

STRUCTURE OF TAX REVENUE IN NEPAL

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in

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Submitted by

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LETTER OF RECOMMENDATION

This thesis entitled “*Structure of Tax Revenue in Nepal*” is prepared by Kavita Aryal under my supervision. I hereby recommend this thesis for approval by the thesis committee.

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ABSTRACT

This thesis analyzes the structure of income tax in Nepal and major problems of income tax collection in Nepal. To make the analysis, both primary and secondary data have been used and presented in tables and figures with the help of tools like percentage, average and regression analysis. Secondary data has been gathered through annual report, journals, economic survey and related publications.

The whole study has divided into five chapters. First chapter has given the introduction about the research topic, back ground of the study, Focus of the study, statement of problems, objectives of the study, Importance of the study, Limitations of the study and Organization of the study. Second chapter is the Review of Literature in which different related books, articles, dissertation have been reviewed in the significant way. Different tools and methods used to analyze the thesis are briefly explained in the third chapter 'Research Methodology'. Data presentation and analysis of the data by using different tools is presented in this fourth chapter and summary, conclusion and suggestion has been attached in the fifth chapter.

Total government constitutes tax revenue and non tax revenue. The share of tax revenue has been found always more than non-tax revenue in the government revenue. Trend analysis shows that growth rate tax revenue has 80.41% (Rs.24424.30 million) and 87.70% (Rs. 405866.40 million) respectively in FY 1996/97 and FY 2014/15. The share of non-tax revenue has 19.59% (Rs. 5949.20 million) and 12.30% (49910.70 million) respectively in FY 1996/97 and FY 2014/15. Among direct and indirect taxes, share of direct taxes has been increased each fiscal year than indirect tax. The data shows that share of direct and indirect tax in total tax revenue are Rs. 355955.70 million (28.40%) and Rs. 254866.40 million (71.60%) respectively in FY 2014/15. Land Revenue and Registration & Tax on Property, Profit and Income are main parts of direct tax revenue. The contribution of Land Revenue and Registration & Tax on Property, Profit and Income in the total direct tax was 13.39% and 86.61% in average of FY 1996/97 to FY 2008/09. The average contribution of Tax on Income, Profit & Capital Gain, Property Tax, remuneration tax and other tax on total direct tax are 87.10%, 8.16 & 2.35% and 2.39 % respectively from FY 2009/10 to FY 2014/15. Contribution percentage of income tax to total direct tax is not satisfactory. Custom Duties and VAT have average share in indirect tax is 39.52% and 44.82% in the FY 1996/97 to FY

2009/10. VAT and Import custom duty contributed 45.95% and 27.49% in total indirect tax in average FY 2010/11 to 2014/15. Contribution of Total Revenue, Total Tax Revenue, Direct Tax Revenue and Indirect Tax Revenue on GDP is 19.14%, 16.79%, 4.77% and 12.02 in FY 2014/15. In income tax structure, the share of entity, proprietorship business & individual, investment income and social security tax are fluctuating every year and they share Rs. 43970.9 million (56.32%), Rs. 19606.6 million (25.11%), Rs. 12482.8 million (15.99) % and Rs. 2015 million (2.58%) in the total income tax amounting Rs. 78075.8 million. Contribution of income tax on total governmental revenue, total tax revenue and GDP were 21.95%, 25.03% and 4.20% in FY 2014/15. There was a clear indication of the serious and growing financial resource problem in Nepal and the increasing magnitude of resource gap indicates the internal indebtedness of the country and there is an urgent need for mobilizing additional resources where income tax has appeared one of the most effective fiscal policy instruments to solve the resource problem.

Income tax exemption limit in Nepal are changed on the basis of time and income level. The present exemption limit is provided Rs. 350000 for individual and Rs. 400000 for couples subject to 1% tax on income from remuneration in the FY 2016/17. There were eight slabs of income tax rate from 10% to 55% in the FY 1985/86 in Nepal but at present there are three slabs of income tax rate of 15%, 25% and 35% for personal income and for corporate tax payers they are taxed at the flat rate of 30% for bank and financial institution, insurance company and industry dealing with petroleum products, 20% for special industry and 25% for other corporate tax payers without any exemption limit. In FY 1996/97, the income tax collection performance was 89.74% of estimation and in the FY 2006/07 & 2015/16 it was 118.55 % & 107.39% of estimation respectively.

Opinion survey was conducted to find out the existing problems in income tax collection and probable recommendation to improve the income tax collection in Nepal and few conclusions are drawn from the survey. The major problems of income tax in Nepal inefficient income tax administration which includes failure to maintain proper accounts and records, lack of trained and competent personnel, defective selection procedure of tax personnel, existence of corruption, complicated tax laws and procedure and instability in government in government policy. Other major problems are lack of consciousness of tax payer, widespread evasion and avoidance of income tax, mass poverty, narrow coverage of income tax, predominance of

agriculture in Nepal etc. widespread illegal business operation, inadequate auditing and investigation, difficulties in locating taxpayers, poor development of corporate sector, open boarder with India & Nepal and lack of proper records of taxable individuals and other transactions also played role in problems in income tax collection in Nepal. The recommended major tools to enhance the contribution of income tax on government revenue are extension of income tax coverage, minimizing the problems of tax evasion and avoidance, tax consciousness of people, reform in income tax administration, reform in income tax assessment, and voluntary compliance by the taxpayers.

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LIST OF ACRONYMS

CV	Coefficient of variation
d	Difference of the Rank
FY	Fiscal Year
GDP	Gross National Product
IRD	Inland Revenue Department
NLSS	Nepal Living Standard Survey
PAN	Permanent account number
PE	Probable error
R	Rank Correlation
SD	Standard Deviation
UK	United Kingdom
US\$	United State Dollar
VAT	Value Added Tax
VDIS	Voluntary Declaration of Income Source
WTO	World Trade Organization