**

- (i) Honest tax officers ()
- (ii) Honest tax payers ()
- (iii) Clear act, rules and regulation ()
- (iv) Effective income tax administration ()
- (viii) Others, Please specify.....

13. Do you have any others suggestions for achieving effectiveness of income tax in Nepal? If yes, please specify:

.....
.....
.....

THANK YOU FOR YOUR GOOD CO-OPERATION

List of Respondents

Tax Officials:

S.N.	Name of the Respondents	Office	Designation
1	Bijaya Acharya	IRO-2	Tax Officer
2	Bol Raj Acharya	IRO-2	"
3	Deepak Gautam	IRO-1	"
4	Dhani Ram Sharma	IRO-1	"
5	Dhruba Pokhrel	IRO-3	"
6	Dilip Kumar Adhikari	IRO-2	"
7	Dinesh Sharma	IRO-1	"
8	Harihar Prasad Acharya	IRO-1	"
9	Jagadish Upadhyaya	IRO-2	"

10	Jay Bahadur Bhandari	IRO-2	"
11	Jhakka Prasad Acharya	IRO-1	"
12	Kapil Prasad Subedi	IRO-1	"
13	Keshab Kumar Uprety	IRO-1	"
14	Lava Kumar Adhikari	IRO Lalitpur	"
15	Madan Dahal	IRO-2	"
16	ManiDev Bhattarai	IRO-1	Chief Tax Officer
17	Mohan Singh Basnet	IRO-1	Tax Officer
18	Rajendra Chudal	IRO-1	"
19	Rajendra Hamal	IRO-2	"
20	Santi Ram Niraula	IRO-2	"
21	Sunil Kumar Shrestha	IRO-1	Chief Tax Officer
22	Tanka Nath Poudel	IRO-1	Tax Officer
23	Tek Bahadur Aryal	IRO-2	"
24	Tika Ram Bhusal	IRO-2	"
25	Umesh Shrestha	IRO-1	"

Tax Experts:

S.N.	Name	Organization	Designation
1	Amar Bahadur Bista	Bista & Co.	RA
2	Anup Shrestha	AB Shrestha & Co.	RA
3	B.K. Agrawal	B.K. Agrawal & Co.	CA
4	Bal Ram Chaudhary	B.R. Chaudhary & Organization	RA
5	Bhanu Bhakta Pokhrel	Pokhrel & Co.	RA
6	Birendra Dahal	Raut & Co.	Audit Assistant
7	Dipak Rimal	Rimal & Co.	RA
8	Diwakar Dahal	D. Dahal & Co.	RA

9	Gopal Kumar Agrawal	B.K.Agrawal & Co.	CA
10	Jit Man Shrestha	A. Kumar & Co.	RA
11	Keshav Tripathi	Thompson Nepal Pvt. Ltd.	CA
12	Mahesh Lamichhane	Mahesh & co.	RA
13	Manish Amatya	Amatya & Co.	CA
14	Narayan Bajaj	Bajaj & Co.	FCA
15	Nem Lal Amatya	Amatya & Co.	FCA
16	Netra Man Singh Karki	Karki & Co.	RA
17	P.K. Swarnkar	B.K. Agrawal & Co.	CA
18	Pawan Khadka	Upendra & Co.	RA
19	Rakesh Lal Karna	S.C. Lal Associates	RA
20	Ratan Kumar Mishra	R.K. Mishra & Co.	RA
21	Ribendra Raut	Raut & Co.	RA
22	S.K. Jhunjhunwala	Subash & Co.	CA
23	Sunil Kumar Jain	Jain & Co.	RA
24	Tulsi Jung Katuwal	Katuwal & Associates	RA
25	Upendra Sapkota	Upendra & Co.	RA

Tax Payers:

S.N.	Name	Organization	Designation
1	Ashish Thakur	Lm Suvir & Brothers Golf Club, Gokarna	Finance Manager
2	Ashok Kumar Agrawal	AC Garments	Director
3	Ashok Kumar Joshi	Multi purpose Institute & Cyber Communication Pvt. Ltd., Gongabu	Accountant

4	Bishal Rimal	Rimal & Co.	Accountant
5	Gagan Kansakar	Autoparts International, Putalisadak	Proprietor
6	Gopi Krishna Chokhani	Dashing Traders	Proprietor
7	Hari Shrestha	The Bakery Cafe	Accountant
8	Kishor Shrestha	Everest Express Tours & Travels, Durbarmarg	Senior Accountant
9	Koshish Rimal	T.M. Subedi & Co.	Accountant
10	Madhur Lal Sinya	Yeti Travels Pvt. Ltd.	Account Head
11	Manish Sapkota	New Saburi Coal Trading	Accountant
12	Mukunda Sharma	Nepal Travels Pvt. Ltd. Durbarmarg	Account Head
13	Nabin Lal Joshi	Thompson Nepal Pvt. Ltd. Tripureshwor	Account Officer
14	Prabhat Acharya	Super Lemicoats Pvt. Ltd., Putalisadak	Administrative Officer
15	Prem Hari Rajbhandari	Mercantile Traders, Durbarmarg	Account Head
16	Rup Narayan Chaudhary	M.S.D. Nepal Pvt. Ltd.	Manager
17	Sajjad Alam	Hotel Everest Ltd.	Senior Accountant
18	Santosh Lal Shrestha	Max International, Buddhanagar	Director
19	Santosh Mani Neupane	Nobel Academy	Director
20	Sekhar Shrestha	Titan International, Chabahil	Accountant
21	Shiba Hari Sapkota	Durbar Hotel	Chief Accountant
22	Surendra Kumar Goel	Arvind Emporium	Proprietor
23	Umesh Katuwal	Katuwal & Co.	Accountant
24	Utpal Rimal	T.M. Subedi & Co.	Accountant
25	Yogeshwor Krishna Parajuli	Taec Consult Pvt. Ltd., Shankhamul	Director

