RESOURCE MOBILIZATION THROUGH INCOME TAX IN NEPAL

By
UMESH SAPKOTA
Shanker Dev Campus
Campus Roll No.: 569/063
T.U. Regd. No.: 7-2-31-532-2003

A Thesis Submitted to:
Office of the Dean
Faculty of Management
Tribhuvan University

In partial fulfillment of the requirement for the degree of Master of Business Studies (MBS)

Kathmandu, Nepal
August 2010

RECOMMENDATION

This is to certify that the thesis

Submitted by:

UMESH SAPKOTA

Entitled:

RESOURCE MOBILIZATION THROUGH INCOME TAX IN NEPAL

has been prepared as approved by this Department in the prescribed format of the Faculty of Management. This thesis is forwarded for examination.

……………………………………..	........……………..……….………….	……………….……………………
Prof. Dr. Kamal Deep Dhakal	**Prof. Bishweshor Man Shrestha**	**Krishna Prasad Acharya**
(Thesis Supervisor)	**(Head, Research Department)**	**(Asst. Campus Chief)**

……………………..……………..

Romakant Bhattarai

(Thesis Supervisor)

VIVA-VOCE SHEET

We have conducted the viva –voce of the thesis presented

By

UMESH SAPKOTA

Entitled:

RESOURCE MOBILIZATION THROUGH INCOME TAX IN NEPAL

And found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirement for the degree of

Master of Business Studies (MBS)

Viva-Voce Committee

Head, Research Department ……………………………

Member (Thesis Supervisor) ……………………………

Member (Thesis Supervisor) ……………………………

Member (External Expert) ……………………………

DECLARATION

I hereby declare that the work reported in this thesis entitled "**Resource Mobilization through Income Tax in Nepal**" submitted to Office of the Dean, Faculty of Management, Tribhuvan University, is my original work done in the form of partial fulfillment of the requirement for the degree of Master of Business Studies (MBS) under the supervision of **Prof. Dr. Kamal Deep Dhakal** and **Romakant Bhattarai** of Shanker Dev Campus, T.U.

..……….………………………

Umesh Sapkota

T.U. Regd. No.: 7-2-31-532-2003

Campus Roll No. : 569/063

ACKNOWLEDGEMENT

This thesis report has been prepared to fulfill the partial requirements for the degree of masters of Business Studies (MBS) of Tribhuvan University. For this, I would like to acknowledge the effort of office of the Dean, Faculty of Management, T.U., for offering such a great course in our syllables to enhance the quality of management education in country.

For this work, I would like to express my heart-felt gratitude to my thesis supervisor Prof. Dr. Kamal Deep Dhakal and Romakant Bhattarai lecturer of Shanker Dev Campus for their grand encouragement and patience up to accomplishment of report.

Similarly, I would like to pour my sincere words of gratification to my cooperative friend Mr. Binod Dahal, Mr. Rajan K.C., Mr. Purushottam Lamichhane, Mr. Shiba Pathak, Mr. Sashi Bhattarai & Miss Sharmila Parajuli for their kind guidance & encouragement during the thesis preparation phase.

I would like to share my deep down love and indebtness to my loving father Mr. Narayan Pd. Sapkota, Mother Mrs. Bhakta Kumari Sapkota, Sister Ms. Saraswoti Sapkota, brother Mr. Dinesh Sapkota and whole family for their immeasurable support, love and inspirations in every walk of my life.

Last, but not a least I can not forget the help and concerns of all friends, colleagues and relatives for their help and keen concerns in my thesis accomplishment.

Umesh Sapkota

1.1.1.1.1.1 ABBREVIATIONS

CEDA	:	Centre for Economic Development and Administration
CEDECON	:	Central Department of economics
CIAA	:	Commission on Investigation of Abuse Authority
DCs	:	Developed Countries
et al.	:	and others
FDI	:	Foreign Direct Investment
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
GN	:	Government of Nepal
GNI	:	Gross National Income
GNP	:	Gross National Product
IMF	:	International Monetary Fund
IRD	:	Inland Revenue Department
IROs	:	Inland Revenue Offices
KTSC	:	Kathmandu Taxpayers Service Centre
MoF	:	Ministry of Finance
NPC	:	National Planning Commission
NRB	:	Nepal Rastra Bank
PAN	:	Permanent Account Number
PCI	:	Per Capita Income
SAARC	:	South Asian Association for Regional Cooperation
SAFTA	:	South Asian Association for Regional Cooperation
TDS	:	Tax Deduction at Source
VAT	:	Value Added Tax
VDIS	:	Voluntary Disclosure of Income System
WTO	:	World Trade Organization

TABLE OF CONTENTS

LIST OF TABLES

LIST OF FIGURES

CHAPTER - I

INTRODUCTION

1.2. Background of the Study

The main objective of government of any developing country is to improve living standard of people through the development process. In order to achieve this objective every government launches different economic, social, cultural and other development activities. For this, government needs huge amount of financial resources.

Nepal is a land locked country lying between two Asian giants China and India. Both of them are able to enjoy high economic growth in the world. However, Nepal has not been able to reap the benefit of synergic development impact of encouraging growth of its neighbor. Nepal has been adopting the system of mixed economy to achieve its development goals. In spite of its planned efforts for development, overwhelming majority of its people enjoy income below the poverty line

In order to uplift the life standard of people, Nepal has given first priority to economic development through planned efforts and the government has continued the implementation of several reform programs initiated in the past. Resource mobilization is the foundation for economic development of the nation. Since Nepal started its planned development efforts in 1956, the need for mobilization of additional financial resources has been growing in multiple folds.

The government can mobilize both internal and external financial resources to bridge its expenditure. However, the internal resources are more preferable to external one for sustainable economic development. Internal resources can be classified broadly into two groups, tax revenue and non tax revenue. Tax revenue includes direct tax on income and wealth and indirect tax on consumption. Non-tax instruments for revenue collection are government charges, fines, dividend, royalty etc.

Income tax is categorized under direct tax on account of its property. It cannot be shifted backward or forward. Taxes on income may be levied on individual as well as business firms. The former is known as personal income tax and the later is known as corporate income tax.

The Great Britain was the first country that introduced modern income tax in 1799 to collect revenue to finance Napoleonic war with France. In 1862, USA introduced income tax to finance Civil War. In India modern income tax was adopted in 1860. In Nepal income tax was introduced in 1959. Both individuals and companies were taxed in similar way during the earlier period but later on companies were levied with a flat rate and individuals with progressive rates (Poudel, 2002: 5).

First law of Nepal regarding to the income tax is Business Profit and Salaries Tax Act, 1960 then after three income tax acts has been introduced in Nepal. These are Income Tax Act, 1962, Income Tax Act, 1974 and Income Tax Act, 2002. However, Income Tax Act, 2002 is in practice.

Income tax is the third largest source of total tax revenue. It is a tool of achieving minimum social and economic objectives as lay down by the constitution of Nepal. As a poor country, sources of government revenue are very limited. The domestic sources of the government revenue should be increased to escape from the condition of dependency on foreign aids and loans. Income tax may be the best way to increase government revenue internally.

1.2 Statement of the Problem

Economic development is the prime concern of every nation. To fulfill this objective, every nation is accomplishing various activities. However, developing countries are facing serious problems in the process of economic development. Nepal is not exception to this condition.

Deliberate planning process began only after 1957 (2013 B.S) in Nepal. Ten (One three year and other five years) periodic plans have been already completed and Three Year Interim Plan is under operation. To fulfill the planning expenditure and for the process of economic development a lot of capital is needed.

Nepal is one of the developing and agro-based countries in the world. Its gross national income per capita is $472. It is the lowest in the SAARC countries and about 30 percent of the total population lies below poverty line (Economic Survey). This scenario shows the economic condition of Nepal. So, Nepal needs huge amount of capital for economic development. Despite the various measures adopted by the government to boost revenue collection there is still a substantial resource gap between expenditure and revenue. The rate of government expenditure is exceeding the rate of growth in revenue collection, almost every year from the beginning of its development phase. The resource gap in FY 2007/08 was 53727.4 millions (Economic Survey). The sources of bridging the resource gap are internal and external borrowing. The external borrowing has playing important role to fulfill the resource gap. However, the use of external borrowing to fulfill growing government expenditure brings various problems.

The development process of a country will be possible only when the government can collect its own internal revenue. Internal revenue constitute a significant portion on government revenue of the total revenue collected in FY 2007/08, Tax and non-tax revenue account for 79.12 percent and 20.88 percent respectively (Economic Survey). The major portion of government revenue is covered by taxation but the tax composition of Nepal shows that the government revenue is highly dependent on indirect tax. In FY 2007/08, the indirect tax had contributed 72.9 percent of total tax revenue (Economic Survey).

In the context of Nepal's accession to WTO membership, it is a great challenge for the government to adjust tax rates accordingly without reducing present level of revenue collection. Revenue collection from direct tax is far behind low compared to indirect tax. Income tax is the major contributor of direct tax.

As the means of economic growth and social justice, income tax has not succeeded to play significant role in Nepalese tax structure. The direct tax had contributed only 27.1 percent of total tax revenue and income tax had contributed 82.63 percent of direct tax in FY 2007/08 (Economic Survey).

In developing nations, people have greater propensity to evade taxes. They have lesser or no knowledge about income tax and they have to maintain their expenditure from their limited income. Rich people are avoiding taxes by using legal loopholes and taking advantages of an inefficient tax administration.

In Nepal, the coverage of income tax is very narrow and people have low tax paying habit. Tax authorities are inefficient and ineffective in collecting tax and broadening tax base. There are no integrated programs for taxpayer’s education, assistance counseling and guidance. The assessment procedure of income tax is ineffective; including delay in tax assessment not only reduces total revenue, but also brings harassment to the taxpayers (Lamsal, 2005: 8).

The coverage of income tax is very narrow in Nepal. Agriculture income is exempted from income tax. Remuneration or salary income is taxed more heavily than the capital income. Retirement amount received by Nepalese people being retired from the service of foreign country is also exempted from income tax. Exemption of these sources provides loopholes for the evasion and complicate to the tax administration. Exclusion of agricultural income from tax net alone, cuts out about half of the GDP. The contribution of direct tax, especially of income tax is considerably low in Nepal compared to other developed countries. Administrative inefficiency, confusing definitions, corrupt bureaucracy, widespread tax evasion etc. are the reason for this state of affairs.

One of the most important tools for shortening resource gap in developing countries, efficient and effective utilization of internal resources has not been practically prioritized yet. And the potentiality of income Tax to mobilize additional financial resources has not yet been recognized properly. In this juncture, it is necessary to study about the role of income tax in resource mobilization. In this study, we have tried to find out the answer of the following questions:

1. What is the role of income tax in resource mobilization in Nepal?
2. What is the legal aspect of income tax in Nepal?
3. What is the administrative aspect of income tax in Nepal?
4. What is the future trend of income tax in Nepal?

1.3 Objectives of the Study

The general objective of the study is to examine the role of income tax in resource mobilization. The specific objectives of the study are:

1. To examine the role of income tax in resource mobilization in Nepal.
2. To compute elasticity and buoyancy of income tax in Nepal during the period of FY 1990/91 to FY 2007/08.
3. To analyze the legal aspect of income tax in Nepal.
4. To project future trend of income tax in Nepal.

1.4 Significance of the Study

Election of constitution assembly has completed after the successful aftermath of the Historic People's Movement and the commencement of the peace process. Now, the government has to spend huge resources for reconstruction, rehabilitation and relief to make modern, prosperous and just Nepal and to address the ambitious expectation of the people. For this purpose, government needs a huge amount of resources. In this regard, income tax can be a major source of government revenue.

Taxation is a powerful instrument for mobilizing the internal resources of any country whether it is undeveloped, underdeveloped, or developed one. In developed countries, taxation contributes more than 3/4th to their total national revenue in which share of income tax is prominent. But case in developing countries is different; income tax has not been contributing the total revenue of country to the extent as it does in developed ones. In developing where financial resource gap is increasing seriously leading the economy to the state of external dependency, taxation only becomes sustainable and non-inflationary internal remedy to overcome this problem of financial resources gap and deficit financing. Because of poor internal resource mobilization capability, Nepal has been facing a serious resources gap for many years and this trend seems to be continued in future if suitable measures are not taken in time properly. For the remedy of external dependency and growing resource gap problem, internal revenue base should be strengthened through the mobilization additional financial resources internally specially through income taxation.

In the revenue structure of Nepal, the share of tax revenue and non-tax revenue were 81.09% and 18.09% respectively in FY 2007/08 which was 77.2% and 22.8 in FY 2004/05. Income tax occupies largest share in the direct tax and that the percentage share of this component in the FY 1990/91 was 54.97% amounting to Rs. 746.2 million. The contribution of income tax to direct tax was highest i.e. 90.10% in FY 2000/01 and minimum i.e. 53.60% in FY 1991/92. Its contribution was reached to 82.63% of direct tax in FY 2007/08.

So, a study on the present and potential role of income tax to mobilize additional financial resources is must. This study will be concentrated on mobilization of additional financial resources through proper management of requirement. This study will be an attempt to explore potential rooms for additional resource mobilization through internal sources with special focus on income tax.

1.5 Limitation of the Study

The limitations of the study are:

1. The study has been fully based on secondary data.
2. This study has covered only the period of 18 years (FY1990/91to FY 2007/08).
3. Only Sahota method has been employed to separate the effects of discretionary changes to total tax revenue.
4. Comparisons have been done with only some major developed and developing countries.

1.6 Organization of the Study

This study is divided in to five Chapters they are:

Chapter - I Introduction

The first chapter deals with background, statement of problem, focus of the study, objective of study, research methodology limitation of study and chapter scheme.

Chapter - II Conceptual Framework and Littérateur Review

The second chapter deals the review of related literatures and available studies, written and prepared by experts and researcher.

Chapter - III Research Methodology

The third chapter "Research Methodology" present the methodology used in this study. If deals with research design, nature and sources of data, collection of data, data processing and method of data analysis.

Chapter IV Presentation and Analysis of Data

The fourth chapter fulfills the objectives of the study by presenting the data and analyzing them with the helps of various accounting and statistical tools and techniques followed by methodology.

Chapter - V Summary, Conclusion and Recommendation

The fifth chapter summarizes the whole study Moreover to draws the summary conclusion and forwards the recommendation for the improvement of effective Tax collection system and to avoid the difficulties in tax collection system.

CHAPTER - II
CONCEPTUAL FRAMEWORK AND LITERATURE REVIEW

2.1 Concept of Tax

2.1.1 Theoretical Framework

Tax is a compulsory contribution to government made without reference to a particular benefit received by the taxpayer. These characteristics distinguish it from a price, which is a voluntary payment for goods and services. This is politically and economically important. The absence of a perceived direct benefit causes taxation to be regarded as burdensome in a way that prices are not, even by persons who recognize that the state provides benefits for the community and who approve its policies. Generally, the amount of tax paid by a person will not affect the benefits that he receives individually, and it will be too small to have an appreciable effect on total benefit. Hence, an individual could rationally, selfishly, advocate reducing his own taxes even though he wished government services to be maintained or expanded (Goode, 1986: 75).

The primary purpose of taxation is to divert control of economic resources from taxpayers to the state or its own use or transfer to others. Taxation restrains total spending by households and enterprises but influences the allocation of economic resources, recognises social costs that are not reflected in market prices, and affects the distribution of income and wealth.

Taxes are usually paid in money and represented a forced surrender of purchasing power. Exceptionally, however they are collected in kind as were agricultural taxes in Japan and Korea immediately after 2nd World War and as are taxes on oil companies in a number of producing countries.

According to Plehn, Taxes are genera; contribution of wealth levied upon persons natural or corporate to defray expenses incurred in conferring common benefit upon the residents of the status (Dhakal, 1998:2).

According to Bastable, “A tax is compulsory contribution of wealth of a person or body of persons for the service of public power” (Dhakal, 1998).

According to Classical Economist Dalton, “A tax is compulsory contribution imposed by public authority irrespective of the exact amount of service rendered to the taxpayer in return and not imposed a penalty for any legal offence (Dhakal,1998).

2.1.2 Origin of Taxation

The history of taxation dates back to antiquity. In early days taxes were not collected in monetary terms but were collected by tribal rules, community heads, etc for communal services and at the time of emergencies (Dulal, 2004: 22). In Hindu tax system, tax was levied on the basis of welfare of the people and people were eager to pay tax because not to pay tax was taken as a great sin. According to Hindus’ Holy Scripture, Vedas, the duty of king was to serve and secure people, maintain peace and carry out social works. In order to perform all those activities, the king used to collect crops and cattle from farmers and gold, silver and copper from traders. These ancient forms of taxation were expanded from time to time under the influence of various economical, political and ethical forces.

In the early Roman society, the citizens had to pay taxes even for the pulling rights. Ancient Athens used to derive its revenue from taxes like customs, sales, and pole tax on aliens and slaves. One who was taxed and failed to pay was guilty of a capital offence. After the end of Punic war in 146 B.C., they were relieved from the poll tax. They started to levy tax on the people of the captured areas instead of there citizens. At the time of Julius Ceaser, 1% sales tax was imposed to the people and he was the first ruler who started to collect taxes through governmental institutions.

Kautilya's '*Arthashastra*' of the fourth century B.C. has classified the tax receipt into three types.

1. Income earned through taxes on goods produced within the country.
2. Income earned through taxes on the capital.
3. Income earned through taxes on imports and exports.

Land revenue was an important source of taxation in ancient India. Kautilya mentioned, "The tax system should be such as not prove a great burden on the public (Praja), the king should act like the bee which collects economic thought was guided by social welfare concept. He suggested heavy taxation for luxuries and other articles, which were not in favor of the public welfare.

Classical writers always favored minimum interference of the government and emphasized on the least taxation. According to the classicists' taxation is the common debt to citizens, a kind of compensation and the price of the advantages which society confers upon them. Thus tax is a quota each citizen has to pay towards cost of public services. Antonio De Viti De Macro has described the misconception of classical economists in the following words:
Taxes were regarded as a sort of hail that destroys part of crop. Therefore, the use to which tax was put after its payment was not studied at all. The consequence was that taxes were regarded, without further ado, as being accompanied by a contraction in the supply of available goods, with all the mistaken consequences of this mistaken premise (Timalsina, 2007: 41).

Until the Great Depression of 1930s, many economists regarded neutrality of tax system as ultimate goal. After the Keynesian revolution, it is generally accepted that taxation is no longer to look upon as a means of collecting the revenue for financing the government expenditure but as one of the primary weapons in the government armory for ensuring general economic stability.

As a fiscal instrument, taxation is used in mitigating the inequality in income and wealth. It is also used to check inflation to provide incentives for production, saving and investment; to influence balance of payments and the structure of economy and to achieve long term economic growth. Thus, Keynes using taxation as a fiscal instrument gave a new direction to its role.

After the great depression of 1930s the function of government has been increased considerably. For smooth functioning, government has got various sources of revenue. Tax is an important instrument of government to mobilize the resources to achieve the objectives. Generally, tax is defined as compulsory payment to government irrespective to the benefits. There are various sector separated for taxation, if the field is income of the people then it is called income tax.

2.1.3 Definition of Tax

Many economist and scholars have expressed their views in regarding to the tax. Some of the definitions on tax given by some scholars are as follows (Gautam, 2006: 32).

According to Dalton "A tax is a compulsory contribution imposed by public authority irrespective of the exact amount of services recorded to tax payer in return and not imposed as penalty for any legal offence."

According to Prof. Seligman "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 above definitions, it is clear that tax is compulsory levy imposed to the person by the government according to the law of the country. The person whom tax is imposed must pay taxes otherwise the law punishes him/her. The government does not provide any corresponding benefit to the taxpayers for the amount of tax.

2.1.4 Classification of Tax

For the first time, Hicks (1954) preferred to classify taxes as on income and consumption. As per international classification taxes can be viewed as (Dahal, Class note):

a. Taxes on income, profits and capital gains (Direct tax)
b. Tax on property
c. Tax on domestic goods and services
d. Tax on international trade and transactions.

In modern times, taxes are broadly classified into two types. They are: direct and indirect tax. The direct- indirect classification is essentially an administrative distinction. The origin of technical classification is unknown.

2.1.4.1 Direct 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. Taxpayer cannot shift the burden of tax to other persons. Examples of direct tax are: income tax, property tax, interest tax, gift tax etc.

2.1.4.2 Indirect Tax

An indirect tax is a tax imposed on one person but partly or wholly paid by another. Indirect tax is transferable. The person paying the tax and the person bearing the tax is different. Taxpayer can shift the burden of tax to other persons. People pay tax when they received or consumed goods and services. VAT, sales tax, entertainment tax, hotel tax, import and export duties, excise duty etc. are the examples of indirect tax.

2.2 Concept of Income Tax

2.2.1 Income

Income means a "person's income from any employment, business or investment and the total of that income as calculated in accordance with this act" (ITA, 2058). It includes all sort of income received for the provision of labour or capital or both of whatever form or nature in the taxable income.

Income as the economic gain received by the person during the particular period, is most, satisfactory defined by Henery Simons as the algebraic sum of items (Due and Friedlander, 1994: 256):

A. The person's consumption during the period, and
B. The increase in the individual's personal wealth during the period.

Symbolically, $Y=C+\triangle W$

Where, Y = income,

C = consumption

$\triangle$W = change in wealth

2.2.2 Income Tax

Income tax is a personal tax imposed on the net income of individuals and corporation. In most of the countries especially the USA, Canada and other countries, income tax is defined in term of the 'flow of wealth' of receipt in money or goods form the taxpayers during the period. Inflow of wealth method, taxation is defined on a realization rather than an accrual basis, and this applies only when a transaction occurs between other persons and taxpayers (Gautam, 2006: 34).

According to the tax economists "An income tax is a levy imposes upon the tax of individuals after the exemption limit. Income tax is direct tax based on the total income of the taxpayer from all the sources and is graduated on a special system of exemption." It is very important source of revenue of each country.

2.2.3 Reasons in Favour of Income Tax

The reasons in favour of income tax are given below (Timalsina, 2007: 47):

i) Income tax is associated with the ability to pay principle of taxation. It is due to this, the poor can be let out from this sort of taxation and appropriate progressivity can be made among the taxpayers.

ii) Although, theoretically, it can distort the work-leisure and saving-consumption choices and other decisions, the evidence suffers that unless extremely high rates are used the income tax creates relatively little substitution of leisure for work effort or other alterations of behavior. So, it is relatively neutral with regard to allocation efficiency.

iii) It serves as an instrument for reducing the inequality of income distribution.

iv) By adjusting the tax burden the government can, in effect, influence the saving ratio throughout the economy and thus the growth rate. Therefore, it also works as a strong build-in-stabilizer.

2.2.4 Reasons Against Income Tax

In spite of all those merits, some weak points are also identified about income taxation they are given below:

i) Tax burden is realized by income tax payers but not by consumption taxpayers. So, there is a tendency of tax evasion relatively higher in former case than that of later.

ii) Consumption tax is preferable to saver and income tax to consumer. Therefore, it hampers saving attitude of taxpayers.

iii) Income is not proper index of taxation due to monetary transfer, self-produced goods etc.

iv) Income tax is said to involve double taxation. Anyone who pays income tax upon his net income has also to pay income tax for interest income. But this sort of double taxation is lacking in consumption taxes.

The debate between commodity taxation and income taxation with their merits and demerits in their own field is never ending. But the comparative study of the tax structure of low, middle and high-income countries show that commodity tax revenue has significant share in total tax revenue in most of the developing countries and least in high-income countries with some exceptions, and reverse is the case about direct tax.

2.2.5 Condition for the Success of Income Tax

The income tax functions successfully if the following conditions were fulfilled (Goode, 1986: 102).

- Existence of pre-dominantly money income.
- A standard of living.
- Prevalence of honest and reliable accounting.
- A large degree of voluntary compliance on the part of taxpayer.
- A political system not dominated by wealthy group acting in their self-interest.
- Honest and efficient administrative structure.

2.2.6 Objective of Income Tax

The objectives of taxation in developing countries can be classified into two categories namely growth objectives and stabilization objectives which are discussed below (Timalsina, 2007: 48-50).

1) The Growth Objectives

In developing countries, it is one of the major objectives for economic development. There must be adequate capital accumulation to finance development projects and to accelerate the pace of economic growth. Economic growth is not possible if the rate of growth of population exceeds the rate of national income. In order to increase per capita income, saving and investment with the help of appropriate tax policy can increase the rate of national income. The experiences of developing countries indicate that early introduction of direct tax will be great value to the people who are living on subsistence level low literacy rate.

In developing countries, tax policy should discourage the consumption of unnecessary goods and encourage the promotion of saving income ratio. According to James Cut the role of tax policy in promoting economic growth, thus, emerges as one of the restraining increase in consumption i.e. tax policy must seek to increase the saving income ratio as national income increase.

In the developing countries, where foreign concerns are not operating at the early stage of economic development the potentiality of corporate income taxation becomes low. So, the development of corporate sector, business sector in developing counties should provide special tax concession such as tax holiday and investment credit needed for the industrial development.

2) Stabilization Objectives

In the developing economy, problem of inflation is depended on the type of expenditure incurred by the public sector on goods and big industries and socio-economic overhead capital. In this regard, taxation can be helpful in minimizing the inflationary trend. From the economic viewpoint, they should lead to growth with stability and be consistent with national economic policies. Inflation of certain degree is helpful for increasing economic growth but it may have various other adverse effects.

In developing countries, where inflation is acute, the prices of the traditional commodities like food, raw materials etc which are used both for domestic as well as export purpose rise very much thus affecting domestic and export markets. The fall in export earnings adversely affect the process of economic growth in these countries. As a result there will be no development in the country’s economic situation.

In UDCs, taxation of income is not advisable to check steep inflation because the potentiality of checking inflation through income tax is limited since the coverage is not wide and the propensity to consume is higher among such a section of people, which is not out of the periphery of income tax.

In the history of 45 years of income tax, it has done a lot in the sector of taxation but it requires further improvement. However, income tax has become an important source of revenue. The income tax is essentially a unitary tax under which all of its gross income and all deductions are combined to arrive at total taxable income subjective to a single table of rates.

At present time income tax in Nepal is ranked third in the order of significant. First is VAT. It is shown by the tax structure of different countries that as the country goes on developing the contribution of income tax in total tax structure goes on expanding. It is clear from the facts that in developed countries like U.S.A., Japan, U.K., France etc. the income tax is the main source of government revenue. Mostly, the developing nations of the world rely on indirect taxes to meet the growing volume of government expenditure. In this connection Nepal is not an exception because in under developed countries the economy is not well integrated.

The developed countries of the world especially industrialized nations of the west channel collect required revenue by tapping direct taxes. In fact the revenue from direct taxes occupies a prominent place in total tax structure and total revenue of these countries, nevertheless, in their early phases of economic development they had to rely mostly on indirect taxes.

To a developing country, highly dependency on foreign aids and loans is not good. So, it would be better to reduce the foreign source of financing for development. The external financing should play only supplementary role in the national economy. But it is pity to say that the internal financing position of

Nepal is very poor. It is unrealistic to expect more tax from poor Nepalese people. As regarding Nepalese economy, external source of financing has been the backbone of all the plans so far framed and implemented since 1956. In future, if the external sources decreases or stop, Nepalese economy will face disastrous consequences. To avoid such circumstances, Nepal should mobilize her own domestic financial resources adequately.

Among domestic financial resources taxation seems to be highly justified. Taxation is viewed as a powerful tool in the hand of government for the purpose of internal financial resource mobilization. Economic development depends, far more than is commonly recognized, on a carefully thought-out and well-organized tax structure.

Upward adjustment in the tax rates or even introduction of new taxes in itself does not ensure desirable increase in revenue. The ability of tax payers, tax consciousness, quality of the tax personal, efficient tax administration, enforceable tax law and policy, scientific and timely tax assessment produce etc are the factors that directly affect the collection of internal revenue.

Taxation comprises direct taxes and indirect taxes. Income tax is a part of direct tax, which is imposed upon the net income of an individual and corporation, derives from business, profession, investment, rent, remuneration and other sources. Income tax is considered to be the vital tool for the government to accumulate adequate revenue and to achieve socio-economic objectives. Its progressive feature makes it an effective instrument for reducing distributional inequalities in income and wealth. It confirms must closely to the “ability-to-pay” principle of taxation. It ensures equal taxation of persons with equal ability and increasing taxation of person with higher income.

Income tax is basically charged for two purposes namely collecting revenue to meet expenses for people’s welfare activities and to create egalitarian community by minimizing the economic gap between haves and haves not.

Income tax is based on the principle of certainty in the sense that the government has already acquired the acknowledgement about income tax and taxpayers have also already known the amount of tax that will be levied to them. It also follows the cannon of economy. It increases the civil consciousness. It is helpful for generating the concept of social responsibility towards the nation and keeps the people vigilant to see the public money may not be misused (Saxena, 1986: 2).

2.3 Review of Historical Background of Income Tax

2.3.1 Income Tax in International Context

Credit for the establishment of the first successful income tax in the world is given to Great Britain where it was first introduced in 1799 in order to finance the wars with France. The main reason for the introduction of this tax was that it was preferable as a substitute for the customs and excise duties in raising revenue. It remained more or less a temporary tax until 1860 when it got accepted as a permanent tax (Timalsina, 2007: 54).

In USA, the first income tax was introduced in 1862 to generate revenue to finance Civil war expenditure. The federal corporation income tax was introduced in 1909. In Japan, income tax was introduced in 1887. It was a general individual income tax and extended to the corporate income in 1899. In German, income tax became an effective instrument since the Persian Reform of 1891 though income tax had been levied in different forms before the unification of Germany in 1871. In India, income tax in its modern form was adopted in 1860, several experiments were made from 1860-1886 and finally the systematic income tax legislation was enacted in 1886.Income tax in Switzerland in 1840, Austria-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, South Korea 1948 and in Nepal 1959 (Khadka, 2004).

After the adaptation of income tax, many countries had undergone considerable changes. Initially, income tax was limited to the income generated within the country but with the globalization taxation of worldwide income came into vogue. There have been different practices regarding the taxation of individuals and companies. Some countries initiated with the taxation of individual and brought companies in to the tax net after a few years of the implementation of income tax. But in some countries both the individual and companies were taxed in the similar way but later on they were taxed in different ways such as companies with a flat rate and individuals with progressive rates.

Until the mid 80s, income tax was used as an effective instrument for the redistribution of income. But the intended objective could not be achieved in real life. Some stress progressive rate structure discouraged to work, invest and save more and complicated the tax administration.

Income tax has been an important element of the modern tax system. All sorts of countries have adopted this tax as an important instrument to generate revenue required to finance state activities and taxable capacity of the taxpayer.

2.3.2 Taxation in Nepal

At the ancient time, tax system of Nepal was based on Vedas, Smritis and Purans. Directives propounded by Manu, Yagya, Balak, Chanakya etc. had guided the taxation system. At that time, the principle of collection tax form the people was imposition of tax without harming the activities of people (Gautam, 2006: 35).

During the period of the Lichhabis, the main sources of government revenue were tax. There was 'Tri-Karas' system such as Bhaga (Tax on agriculture), Bhoga (tax on livestock) and Kara (tax on trade). Amsubarma, the popular king of that period imposed water tax and religious monument repair tax. Tax was payable in accordance to taxpayers ability. At that time, a tax on income of the farmers from agriculture was imposed at the rate 1/6, 1/8 and 1/12 shares of crop production depending on the land quality (Kandel, 2004: 11).

In Malla period, there were taxes related to land, trading, etc. Jayasthiti Malla, imposed taxes on cremation (Daha Sanskar) and caste purity.

In Shah Period, there was continuation of the tax system of Malla period. There were different types of taxes like Walak (tax on each family), Gaddimudark, Chumawan, and Goddhawk etc.

Prithivinarayn Shah introduced Pota tax in 1772. This system of tax was based on flat system and limited on small Birta owners. In the period of Surendra Bikram Shah, excise was introduced in Nepal.

During Rana period, the main source of government revenue was land taxes, custom duties and excise. Sanads and Sawals were the laws guiding the tax system. Lagati (based on cost record) and Hasawali (not based on record) were two types of revenues. Jamna Nasodnu, Kachha Nachhodnu (Not to get total and not to leave even a single paisa) was the principle of revenue collection in Rana period (Gautam, 2006: 36).

After the dawn of democracy, the first budget, which was introduced in 2008 B.C. stated about the introduction of income tax in Nepal. But it was actually started from 1960 in the form of Business profit and Remuneration tax.

2.3.3 Legal Aspect of Income Tax

Although there was tax system in Nepal in ancient time also, the concept of income tax was brought only by the first budget. The budget introduced in 1951 A.D. stated about the introduction of income tax system in Nepal. However, it was actually introduced in 1960 when the Finance Act, 1959 and Business profit and Remuneration Tax Act, 1960 were enacted (Kandel, 2004: 16).

2.3.3.1 Business Profit and Remuneration Act, 1960 (2017 B.S.)

The Business Profits and Remuneration Tax Act, 1960 (2017 B.S.) had 22 sections. The salient features of this tax act were as follows (Timalsina, 2007: 58-59):

1. Only remuneration and business profits were subject to tax.
2. Deductions were not specified for the purposes of calculating the taxable income.
3. Tax on remuneration was to be deducted at source.
4. The basis for calculating the tax liability for remuneration was the income of the current year and for business profits it was the profit of the preceding fiscal year.
5. Salary of any diplomatic representative, foreign citizens, dividend or shareholders, profits to be spend on religious or public welfare activity, profits of local autonomous organization, allowances granted by GN to Ministers, Assistant Ministers and other government employee, crop from own land, money drawn from provident or saving fund were exempted from tax.
6. The tax officer was empowered to assess tax on best judgment estimate where tax return was not filed or a false return was filed.
7. In case of default, fines up to Rs. 5000 were prescribed.
8. The first court of appeal was local "Bada Hakim" or Magistrate. Therefore, appeal could be lodged at revenue court. Every appeal was to be accompanied by security deposit or guarantee for the amount of tax payable.
9. There was provision of reward to the informants who give information about the tax evasion.

Profits from large industries were granted a rebate of 25 percent and profits from small industries were granted a rebate of 50 percent. In the beginning, the government servants were the main taxpayers. The taxation laws were not enforced effectively.

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

The experience of three years indicated that the Business Profits and Remuneration Tax Act are rather narrow as well as vaguer. This was replaced by Income Tax Act, 1962 (2019 B.S.). It consisted 29 sections in it. The additional features of the Income Tax Act, 1962 were as follows (Paudel, 2002: 27).

1. Income was defined as all kinds of income including income from business, salaries, any profession, rents from houses or lands, investments, agriculture, insurance or any other sources.
2. The personal as well as residential status of the taxpayer for tax purposes was defined.
3. The procedures for assessment and collection of income tax were made for the allowable deductions. Methods were also specified for the calculation of income.
4. The basis was specified for assessing tax on the best judgment estimated of the tax officer.
5. The Act granted power to constitute net income assessment committee.
6. Provision was made for payment of tax in instalment as well as advance payment of tax.
7. Provision was made for reassessment of tax as well as rectification for any arithmetical errors.
8. Provision was made for the exemption of income tax for new industries for a period not exceeding 10 years.
9. The industry recommended by the Department of Industries must be exempted from income tax.
10. A regular taxpayer who suffered from a loss due to some reason, the loss for past two years may be deducted from his income of the year for which the tax had been assessed.
11. Agricultural income was brought under the scope of income tax for the first time. Which considered one-fourth of the total income from agriculture were the net earnings.

The Income Tax Act, 1962 as amended in 1972 remained low till 1974. However, in order to keep the law in tune with the changes in the socio-economic environmental setting of the country, the need was felt for consolidating and amending the existing law.

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

The Income Tax, Act 1974, as amend in 1974 (2031 B.S.) had the 66 sections. Its basic framework had been derived from the Income Tax Act, 1962. It has retained or amended certain provisions of the old act and had added certain new provisions. Some of the salient points of this Act were as follows (Timilsina, 2007: 61-62):

a. It had clarified certain definitions, especially relating to tax, assessment of tax, and year of income, personal status of the taxpayer, firms, company and non-residential taxpayers.
b. Five sources of income (agriculture; industry; trade, profession, and remuneration; house and land rent and others) had been specified. Methods of computing net income from each source for various types of taxpayers including the deductions allowance had been specified.
c. It had made obligatory for the taxpayers to register their industries, trade, profession or occupation in the tax office. Any change should also be notified to the tax authorities.
d. It was made provision for self-assessment of tax for the first time in Nepal.
e. Deduction was allowed for life insurance premium.
f. It had made provision of calculating net earning from the total income of different sources.
g. Taxpayers were required to keep account and record for their sources of income and preserve those records for a period of six year.
h. Provision had been made for reassessment on additional tax assessment.

i. Procedure for assessment, collection, payment and refund of tax had been streamlined. Powers of search and arrest had been specified. Penalties of various forms had also been specified.
j. This Act became retroactively applicable for assessments of tax yet to be made.
k. Exemption from income tax was widely and clearly defined.

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

Income Tax Act, 2002 is implemented from 19/12/2058 B.S. This Act replaced the Income Tax Act, 1974 and other Act related to income tax. The Act is quite advance that has ever introduced in Nepal. This Act has 24 chapters and 143 sections.

The major objectives related to Income Tax Act, 2002 are as follows:

- To bring all the income generating activities within tax net.
- To increase the base of the taxation.
- To make income tax related provisions clear and transparent.
- To minimize the tax avoidance and evasion.
- To make the tax system compatible to modern economy
- To make the system based accounting.
- To separate administrative and judicial responsibilities etc.

There are various additional provisions in the new Act are (www.ird.gov.np):

1. Income Tax Act 1974 had classified income tax into five headings where as this act divides only into three headings. They are income from business, employment and investment.
2. When Income Tax Act 1974 was in practice, there were several exemptions and deductions provided by the Act and other related acts. But now, there are no more exemptions and deductions except the ones provided for by the Act.

3. Regarding to this new Act, income is defined as “a person’s income from any employment, business or in accordance with this act.” It includes all kinds of income received for the provision of labour or capital or both in whatever form or nature in the taxable income.
4. The act has given the option for husband and wife as a separate natural individual until they don’t accept as a couple.
5. A resident person may claim a foreign tax credit for any income year for any foreign income tax paid by the person to the extent to which it is paid with respect to the person’s assessable income for that year.
6. There is a provision of functional division of work among tax officers. The division is to be made under the direction of GN and other tax officers.
7. The penalties are divided into two parts. The tax officer can levy only fines and interest and the court can levy penalties and imprisonment.
8. The Act has determined the rate of income tax itself for the first time, which used to be determined by the Finance Act in the previous year.
9. There are special provisions of deductions related to overhead costs while calculating a person’s income from any business or investment.
10. The governmental allowances to widows, elder citizens or disabled individuals; gifts, bequest, inheritance; scholarship; income of foreign officials government bodies and non- profit making organizations have been exempted from the income tax net.
11. A person has defined as a resident whose place of habitat is in Nepal and who presents in Nepal at any time or who presents Nepal for 183 days or more within the income year or who is employee of GN posted abroad during the income year.
12. The income of an approved retirement fund is free from tax. But retirement payments in the hands of employees are taxable.
13. According to this Act, a company is liable to tax separately from its shareholders. The bonus, share, loans and advances to directors and

shareholders distribution made on liquidation etc. are also brought under the tax net in order to plug loopholes for avoidance.

14. Capital gains are taxed under this Act for the first time (after four decades of the introductions of income tax). In case of business capital gains, gains on the disposition of business property are taxed as an ordinary income and in case of non-business capital gains; only the gains from the causal sales of real property and securities are subject to capital gains tax at a flat rate of 10 percent. There is provision for adjusting net loss during the FY.
15. The Act is based on the global income tax principle and has brought all sources of income into the tax net and has treated in an equal manner. This Act had abandoned the itemized system of deduction and expenses one taken into account or a global manner not on a line-by-line basis.
16. The Act has adopted a pooled system of depreciation in which assets are broadly classified into five categories. The depreciation rates are 5, 25 20, 15 percent respectively for first four which are based on diminishing balance method of depreciation and for last one the rate is based on straight line method.
17. The Act has introduced the concept of medical tax credit under which resident individuals may claim at a medical credit of 15 percent of the amount of approved medical costs.
18. Presumptive tax is limited to small taxpayers whose annual net income is up to Rs.100000 or annual turnover is up to Rs. One million and subject to flat annual taxes.
19. This Act has introduced the concept of administrative review to correct the administrative mistakes. The Inland Revenue Department (IRD) should give its decision within the given time limit, the taxpayers can appeal to Revenue Tribunal.
20. This Act has introduced the concept of administrative review to correct the administrative mistakes within the period of 90 days.
21. According to this Act the IRD is responsible for the implementation and administration of this Act.

2.3.4 Definition of Some Terms Related to Tax and Income Tax

Before proceeding ahead, the basic terms used in Income Tax Act should be defined clearly. It is important to have through understanding of the various terms used in the enactment before embarking on the detail study of any act. The important terms used in the act have been defined under section two of the Income Tax Act, 2002. Some special terms used in this study are as follows:

a) Assessment

Assessment is the process of ascertaining the tax liability. It is the process and art of checking the document in which the details of calculation of income tax is recorded.

b) Income Year (Section 2 Jha)

Income year means, for every person, the period from the start of July to the end of June when the assessed earns the income ITA, 2002 has regarded Nepalese fiscal year as an income year.

c) Income (Section 2 Ja)

Income means a "person's income from any employment, business or investment and the total of that income as calculated in accordance with this Act". It includes all sorts of income received for the provision of labour or capital or both of whatever form or nature in the taxable income.

d) Company (Section 2 Da)

Company means a company established under the company laws for the time being in force. For tax purpose, a company means any corporate body or unincorporated association, committee, institution, society or group of persons or proprietorship firm whether or not registered as a trust. According to law, the word company also includes a firm registered under partnership Act, 1964 or not registered having 20 or more partners, a retirement fund, a cooperative, a unit trust or a joint venture, a foreign company and any foreign institution specified by Director general as company.

e) Business (Section 2 Ka. Ja)

Business means an industry, a trade, a profession, or the likely isolated transaction with a business character and includes a past, present, or prospective business. However, the term does not include employment.

f) Exempt Organization (Section 2 Dha)

Exempt organization means any entity that should not pay tax legally. Organizations that are of not for profit earning are provided such facilities ITA, 2002 has indicated various entities as tax-exempt organization.

g) Individual (Section 2 Wa)

Individual means a natural person and a proprietorship firm whether registered or unregistered owned by the person, if any and a couple making an election as single natural person under section 50.

h) Entity (Section 2 Bha)

An entity is an organization established under the law whether profitable or non-profitable. For the purpose of ITA, 2002, it includes a partnership, trust, or company, or Village Development Committee, District Development Committee, Municipality, Government etc.

i) Special Industry

Special industry is a manufacturing industry as categorized in Section 3 of the Industrial Enterprise Act, 1992 other than liquor and tobacco.

j) Business Exemption and Concession

Allowable deduction means expenses pertaining to business or investment, which have been described in the Act being allowable while computing Income from business or investment.

l) Assessable Income

Assessable income means income of a resident person from the employment, business or investment irrespective of the source of the income and income of a non-resident person with source in Nepal.

m) Adjusted Taxable Income

Taxable income of a person without deduction of pollution control cost,, research and development cost and donation.

n) Assesses (Tax Payers)

A taxpayer means a person (an individual or an entity) whom the tax is imposed on and realized from as per Income Tax Act, 2002.

o) Self-assessment

It is the assessment done by the assesses himself at the time of submission of income.

p) Tax Planning

Tax planning is avoiding tax by availing of the various relief and concessions available in the law.

q) Tax Evasion

Tax evasion is avoiding tax by adopting dishonest means.

r) Tax Management

Tax management is the maintenance of records and documents, filling of tax returns in time and performing tax related duties efficiently.

s) Presumptive Taxation

Presumptive Taxation means a system of taxation under which income tax is levied on average income in place of actual income.

t) Resident (Section 2 Ka, Nga)

For the purpose of taxation, a taxpayer is divided into resident and non-resident. In case of individual, resident person includes an individual whose normal place of abode is Nepal. It also includes the person who is present in Nepal at any time during the income year or who is present in Nepal for more than 182 days in any period of 365 consecutive days of which 183 days fall within the income year. According to the Act, a resident is also an employee or an official of His Majesty's Government posted abroad at any time during the income year. In case of trust, it is resident if it is established in Nepal or it has a trustee that is a resident person for the income year. Accordingly, an entity controlled directly or through one or more interposed entities by a person or persons one of whom is a resident person for the income year is also taken as resident. A company and local government bodies in Nepal are resident if they are incorporated or formed under the laws of Nepal or they have their effective management in Nepal during income year. In contrast to resident, non-resident person means a person who is not a resident of Nepal.

2.3.5 Income Tax Administration in Nepal

In the absence of diligent execution of taxes, goals of tax policy are difficult to attain. Ineffective enforcement of existing taxes may lead to public irritation and ill feeling and may defeat even its basic purposes to impose. Prof. Colbert has rightly observed that the art of taxation consists in so plucking the goose as to obtain the largest amount of feathers with the least possible amount of hissing. For this to achieve in practice, what is required is the diligent execution of taxes. But in developing countries, administrative tax machinery are mostly inexperienced and tax payers are usually unfamiliar with the existing tax-laws and even maintenance of proper records of their accounts are not in common practice. As a result, effectiveness of tax administration is highly constrained (Nepal, 2002: 259).

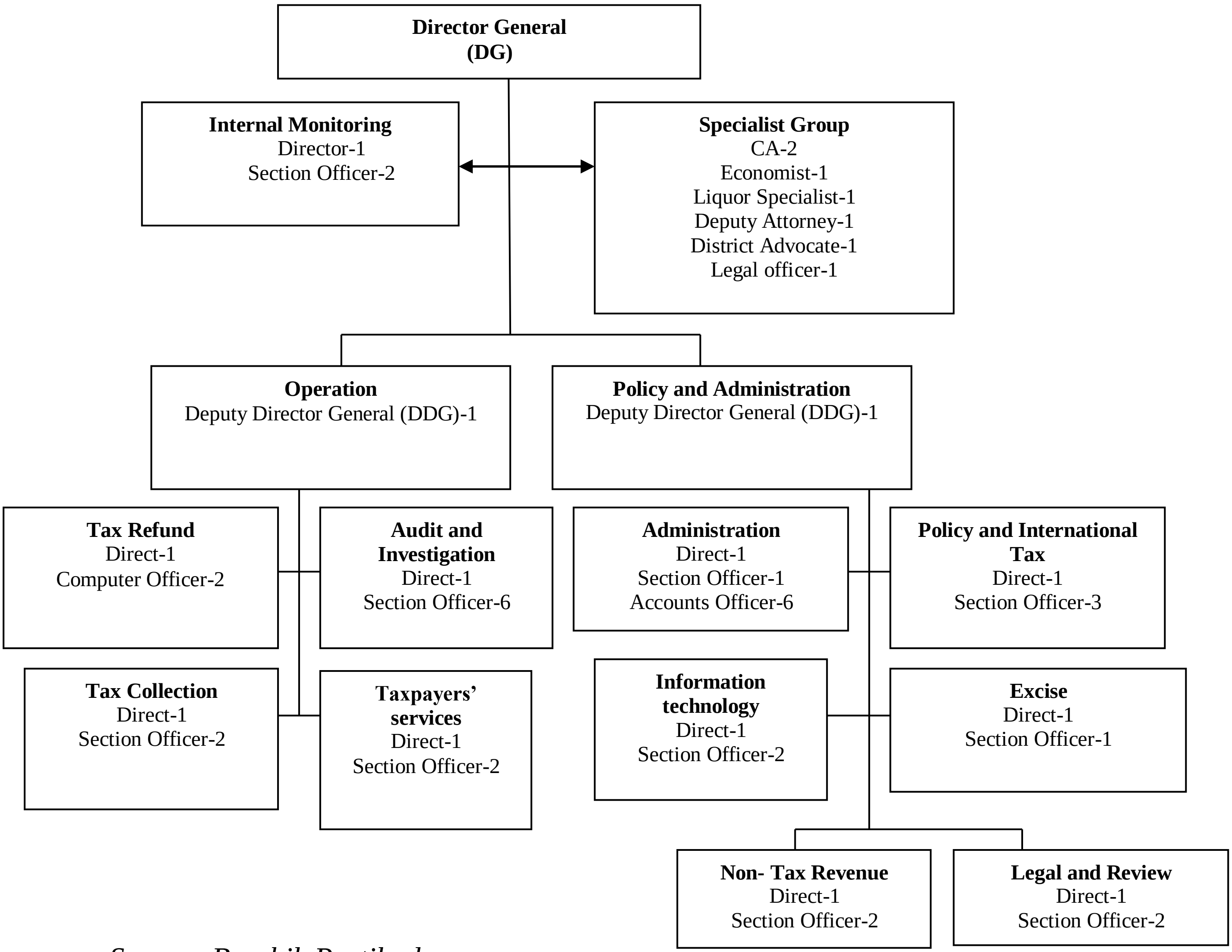
Ministry of finance is the apex of the tax administration in Nepal. The Revenue Division of the ministry is responsible for formulating tax policy and setting up the appropriate tax administration to implement the tax policy. Tax Directorate set up in 1959 is the first organized income tax administration of Nepal. In 1961/62, the Tax Directorate was named Internal Revenue Department and in 1963/64 the department was converted into the Department of Taxation. In the mid April 2001, the Department of Taxation and the Department of Value Added Tax are merged. After the merger of two departments into one organization the merger department is Inland Revenue Department (Bajgain, 2005: 36-37).

There is no separate body for the administration of income tax in Nepal. The Inland Revenue Department is responsible for the income tax administration in Nepal. Organizational structure of the Inland Revenue Department, its personnel structure and position created in the Inland Revenue offices are presented below:

2.3.5.1 Organizational Structure of the Inland Revenue Department

The present organizational structure of the Inland Revenue Department is given below:

Organizational Structure of the Inland Revenue Department



Source: Barshik Pratibedan

There are two main divisions in the IRD: the Operation Division and the Policy and Administration Division. Functions like tax audit, investigation, refund, collection, information technology and taxpayers' services fall under their jurisdiction of the Operation Division. Policy, international tax, advance ruling, appeal, administration, excise and non-tax revenue matters fall under the Policy and Administration Division.

2.3.5.2 Inland Revenue Offices

The nascent organization, at the central level, was called IRD, while filed offices under this department were named Inland Revenue Offices. There are 21 IROs and One large taxpayer office throughout the country, replacing 17

VAT offices and 40 tax offices. Name, place and operational area are given below:

Table 2.1
Inland Revenue Offices

S. N.	Name	Location	Work Area
1	IRO, Bhadrapur	Bhadrapur	All District of Mechi Zone
2	IRO, Biratnagar	Biratnagar	Morang Districk
3	IRO, Dharan	Dharan	Sunsary,Dhancuta,Therhathum, Bhojpur and Sankhuwasava
4	IRO, Lahan	Lahan	All Districk of Sagarmatha zone
5	IRO, Janakpur	Janakpur	Dhanusa, Mahottari, Sindhuli, and Sarlihi
6	Large Taxpayer' Office	Hariharbhawan	High Taxpayers defined by NG
7	IRO, kathamandu 1	Babarmahal	Certain east part of Kathamandu District
8	IRO, Kathamandu 2	Babarmahal	Certain part of Kathamandu District
9	IRO, Kathamandu 3	Lagimpat	West Kath., Rasuwa, Nuwakot,and Dhading
10	IRO, Lalitpur	Lalitpur	Lalitpur District
11	IRO, Bhaktapur	Bhaktapur	Bhaktapur, Kabre, Sindhupalchok, Ramechhap, and Dolakha
12	IRO, Hetauda	Hetauda	Makawanpur District
13	IRO, Birganj	Birgunj	Parsa District
14	IRO, Simara	Simara	Bara and Rauthat District
15	IRO, Bharatpur	Bharatpur	Chitawan and Nawalpur area of Nawalparasi District
16	IRO, Bhairahawa	Bhairahawa	Rupandehi, Palpa, Gulmi and Parasi
17	IRO, Krisnanagar	Krisnanagar	Kapilbastu and Arghakhanchi District
18	IRO, Pokhara	Pokhara	Gandaki and Dhawalagiri Zone
19	IRO, Dang	Dang	Rapti Zone
20	IRO, Nepalganj	Nepalganj	Veri and Karnali Zone
21	IRO, Dhangadi	Dhangadi	Seti Zone
22	IRO, Mahendranagar	Mahendranagar	Mahakali Zone

Source: Barsic Partibedan

2.3.5.3 Personnel of Inland Revenue Department

All tax personnel in Nepal belong to civil service. The government had constituted the 'Revenue Group' within the administration service with a view to bring about specialization and expertise in revenue personnel.

The government has been trying to make the tax administration officer oriented. In this respect, the number of tax officers has been increased substantially over the years. The rationale behind the government's movement is that the tax officers are more knowledgeable and responsible to their duties and can easily adopt to change (Dulal, 2004: 76). The brief description about the personnel of Inland Revenue Department is presented in table below:

Table 2.2

Personnel of IRD

S. No.	Position	Grade	Service	Group	No.
1	DG	G I	Administration	General Administration	1
2	DDG	G I	Administration	General Administration	2
3	Liquor Specialist	G I	Miscellaneous	--	1
4	CA	G II	Contract	General Administration	2
5	Director	G II	Administration	Revenue	10
6	IT Director	G II	Miscellaneous	--	1
7	Deputy Attorney	G II	Law	Govt. Advocate	1
8	Economist	G III	Miscellaneous	--	1
9	Section Officer	G III	Administration	Administration	1
10	Section Officer	G III	Administration	Revenue	22
11	Account Officer	G III	Administration	Account	1
12	Legal Officer	G III	Law	Law	1
13	District Attorney	G III	Law	Law	1
14	Computer Engineer	G III	Miscellaneous	--	2
15	D.E.S.	NG-I	Miscellaneous	--	12
16	Account	NG-I	Administration	Account	3
17	Nayab Subba	NG-I	Administration	Revenue	16
18	Kharidar	NG-II	Administration	Revenue	11
19	A.D.E.S.	NG-II	Miscellaneous	--	2
20	Driver				6
21	Office Assistant				15
Total					112

Source: Inland Revenue Department

The Director-General, who is a Class I gazette officer, is head of the IRD. He is assisted by two Deputy Director Generals and an Alcohol Specialist, all of who are gazette Class I officers. There are 14-gazetted class II officers, including chartered accountants and government advocates, and 29-gazetted Class III officers. There are altogether 44 non-gazette Class I and Class II positions and 21 other posts, including those of drivers and office assistants. The total number of personnel in the IRD is 112.

2.3.5.4 Physical Facility

It has become a challenging task for the Revenue Department to mobilize the revenue successfully. The physical facility provided to the tax administration is very poor. There is lack of furniture and other necessary equipments. The tax personnel have to work in congested environment. Lack of basic administrative facilities like transportation, communication, power supply along with appropriate building is the urgent needs.

The senior officials should get the opportunity to undergo trainings on audit; tax laws, investigation techniques and international taxation so that, they can be efficient in their field and the tax avoidance through loopholes can be reduced.

Staffs of the revenue office have to work more than usual time so that they should give over time allowances otherwise the root of corruption may strengthen. To increase the efficiency of the worker in their performance proper over time allowances with other fringe benefits should be provided to them. This will enhance the administrative efficiency and control the corruption on the other hand.

In classical economics tax was taken as an extra burden to people. But now time has changed and tax has become main source of resource mobilization. Since FY 1959/60, when income tax was started in Nepal, many individuals and institutions have studied in this subject regarding legal aspect, administrative problem, historical aspect, trend and structure productiveness of income tax etc. They are as follows:

2.4 Problem and Prospects of Resource Mobilization through Income Tax in Nepal

2.4.1 Problems of Income Tax in Nepal

Nepalese tax system is circumscribed by serious structural constraints. The major constraints existing in the tax system is that it lacks simplicity and transparency. With extremely limited tax base, low tax elasticity, relatively higher tax rates, poor voluntary compliance, ineffective tax administration, growing arbitration in assessment, rigid and incomprehensive tax laws and regulations, and numerous tax shelters, taxation in Nepal has so far been attributed to negation resulting in rampant corruption. Tax avoidance, evasion and delinquency have also increased substantially over the fears. A majority of the taxpayers are ignorant of insisting laws and regulations. There is apprehension that taxpayers are neither sufficiently protected by the law nor is their contribution ever recognized. A significant amount of revenue is missing before reaching treasury in between the taxpayers and tax officials. The major challenge facing Nepal’s tax administration is how to identify improving voluntary compliance (Dahal, 2004: 319).

The problems of taxation differ with respect to individual taxes. The problems of income tax are broadly categorized into three different heads viz. administrative problems, legal problems and structural problems.

2.4.1.1 Administrative Problems of Income Tax

(i) Failure to Locate New Taxpayers

The tax administration in Nepal lacks up to-date roll of insisting as well as potential taxpayers. The major problem of locating new taxpayers is in the case of non-residence and non-citizen persons. The open border with India has compounded these problems.

(ii) Failure to Maintain Proper Accounts and Records

The Inland Revenue Department is failure to maintain proper accounts and records of income tax. Nepalese tax administration does not have enough information about actually how much taxpayers are in Nepal? What is the actual income status of Nepalese people? Due to the poor database, there is greater possibility of tax evasion.

(iii) Assessment Delays

Assessment refers to the calculation of tax liability by applications of governing rates to taxable income. Assessment procedure, non–maintains of financial records and accounts, lack of information etc. are the major causes of assessment delays.

(iv) Poor Taxpayers Compliance

Nepalese people have tradition of paying indirect taxes. They do not seem to have accepted the payment of income tax as a normal way life. Many people still perceive income tax as an unnecessary payment. There is a general lack of income tax consciousness. Lack of taxpayer education, complicated laws and procedures, unhelpful attitude of tax personnel, poor enforcement of fines and penalties are the main reasons for poor taxpayers' compliance.

(v) Avoidance and Evasion of Income Tax

Avoidance and evasion of income tax is the main problem of income tax. Taxes are compulsory payments, not voluntary contributions. So, people always look for a way to avoid and evade tax in order to minimize present tax. Corruption, illegal business activities, high tax rates, ineffective use of fines and penalties, lack of support from public etc. are the main reasons for tax avoidance and evasion.

(vi) Defective Personnel Management

The human factor is the heart of effective tax administration. The effectiveness of tax administration depends on its personnel. However the personnel of tax administration of Nepal are also falling in corruption. Thus, the tax administration of Nepal is not efficient. Defective selection procedure, lack of efficiency in tax personnel, poor training opportunities, and defective organizational arrangements are the main reasons for defective personnel management.

2.4.1.2 Legal Problems of Income Tax

(i) Complicated Laws and Procedures

Laws related to income tax in Nepal are complicated for average taxpayer to comprehend. They provide widespread discretionary power to tax officers. A taxpayer in Nepal cannot know for certain what his tax liabilities should be. In fact his tax liability varies with whatever the tax officer thinks it to be reasonable.

(ii) Difficult to Charge the Tax on Dual Used Commodity

There are many dual used commodities, which require good judgment either brings it under the tax net or exempt it from taxation. For example, consider the example of a farmer and mini truck. If the farmer uses the truck for further income generating purpose, no doubt, he should pay tax. But if he use this trucks foe his own agricultural purpose, there would not be any income and his property should be tax-free. So, how do the government charge the tax from such kind of dual used commodities, is the great problem of income tax.

(iv) Deviation from the Basic Principle of Income Taxation

The essence of a progressive income tax is that it should take into account the personnel circumstances of the taxpayers. The Nepalese income tax has deviated considerably from this principle. It treats different sources of income differently, resulting in an unequal tax burden upon taxpayers having equal taxpaying capacity. Employees, particularly in the public sector, pay full tax on their income due to withholding of tax. Self-employed people who earn more money, however, are almost out of the tax net, they pay little or no tax on their income.

(v) Long Time Lag

The lag in the collection of income tax is rather long. A taxpayer has to pay the final tax due within 35 days after the receipt of the notice of assessment. The taxpayer is not able to pay within the stipulated period; he must file for an extension with 35 days of the notice of assessment and after the payment of any penalties. The tax officer may allow an extension of up to 9 months. Although fees are charged for late payments, they are not adequate to deter delays in payments.

2.4.1.3 Structural Problems of Income Tax

(i) Narrow Coverage

The base of income tax is extremely very low in Nepal. Agricultural income is exempt from income tax. Capital income is treated favorably. For example, capital gains are not taxed. Dividends are kept out of the income tax net at the shareholders' level while interest on deposits from an account with a bank or finance company is taxed highly. Although, labour income is taxed more heavily than the capital, allowances such as travel allowances, the leadership allowances, medical allowances, telephone allowances, pensions etc. granted to employees are all excluded from the coverage of income tax. In addition, a number of tax incentives have been provided to industries.

(ii) Relatively Higher Tax Rates

Different studies have shown that the large amount of illegal economic activities are prevalent in the under developing countries which are subject to out of tax net. The formally organized sectors, which are under tax net, have to compete with the sectors, which do not pay any tax. It increases the tax evasion and illegal economic activities in the economy. At present 15 percent and 25 percent tax rates are in practice for individual taxpayers. The taxable income that is taxed at 15 percent is Rs.75000, which is slighter low and more income is taxes at the higher rate of 25 percent. So the taxable income at 15 percent rate should be increased. The tax rate should be decreased in order to widen the coverage.

The presumptive tax depending on the business is relatively same over the years. But the limit of profit and transaction is increased. They should be increased proportionately for its effectiveness.

Income derived by an individual from running special industry has to pay 20 percent where as it is 25 percent for the individual taxpayer. This causes the tax avoidance. Hence, such discrimination should be replaced by an appropriate tax rate.

(iii) Exemptions Limit

The exemptions limit does not show any definite relationship with per capita GDP or with inflation rate or with poverty norms. Thus it is unscientific and policy maker should give attention in this aspect in the coming days.

The exemptions limit being equal to the remuneration taxpayers and business individuals do not seem reasonable. To bring all the sources of income including fringe as well as retirement benefit under the tax net, the exemption limit for remuneration taxpayers should be made comparatively higher.

(iv) Deduction

There is no transitional provision for unrelieved pre-operating expenses occurred before income tax act 2002 and there is no provision for the treatment of pre-operating expenses. Hence, the ambiguity in deducting such expenses while calculating taxable income should use, properly defined.

The cost of repair and maintenance of machinery and plant has increased in the latter years, the provision of 5 percent depreciation basis for deduction of that form the assessable income does not totally cover. It discourages the capital formation in the economy.

The tax act 2002 provides Rs.100, 000 or 5 percent of adjusted taxable income, whichever is less as deduction of donation expenses. This limit was fixed many years ago now it should be revised. If the limit is low, it restricts the businessmen from spending money in social sector.

Since Nepal has adopted liberalization policy and tried to attract FDI in different sectors. So investment friendly policy with regard to taxation should me made. The facility of carry forward of unrelieved loss for 7 years in different sides of hydro project is low because of its long gestation period.

2.4.2 Prospects of Resource Mobilization through Income Tax

Income tax can be a major source of resource mobilization if certain pre-requisition or condition are fulfilled.

2.4.2.1 Existence of Predominately Monetized Economy

This means that every economy activities should be monetized. Higher the economy to be monetized, greater will be the possibility to introduce new taxes. Due to the lack of predominant monetized economy developing countries like Nepal have not been able to properly mobilized resources through income tax.

2.4.2.2 A High Standard of Literacy

If the society is highly literate, voluntary compliance will be high. They also realize why they should pay taxes.

2.4.2.3 Large Degree of Voluntary Compliance

Voluntary compliances mean voluntarily disclosement of income and paying taxes according to the rule. If voluntarily compliance is, a great amount of resources can be mobilized through income taxation.

2.4.2.4 Reliable Record of Accounting

In the absence of reliable records of accounting, one cannot actually calculate the income of individuals. There greater possibility of tax evasion. Therefore there should be reliable records of accounting for the proper implementation of income tax.

2.4.2.5 Absence of Wealthy or Comprador Class in the Policy Making

If there is wealthy of comprador class, they act in their self-interest. Their activities go against the proper implementation of income tax government cannot mobilize resources through income taxation.

2.4.2.6 Honest Efficient Administration

Honest and efficient administration is needed for any tax, but minimum acceptable standards appear to be higher for income taxes than for many other levies. Difficult as the task of establishing a satisfactory administration may be, it is probably the condition for successful income taxation that can be met most quickly. The expert, nevertheless, must guard against the assumption that a tidy organization chat and political staffing assure neither good administration nor can he be confident that the best attainable administration will eliminate obstacles to heavy reliance on income taxes.

2.4.2.7. Improve the Tax Administration

In order to improve tax administration the following should be done:

- Every tax administration must get the message that honesty is honored and rewarded, while corruption gets punished.
- Given the resources constraint, resource made available to tax department must be used in a cost efficient way.
- Taxpayer must get the message that evasion would be punished.
- In a large and growing population of tax payer it is not possible to check the returns filed by each assesses. So there is need to proceed on the basis of "self –assessment". It means that tax authority should accept whatever

taxpayers declare on their own subject to random checks. It may not be very wise to concentrate only on “large case”.

- In order to facilitate enhancement, the following need to be done:
- Extension of the scheme of withholding over wide areas such as salary, interest, dividend and even rental incomes.
- Adoption of presumptive approach in taxing the hard-to-tax group.
- Development of an efficient information system.

2.4.2.8 Others

- Increase the extent of tax base.
- Rationalization of tax rates compatible with SAFTA and WTO provision.
- Self-assessment system should be made more effective.
- Improving the efficiency of the tax administration.
- Developing an effective data and information system by using new technology.
- Gradual elimination of exemption.
- Introduction of voluntary dis-closement of income schemes (VDIS).

2.5 Review of Related of Studies

2.5.1 Review of Books

While reviewing the books, most of the books are found syllabus oriented and some of them have described the problems, prospects and development of income tax. There is no detailed studies made on the topic income tax provision related to exemption, concession, deduction and problems, and role of income tax in resource mobilization nevertheless, some books are more important and relevant for this study, which are as follows:

Musgrave (1959) in his book entitled "The Theory of Public Finance" has divided his study into four major parts. First part provides a general framework for an economic theory of the household, combining the functional finance of the stabilization type with other equally important objective of budget policy, including provision for the satisfaction of social wants and adjustment in the distribution of income. Application of welfare economics to the issues of budget determination, the general range of problems usually connected with incidence and effects of budget policy and the problems of fiscal policy as a means of economic stabilization have been described in part second, and fourth respectively.

Amatya (1965) in his book entitled "Nepalma Aayakar Bebastha" has analysed the legal aspects of the income tax. This book is only the description of the income tax and is mainly based on Income Tax Act, 1962.

Marahatta and Khatiwada (1970) in their book entitled "Fundamental of Nepalese Income Tax: with up to date Financial Directives and Regulations" have presented the legal provision as well as practical aspects related to income tax.

Lal (1990) in his book entitled "Direct Taxes: Income Tax, Wealth Tax, Gift Tax and Tax Planning" has explained that income tax plays a very important role in the national economy. It is one of the important sources of revenue to the government. In addition, it is also taken as a tool for achieving the social and economic objectives. Thus, he has concluded that besides, being a source of revenue, income tax has become an effective instrument to ensure balanced socio-economic growth.

Poudyal and Timilsina (1990) in their book entitled "Income Tax in Nepal" have described the theoretical as well as practical aspects of income tax. This book is descriptive rather analytical.

Tiwari(1993) in his book entitled "Income Tax System in Nepal" has described the legal provision related to income tax. He has described the process, provisions and methods to assess the income tax with numerical examples.

Khadka (2001) in his book entitled "Income Taxation in Nepal Retrospect and Prospects" has stated that income tax is annually the third largest source of government revenue producing about 20% of tax revenue. Khadka states that although some attempts have been made in recent time to broaden the coverage, the tax base is still narrow both legally and administratively covering less than one percent of total population of Nepal.

Adhikari (2002) in his book entitled "Income Tax Law: Then and Now" has described the legal provision of new Income Tax Act, 2002. He has also described the decisions made by supreme court about the income tax and also described the legal provisions with critical analysis.

Kandel (2003) in his book entitled "Tax Laws and Tax Planning" has presented various practical and theoretical aspects of taxation with clear and proper logics supported by theoretical explanations and practical problems, in the context of changed act, Income Tax Act, 2002.

Mallik (2003) in his book entitled "Modern Taxation System of Nepal" has presented the history of modern income tax periodically from the very beginning to Income Tax Act, 2002 with the justification of changes and amendments made in the act and regulation. The author has presented Income Tax Act, 2002 in simple and clear crystal manner with suitable examples and explanations wherever necessary.

Agrawal (2007) in his book entitled "Income Tax, Theory and Practice" has dealt with the various aspects of income tax. He has mentioned that the new act (i.e. 2058) is a result of a great deal of efforts by some prominent figures of Nepal and some friends of Nepal. The Income Tax Act, 2058, has completely replaced the old act of 2031.

Amatya, Pokharel and Dahal (2004) in their book entitled "Taxation in Nepal: Income Tax, Property Tax and Value Added Tax" have defined all the terms relating to income tax and value added tax. The examples that are presented in this book are very useful to reader to know more about provisions and procedures of the Income Tax Act, 2002.

Musgrave and Musgrave in their book entitled "Public Finance in Theory and Practice" have focused on individual income tax's provisions, structure of the tax base, problems of inclusions and deductions of income tax. They have further explained the structure and integration of corporate income tax.

2.5.2 Review of Reports and Articles

Some report and articles have been reviewed while conducting this study and they are as follows:

Reejal(1976) in his article named "Revenue Productivity and Elasticity Aspects of Nepalese Taxation" Published by CEDA explained that Nepalese tax structure, as a whole was fairly elastic, with elasticity coefficient 1.82 and buoyancy 2.18 for the total tax revenue. This study found that the income tax to be highly elastic 4.39 which was highest among all the tax categories.

Agrawal (1978) in his article named "Resource Mobilization for Development: The Reform of Income Tax in Nepal" has found that buoyancy of income tax with respect to GDP for period FY 1967/68 to FY 1975/76 is 2.18 and elasticity is 2.01. He was further identified that the main defects of the income tax administration as failure to locate new taxpayers, to maintain the accounts, delay in assessment, poor taxpayer compliance, evasion and avoidance of tax, and defective management.

Jantrcher and Bird (1992) in their article "The Reform of Tax Administration" have suggested three main ingredients that are necessary for a successful tax administration reform in developing countries. First, the tax structure usually needs to be simplified for ease of compliance to the administration. Second, a reform strategy suitable to the specific circumstances of country must be developed. Finally and overall, there must be a strong political commitment to the improvement of tax administration and best-designed efforts will fail.

Easterly and Rebelo (1992) in their working paper named "Marginal Income Tax Rates and Economic Growth in Developing Countries" have explained that the high income tax rate has a negative effect on the pace of economic expansion. This report has provided suitable methods for computing average marginal income tax rates that combine information on statutory rate with the amount of tax revenue collected and with data on income distribution.

Dahal (2052) in his report named "Review of Tax System" has addressed the narrow tax base, low tax elasticity, higher burden of indirect tax compared to direct tax lack of voluntary compliance, wide spread tax evasion, leakage's etc. as main constraints of Nepalese tax system. Including income from agricultural sector, income from domestic industries, social sector and electricity sector, which contributes 52% of total GDP, is exempted from income tax. This report has suggested that about 40% extra resource mobilization is possible if proposed tax policy and program are in place.

Bonis (1997) in his working paper named "Regional Integration and Factor Income Taxation" has analyzed the issue of factor income taxation in the context of regional integration agreements. If Countries remove the barriers to trade and factor movement, taxation will distort the allocation of resources across borders. He has further concluded that the cross country uniformity of taxes on income from mobile factors is not necessarily an optimal outcome because the tax rate around which equalization takes place might not be the 'right' one.

Thapa (2000) in his article entitled "Nepalko Rajaswako Samrachana, Rajaswako Sthiti Ra Chunautiharu" published in Rajaswa has described that the agricultural income which contributed about 40% of GDP being tax free, about 50% of total population being below the poverty line, tax holiday for new industries, lack of political commitment are the major causes of poor resource mobilization in Nepal.

Kandel (2001) in his article named "Draft of Income Tax Act, 2002. Critical Analysis" has analyzed the draft on several grounds like exemption of agricultural income from tax coverage, export duties levied upon export inequality in tax rates imposed on different capital earned income and no adjustment for inflation rate in the tax act, rules and regulation.

Regmi (2007) in his article entitled "Income Tax Evasion is a Crime in Nepalese Legislation" has explained that the current trend of collection of income tax and the contribution of it in the national revenue is far from satisfaction. This study has also suggested to enhance some progressive reforms in current income tax law with practical solutions and well set up mechanisms.

Timsina (2007) in his article entitled "Tax Elastically and Buoyancy in Nepal: A Revisit " has concluded that the automatic response of tax to income is low. Compared to the period FY 1975 to FY 1994, the elasticity coefficients of tax during the review period (FY 1975 to FY 2005) did not reveal significant differences. The buoyancy and elasticity of income tax during the study period was 1.37 and 0.41 respectively. This study has further concluded that only the discretionary measures cannot generate more revenue freeware. Improvement in tax administration to control the leakage and to broaden the tax bases in practice is important for enhancing the elasticity of the tax.

2.5.3 Review of Thesis and Dissertations

Some theses and dissertations are reviewed for this study and they are as follows:

Kayastha (1974), in his dissertation named *"Taxation of Income and Property"* has discussed the role, importance, and historical and legal aspects of income tax. Main objectives was to examine of tax poverty in Nepal in the context of planned economic development since 1951, objectives broadly classified in three categories namely growth, equitable distribution and stabilization.

He has concluded that the reason for the very poor significance contribution of income tax to government revenue is due to the tax evasion. He has pointed out that the tax evasion is the main problem of income tax system of Nepal.

Major Finding:

Of the three main objective of taxation the objective of growth is naturally emphasized must in Nepal. The other two are regulated to the background.

- Lack of proper valuation method of urban poverty.
- To tap the resources, in 1959/60 the tax structure was diversified & many new taxes like salary tax, business tax, poverty tax etc. were introduced.
- Before 1950, Nepal didn't have scientific economic policy which could facilities the economic development of the country.
- The budgetary figures show that during two decades starting from Fiscal year. 1951/52 to 1971/72, the budget ran into deficit except in four fiscal year. Government financial resources gap in resent time is estimated to increase & rich Rs. 120 crore rs 7 Rs.350 crorers by 1975/76 7 1980/81 respectively.

Bhandari (1994), in his dissertation named *"Contribution of Income Tax to Economic Development of Nepal: with Reference to Kathmandu and Pokhara Valley"* has found that to increase the contribution of income to economic development of Nepal, capital gain and agricultural income should be taxed. He has also suggested differentiating the exemption limit to the family with one child and two children. The main objectives were:

- To examine the historical background of income tax in Nepal
- To examine the trend of income tax collection of tax revenue as well
- To examine the Nepalese income tax structure
- To identity the factors to increase taxpaying habit of income tax payer
- To examine the contribution of income tax to the economic development of Nepal.

Major Finding:

1. There is part taxpaying habit of Nepalese people , basically due to the little knowledge of tax & its importance, povertyness of tax payer & wide spread practice of illegal business.
2. Is increase contribution of tax to the economic development of Nepal , it is necessary to impose capital tax for high class farmer.
3. Among the various sources of income tax, individual tax payers, public enterprises, remuneration, semi-public enterprises, & private corporate bodies occupy first and 2^{nd}, 3^{rd} 4^{th} & 5^{th} position respectively.

Shrestha (2001), has presented a dissertation named *"Revenue collection from Income Tax in Nepal"* problem and prospects to T.U. In her study, she had described the conceptual frame work, legal provision administrative aspect and structure of income tax in Nepal. She bas been conducted and opinion survey in respect of problem and prospects of income tax in Nepal.

He finding about problem of Nepalese income tax system were mass poverty narrow tax coverage and lack of consciousness of tax payer, predominance of agriculture widespread evasion and avoidance of income tax, unscientific tax assessment procedure in efficient tax administration, complicated tax laws and procedures instability in government policy. She had found various weak point of Nepal ease tax administration. The major weak point are: failure to maintain proper account and seconds defective selection of personally lack of trained and competent tax personnel, undue delay in making assessment, lack of motivating in tax personal, existence of corruption.

She suggests that income tax system will be succeeded if the system were widening of tax coverage, tax consciousness to people, minimize the evasion and avoidance problem, and enhance the self assessment system reform in income tax assessment and administration system.

Poudel (2002), in her dissertation named *"Income Taxation in Nepal: A Study of its Structure and Productivity"* has explained that within the direct tax, income tax is the largest source, which contributed more than 86% in FY 1999/00. The contribution of income tax to direct tax has increased significantly since its introduction. The elasticity and buoyancy coefficient of income tax has been found to be 0.61 and 1.36 respectively during the period FY 1975/76 to FY 1999/00. This shows that Nepalese income tax is very inelastic and there are minimum chances for further discretionary changes.

Sharma (2002), in his thesis named *"Taxation of Income in Nepal"* has explained that with the passage of time, the ancient taxation of property become both less fashionable and less productive. The relative welfare position of individuals began to measure in terms of their income and therefore tax on income become respectable both among the ranks of economists and policy makers. He has further mentioned that the internal resource mobilization as a percentage of GDP has gone up and the structure of income tax in Nepal is not much responsive.

Palli Magar (2003), had covered tax structure, role of income tax and exemptions and deduction provided in the law. He had found that there was dominated share of tax structure in Nepalese government revenue. Income tax had occupied third positions his study period and it was increasing trend. The tax/GDP ratio was not found satisfactory. With the income tax, there was the dominated role of corporate income tax but it was in decreasing trend and contribution of individual income tax was second position and it was in second position it in 1 me, trend. Lack of trained employees, shortage of income tax expert's professional in tax administration, lack of public participation, faulty organizational structure of tax administration, weakness in government policy, defective income tax act were the major cause for inefficient tax administration, observed by him. His suggestion about exemption were: revision the exemption unlit, elimination double taxation oil dividend, tax rebate, for submitting true income statement in time, increase income tax rate slab up to 10, increase the exemption limit to individual as well as family etc. Besides above, suggestions about deduction were: clear provisions for deduction; frilly allowed interest expense, pollution control expenses, repair and improvement expenses, research and development expenses. He is totally concentrated oil the exemption and deduction iii study. He has not study about various aspect of income tax.

Dulal (2004), in his dissertation named *"Income Taxes in Nepal: Study of its Structure and Contribution to Revenue Generation"* has explained that the contribution of income tax to total revenue was 7.8% in FY 1975/76 and in FY 1999/00 it was 14.5%. This study has explained that the income tax rates and slabs have been changed radically in recent years. Under new Income Tax Act, 2002, individual income tax is levied with low rates of 15% and 25% and the corporate income tax is levied with single rate of 25%. For bank and financial institutions the rate is 30% of taxable income.

Neupane (2005), in his dissertation entitled *"Income Tax as an Internal Source of Resource Mobilization in Nepal"* has concluded that the Tax/GDP ratio in Nepal is very nominal as compared to the same ratio in neighboring SAARC and other developing countries Among various objectives of his study, some objectives are to study the reasons for growing resource gap in Nepalese economy, to analyze the role of income tax as an internal instrument of resource mobilization, to identify the role and status of income tax in total tax structure and to provide suitable recommendations for the improvement of internal resource mobilization through income taxation in Nepal. He has also concluded that income tax is the main component of direct tax and its contribution on direct tax and total tax revenue is 78.78% and 19.02% respectively. He has further said that for the economic upliftment of the nation, additional internal financial resource mobilization should be strengthened and generation of more revenue internally, planned development efforts, political stability and liberal economy may be the means for such mobilization.

Sapkota (2008), presented a dissertation entitled "*Contribution of Income Tax to National Revenue; Before and After Enactment of Income Tax Act 2058"*. The main objective of the study was to analyze the contribution of income tax in national revenue before and after enactment of Income Tax Act 2058, to provide suitable suggestion for the betterment of income tax system in Nepal. During his study, he found that performance of income tax before and after new act seems not regular. The new income tax act is introduced on 2001/2002 and total income tax has first time declined by 210.3 million and by-2.3% that year. It further decreased by 937.5 million and -10.5% for FY2002/03. In FY2000/01 growth rate was 22.8% and that was more than 20% for other preceding year but is just 2.1% in the year FY2005.06. He suggested that overall revenue policy as well as tax policy should be revised. Tax offices should be decentralized for broad coverage of geographical region. Different recent technologies such as e-taxation should be introduced and promoted to avoid complexities and delay in income tax administration.

2.6 Research Gap

Tax is the strong sources of Government revenue. It plays important role in revenue collection and help to effective mobilization of verious resource. Tax system depends on its legal provision and its popularity also depends oil its transparency for providing a lot of information about tax. Different researches have research oil the topics of income tax in different ways. Their objectives and analyzing system are in different way. After studying different research paper held on "Resource Mobilization through Income Tax in Nepal", the researcher I make this research different for other found various gap on selected topic to make this different also analyze theoretical concepts. Analyze the reliable data and analyze the different views of different respondents.

This thesis has tried to find the resource mobilization trend through income tax in Nepal since 1990/91 with covering eighteen years data. Various studies have been done on the topic of revenue collection and contribution of income tax, but no one has given focus on mobilization of resource and trend analysis through income tax. This research focused previous analysis and future trend analysis to compute elasticity and buoyancy of income tax in Nepal and it has also focused problem and prospects in such field.

CHAPTER - III

RESEARCH METHODOLOGY

3.1 Introduction

Resource mobilization has a crucial in fiscal policy implementation, especially in a developing country where the demand of public funds for public expenditure is high. It is the better source of resource mobilization than other sources such as deficit financing and money creation. As tax revenue is the major source of domestic revenue in Nepal, the measurement of tax elasticity and buoyancy would be very beneficial in terms of reforms in tax structure as well as revenue administration. In addition to this, the study of tax elasticity and buoyancy is also useful for revenue forecasting (Timsina, 2007: 9).

Tax revenue may change due to verity of factors, such as changes in income, changes in tax rate and tax base, changes in efficiency of tax assessment and collection, among others. The responsiveness of tax revenue to such changes can be explained with the help of tax elasticity and buoyancy. Tax elasticity may be defined as the ratio of a percentage change in adjusted tax revenue to a percentage change in income i.e. nominal GDP. On the other hand, tax buoyancy refers to changes in actual tax revenues due to the changes in income as well as due to the changes in discretionary measures such as tax rates and tax bases (Mukul, 1997: 63). This distinction between the tax elasticity and buoyancy is very useful in analyzing and evaluating whether further revenues will be sufficient to meet the resource needs without changing the rates or bases of the existing tax. To measure the tax elasticity, historical tax series must be adjusted so as to eliminate the effects of tax revenue from discretionary changes. If there is no change in tax rates and tax base during the reference period, buoyancy will be the same as elasticity.

Elasticity is measured with adjusted data while buoyancy is measured with unadjusted data. If an elasticity of unity means that each one percentage change in GDP is accompanied by one percentage change in tax revenue, an elasticity of less than unity means that the percentage change in revenue will be less than the percentage change in GDP and an elasticity greater than one means that the percentage change in revenue will exceed that in GDP. A tax system is said to be elastic if the measure exceeds one and inelastic if it is less than one (Goode, 1986: 92). High tax elasticity is said to be desirable attribute because it leads to natural growth in revenue for financing the rapidly growing development expenditure without the need for politically difficult decisions to raise taxes. However, major sources of government revenue may have a low elasticity, in which case the authorities must seek additional revenue by introducing discretionary changes (Timalsina, 2007: 28). The difference between the elasticity and buoyancy coefficient of the tax is used to whether discretionary changes always siphon off additional revenue and vice versa. Because of the nature of discretionary changes they can be adopted in a particular situation to collect more revenue immediately to fulfill the current requirement but in the long run, raising elasticity is desirable and frequent discretionary changes might be intractable and may be unpopular as well.

An efficient tax system ought to give better results and be progressive; it should possess elasticity greater than one. Of course the degree of progressiveness depends upon the desired level of objectives of the economy. Generally, elasticity and buoyancy are defined as the ratio of relative change in dependent variable (tax yield in the study) to the relative change in independent variable (GDP). Mathematically, both elasticity and buoyancy have been calculated on the basis of following equation;

$$e = \frac{\Delta T}{T} \times \frac{Y}{\Delta Y} \ldots\ldots\ldots\ldots\ldots\ldots\ldots (1)$$

Where,

e	= elasticity of total tax to GDP		
ΔT	= change is tax revenue		T = tax revenue (income tax)
ΔY	= change in GDP		Y = GDP

The income elasticity of each separate tax may be decomposed into the elasticity of tax to base and the elasticity of base to income. Thus, the base elasticity and buoyancy have been calculated on the basis of the following equation:

$$e_1 = \frac{\Delta T}{T} \times \frac{B}{\Delta B} \text{ .... (2)}$$

Where, e_1 = elasticity of total tax to proxy base

ΔT = change in tax revenue T = tax revenue

ΔB = change in proxy base (non-agriculture GDP)

B = amount of proxy base (non-agriculture GDP)

For calculating elasticity, the adjusted revenue yields are used. This is done to eliminate discretionary changes to find out the built in flexibility where as the actual yields are used to calculate buoyancy. By calculating the difference between elasticity and buoyancy the role of discretionary changes in income tax revenue is observed.

3.1.1 The Adjustment Procedure

Tax revenue usually changes due to discretionary measures, for example, changes in tax rates, tax net expansion and so on. Therefore, a need to separate the changes in revenue emanating through the discretionary measures from that due automatic measures arises to estimate the elasticity. This is the way to distinguish tax elasticity from tax buoyancy.

Tax revenue series can be adjusted in four ways: constant rate procedure, the proportional adjustment procedure, devise index procedure and the dummy variable procedure. The selection of the appropriate adjustment method depends upon the availability of the data on tax changes and the type and frequency of such changes. The constant rate structure method requires disaggregated data on tax rates and tax bases; whish is not easily available in Nepal. Since the tax revenues change frequently through the discretionary changes, the dummy variable procedure is not applicable. So the proportional adjustment procedure, which requires calculation of the revenue implications of discretionary measures, is applied in the study to adjust the historical tax revenue data. In this method, to remove the estimated revenue impact through discretionary measures, the annual observed data are adjusted for discretionary changes. The resulting series are converted to the first year's basis by adjusting the year to year changes by the ratio of the tax yield on the basis of the first year rates to the actual tax yields.

In Proportional Adjustment Method, it adjusts the historical revenue series for each to derive a revenue yield based on the structure of rate and exemptions for a reference year. In this method, there are several alternative methods for adjustment such as: Prest Method, Sahota Method and Chand Method.

Sahota Method

Sahota's adjustment of actual tax receipts to a series (I_i), which he argues, excludes discretionary effects, is accomplished by:

$$I_i = \frac{T_i}{T_{i-1}}(I_{i-1})$$

Where, T_i stands for i^{th} year tax collection adjusted to rates in year i-1. This can be written in other way:

$$IT_t = \frac{AT_t \pm RT_t}{AT_{t-1}} \times IT_{t-1}$$

Where,

IT_t = index of net tax receipt of the year t.

AT_t = actual tax yield of the year t.

RT_t = actual discretionary changes

t = the t^{th} year.

t-1 = the one period lag.

Sahota Method is used for making adjustment to eliminate discretionary changes. It adjusts the actual figure or the current year on the basis of the adjustment figure of the previous year. Same result comes from another Prest Method also. Constant Structure Method is the best method for calculating adjusted revenue series in developed countries where previous data are easily available but for developing countries like Nepal, Sahota method is the second best method, as it requires less data details.

3.2 Research Design

This research has been an analytical and descriptive in design using historical data to assess the current role of income tax in resource mobilization internally and to explore some potential areas for additional domestic resource mobilization through income taxation to shorten the gap of resource deficit in Nepalese Finance.

This research has tried to analyze and describe the taxation system by its own procedure. Historical data of last 16 years has been fully taken into consideration. The main variables used in analysis are Gross Domestic Product (GDP), tax revenue and non-tax revenue of government. Tax revenue of the government is broken down into direct tax and indirect tax. Both direct and indirect taxes are again sub divided into different subcomponents

3.3 Nature and Sources of Data

Secondary sources of data have been used for the conduct of this research. The sources of data consist of books, journals, newspapers, reports and dissertations. The major sources of secondary data are as follows:

a. Different Publications of Ministry of Finance.
b. Report and records of Inland Revenue Department.
c. Published documents of NRB and NPC.
d. Dissertations available at the central library of T.U.
e. Dissertations available at library of Shankar Dev.

f. Articles published on different journals and news magazines.
g. Different publications of Central Bureau of statistics (CBS).
h. Internet, e-mail.
i. Different publications of World Bank.
j. Different publications of IMF.

3.4 Variables Used in the Model

Total revenue of the government has been classified into tax and non-tax revenue. Further, tax revenue is again divided into direct tax and indirect tax. Direct tax includes income tax, the tax on land revenue and registration fees. Similarly, indirect tax in turn is divided into custom and tax on consumption and production of goods and services. The independent variable, GDP, will be regressed with income tax as the dependent variable in the study to estimate the elasticity and buoyancy coefficient of income tax.

Dependent Variable	Independent Variables
Income Tax (T)	Total GDP (Y),
	Non-Agri.GDP (Y_1)
	Income Year (x)

3.5. Identification of the Model

The formula that is used to estimate elasticity as shown in the equation (1) ignores true functional relationship between the variables. Therefore, elasticity can be obtained by regressing the income with the tax yield by using following exponential form of equations as:

$$T = \alpha Y^{\beta} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots .. (3)$$

Where,

β measures the elasticity or buoyancy

Elasticity is defined as the automatic response of tax revenue to change in GDP and buoyancy as the total response of tax revenue including discretionary changes, associated with a given percentage change in GDP.

Least square method is used for trend analysis and projection. The equation of trend line is given as follows:

$$Y = a + bX$$

Where,

Y = Income Tax

X = Income Year

a and b = Parameters

3.6 Specification of the Model

In this study the double log linear model is used to estimate the built-in-flexibility or elasticity with respect to adjusted revenue series is measured from the relation.

$$T_a = \alpha Y^{\beta}$$

Taking log on both sides;

$$\log T_a = \log \alpha + \beta \log Y \text{ ……………………… } (4)$$

For base elasticity,

$$\log T_a = \log \alpha + \beta \log Y_1 \text{ ……………………… } (5)$$

Similarly, sensitivity or buoyancy coefficient with respect to actual tax revenue series and GDP is estimated from the relation.

$$T = \alpha Y^{\beta}{}_1$$

Taking log on both sides;

$$\log T = \log \alpha + \beta_1 \log Y \text{ ……………………… } (6)$$

For base buoyancy,

$$\log T = \log \alpha + \beta_1 \log Y_1 \text{ ……………………… } (7)$$

Where,

T_a = adjusted tax revenue series

T = actual tax revenue series

Y = total GDP

Y_1= total non-agriculture GDP

β = elasticity coefficient

β_1= buoyancy coefficient

α = coefficient

Empirical test developed here is that there is good and strong relationship between respective independent variables and dependent variables. Common statistical test namely F-test has been used to test the significance of the coefficient of elasticity and buoyancy at 1 percent level of significance and to test the reliability of the model being used. The value of R^2 has been calculated to see how good the relationship between the dependent and independent variables are in the equation.

The least square method of a time series analysis is used for the trend analysis and projection.

$$Y_c = a+bX$$

Where,

Y_c = Estimated value of Y for any given value of independent variable X.

a =Y-intercept or value of Y when X=o

b =slope of the trend line/ amount of change inn ‘Y’ per unit change in ‘X’

The value of ‘a’ and ‘b’ is obtained by solving the following two normal equations:

$$\sum Y = Na + b\sum X$$

$$\sum XY = a\sum Y + b\sum X^2$$

Where,

N= number of years

Now, substituting the value of ‘a’ and ‘b’ in equation (1), gives the equation of the trend line.

3.7 Tools of Analysis

Both quantitative as well as qualitative methods have been employed for the purpose of data analysis. However, the quantitative tools have been employed widely. It has been seen as the best method for the data analysis and also to reach at the conclusion. Different statistical tools for both estimation and test have been employed as demanded by the objectives so specified above.

With regard to the model used above, following measures are carried out to check the reliability of the analysis:

Coefficient of Determination (R^2)

The R-squared (R^2) statistic measures the success of regression in predicting the values of dependent variables within the sample. Estimate of coefficient of determination (R^2) shows the percentage of the total variation in dependent variables explained by independent variables. The value of R^2 lies between 0 and 1. The higher the R^2 the greater will be the percentage of the variation of dependent variable (T) explained by the independent variable (Y) i.e. the better the 'goodness of fit' of the regression plane to the sample observations and closer the R^2 to zero the worse the fit of regression plane.

Adjustment Coefficient of Determination ($\overline{R^2}$)

This measure is also employed to get additional information about the goodness of fit. One problem with using R^2 as a measure of goodness of fit is that the R^2 will never decrease as more regressors are added. In the extreme case, we can always obtain an R^2 of one if we include as many independent regressors as there are sample observations. The adjusted, commonly detonated as $\overline{R^2}$ penalizes the R^2 for the addition of regressors, which does not contribute to the explanatory power of the model.

t-test

The t-test is based on the students' distribution. It is used to test the hypothesis about any individual partial regression coefficient. To compute the t-statistic, the standard errors for each input are computed separately. The t-ratio is the significant test of the regression coefficient of the hypothesis. Broadly speaking a test of significance is a procedure by which sample results are used to verify the truth or falsity of null hypothesis. The decision to accept or reject null hypothesis is made on the basis of value of the test statistic obtained from the data at hand. The t-statistic, which is computed as the ratio of an estimated coefficient to its standard error, is used to test hypothesis that a coefficient is equal to zero, to interpret the t-statistic given that the coefficient is equal to zero.

F-test

For the purpose of analysis of variance, this test is employed. The F-statistic tests that all of the slope coefficients in a regression are zero. For ordinary least square models, the F-statistics is computed as,

$$F = \frac{R^2 / (K-1)}{(1-R^2) / (N-K)}$$

Under the empirical test with normally distributed errors, this statistic has an F-distribution with K-1 numerator degrees of freedom and N-K denominator degrees of freedom.

The p-value denoted probability (F-statistics) is the marginal significance level of the F-test. If the p-value is less than the significance level we are testing, say, 0.01, we reject the empirical tests that all slope coefficients are equal to zero. For the explanation above, the p-value is essentially zero, so we reject that all of the regression coefficients are zero.

CHAPTER - IV

DATA PRASENTATION AND ANALYSIS

4.1 Resource Gap in Nepalese Finance

Scarcity of resources is constrained for the realization of development goals in developing countries. Nepal has also been facing serious and growing problem of resource gap in her finance since her first budget 1951/52. A resource gap is taken to be the difference between expenditure and revenue. The outlook of resource gap can be seen as follows:

Resource gap 1= Expenditure –Revenue

Resource gap 2= Resource gap 1- Foreign grants

Resource gap 3= Resource gap 2- Foreign loans

To fill the ditch of growing resource gap, a large amount of external aids, loans and internal loans has to be borrowed but scarcity of resource seems to be never ending phenomenon in Nepal. In the first budget of Nepal there was a regular expenditure of Rs. 42 million and there was no development expenditure. A total of Rs. 30.5 million was collected as revenue and the government did not take any foreign loan and grant. This year the resource gap was of Rs. 11.5 million (Neupane, 2005: 43).

Table 4.1

Resource Gap in Nepalese Finance

Amount Rs. in Million

Fiscal Year	Total Expenditure	Total Revenue	Resource Gap 1	Foreign Grants	Resource Gap 2	Foreign Loans	Resource Gap 3
	A	B	A-B	C	A-(B+C)	D	A-(B+C+D)
1990/91	23549.8	10729.9	12819.9	2164.8	10655.1	6256.7	4398.4
1991/92	26418.2	13512.7	12905.5	1643.8	11261.7	6816.9	4444.8
1992/93	30897.7	15148.4	15749.3	3793.3	11956	6920.9	5035.1
1993/94	33597.4	19580.8	14016.6	2393.6	11623	9163.6	2459.4
1994/95	39060	24575.2	14484.8	3937.1	10547.7	7312.3	3235.4
1995/96	46542.4	27893.1	18649.3	4825.1	13824.2	9463.9	4360.3
1996/97	50723.7	30373.5	20350.2	5988.3	14361.9	9043.6	5318.3
1997/98	56118.3	32937.9	23180.4	5402.6	17777.8	11054.5	6723.3
1998/99	59579	37251	22328	4336.6	17991.4	11852.4	6139
1999/00	66272.5	42893.8	23378.7	5711.7	17667	11812.2	5854.8
2000/01	80483.3	48893.9	31589.4	6753.4	24836	12044	12792
2001/02	80752.4	50445.6	30306.8	6686.2	23620.6	7698	15922.6
2002/03	83939.9	56229.7	27710.2	11339.1	16371.1	4546.4	11824.7
2003/04	89601.9	62331	27270.9	11283.4	15987.5	7629	8358.5
2004/05	104184.4	70122.7	34061.7	14391.2	19670.5	9266.1	10404.4
2005/06	110106.2	72282.1	37824.1	13827.5	23996.6	8214.3	15782.3
2006/07	133604.5	87712.2	45892.3	15800.8	30091.5	10053.5	20038
2007/08	161349.9	107622.5	53727.4	20320.7	33406.7	8979.9	24426.8

Source: Economic Survey and A Handbook of Government Finance and Statistics

Table 4.1 provides a picture of growing resource gap in Nepalese finance. Resource gap 1 which is the difference between total expenditure and total revenue is in increasing trend. It has increased from Rs 12819.9 million in FY 1990/91 to Rs 53727.4 million in FY 2007/0788. This increase in resource gap indicates the poor performance of domestic resource mobilization.

Resource gap 2, which is the difference between expenditure and revenue plus foreign grants, is also is in increasing trend. This type of resource gap started since the budget of FY 1956/57. In this year it was Rs 0.7 million that rose to Rs 609.4 million in FY 1978/79 with an average annual growth rate of 2.86 percent (Neupane, 2005; 45). This gap was 10655.1 million in FY 1990/91 and reached to 33406.7million in FY 2007/08. This gap was minimum (i.e. 10547 million) in FY 1994/95 under the study period.

The picture of resource gap 3, which is the difference between expenditure and total revenue plus foreign grants plus foreign loan, is still not promising. It was increase from 4398.4 million in FY 1990/91 to 24426.8 million in FY 2007/08. This gap was minimum (i.e.2459.4 million) in FY 1993/94 under the study period. This increasing magnitude of resource gap clearly indicates that there is urgent need for mobilization of additional resources even through income tax.

The increasing gap between government expenditure and revenue and high fiscal deficit have contributed economic distortion such as increasing in prices, large flow of imported goods and services, low level of domestic savings and heavy reliance on external debt, leading the economy to the state of external dependency. Increase in regular and development expenditure of government, burden of debt servicing charges, poor utilization of natural resources, poor economic growth, inadequate tax efforts, political, instability rising inflation etc. are the reason for growing resource gap in Nepalese finance.

4.2 Role of Income Tax in Resource Mobilization

The need for mobilization of financial resources has been growing rapidly since planned development efforts began in Nepal. This need has been specially pronounced the urgency for domestic resource mobilization. If we see the details of financial outlay in various development plans the resource need has increased 194170 times being the tenth plan outlay of Rs. 64076000 million in comparison to the first plan outlay of Rs.330 million. This has indicated a rapidly increasing trend in financial outlays for development.

In developing nations, use of foreign aids and loans have produced bitter experiences as well as mixed consequences. The repayment of principle and interest is providing to be a net burden for many of them. It can at most occupy only a marginal and dwindling importance in the financing of development activities. Mobilization of resources from domestics source is the only viable stress needs to be placed on financing of development efforts in Nepal. Foreign aid should be taken as complement to domestic efforts not substitute for domestic source of government financing.

The success of development efforts of any country depends on its ability to mobilize additional internal resources to finance regular and development expenditure. Tax is considered safer and better means for the mobilization of additional financial resources as compared to other internal and foreign recourse as compared to other internal foreign sources of deficit financing. Income tax is one of the major components in total tax revenue that plays a vital role in internal resources mobilization. The rate of role of total tax and income tax for additional financial recourse mobilization is analyzed on the basis of their relative contribution to the GDP.

4.2.1. Tax Effort Ratio and Per Capita Income: International Comparisons

The level of taxation is typically measured by tax revenue as a share of GDP. Comparing levels of taxation across countries provides a quick overview of the fiscal obligations and incentives facing the private sector.

Low ratios of tax revenue to GDP may reflect weak administration and large-scale tax avoidance or evasion. Low ratios may also reflect a sizeable parallel economy with unrecorded and undisclosed incomes. Tax revenue ratios tend to rise with incomes, with higher income countries relying on taxes to finance a much broader range of social services and social security than lower income countries are able to (WDI, 2007: 287).

Table 4.2

GDP, Per Capita Income and Tax Revenue as Percentage of GDP of Selected Countries in 2005

Countries with different Income Group	GDP in 2005 (in million of $)	GNI Per Capita 2005 (in US $)	Tax Revenue as % of GDP
Lower Income			
Nepal	7,391	270	10.1
India	805,714	730	10.2
Pakistan	110,732	690	9.5
Ghana	10,720	450	22.4
Lower Middle Income			
Sri Lanka	20055	1010	14.0
Thailand	161688	2490	17.1
Peru	68637	2360	13.5
Upper Middle Income			
Argentina	153014	3580	14.2
Chile	94105	5220	19.9
Malaysia	118318	4520	17.6
South Africa	212777	3630	27.5
High Income			
Australia	637327	27070	23.9
Switzerland	357542	35840	26.0
USA	11711834	41440	11.2
UK	2124385	33630	28.3

Source: World Development Indicator

Nepal is one of the poorest countries with GDP 6707 $ million in 2004 and GNI per capita is 250 $ in 2004, according to the World Development Indicator 2006. The contribution of tax revenue to GDP in 2006 was only 9.8 percent, which is the lowest in the SAARC countries. The table 5.1 shows that the highest GDP is of USA 11711834 $ million in 2004 while tax revenue as percentage of GDP is 9.8 percent. Similarly, the highest contribution of tax revenue to GDP is 27.4 percent in the case of UK. GNI per capita of Nepal is also very low and it is around 250 $ since long time. But with regard to other countries either belongs to low-income country or lower middle-income country the GNI per capita income is comparatively very high.

4.2.2 Tax Structure of Nepal

When the GN presented first budget in the FY 1951/52, the revenue structure was typically that of traditional economy with 73 percent of government receipts coming from non-tax sources and land tax only. But latter in the late 1950s the share of non-tax revenue declined drastically, because of the increasing contribution of indirect tax on foreign trade (Timalsina, 2007; 57). In the FY 1990/91 the share of non-tax revenue was 23.79 percent of total revenue. But it reached to the maximum 26.91 percent in the FY1991/92.

Table 4.3

Contribution of Tax Revenue and Non Tax Revenue in Total Revenue (FY1990/91 to FY2007/08)

1.1.2 Amount in Rs. Million

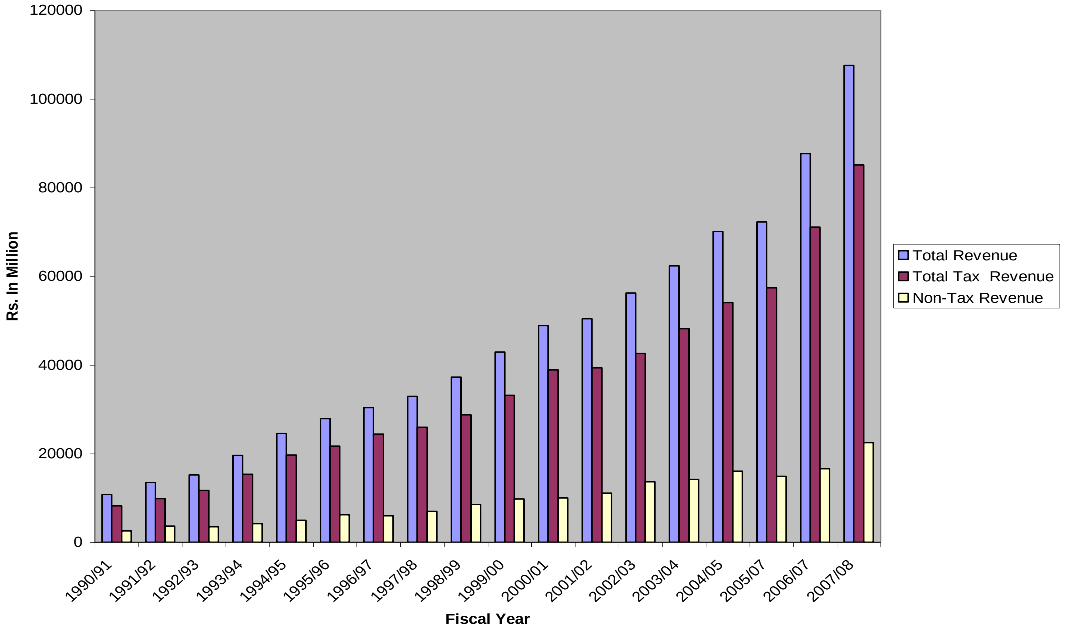
Fiscal year	Total GDP	Total Revenue	Revenue % of GDP	1.2 Total Tax Revenue	TR as % Total Rev.	Non-Tax Revenue	NTR as % Total Rev.
1990/91	116127	10729.9	9.23	8176.3	76.20	2553.5	23.79
1991/92	144933	13512.7	9.32	9875.6	73.08	3637.1	26.91
1992/93	165350	15148.4	9.16	11662.5	76.98	3485.9	23.01
1993/94	191596	19580.8	10.21	15371.5	78.50	4209.4	21.49
1994/95	209974	24575.2	11.70	19660	79.99	4945.1	20.12
1995/96	239388	27893.1	11.65	21668	77.68	6225.1	22.31
1996/97	269570	30373.5	11.26	24424.3	80.41	5949.2	19.58
1997/98	289798	32937.9	11.36	25939.8	78.75	6998.1	21.24
1998/99	330018	37251	11.28	28752.9	77.18	8494.4	22.80
1999/00	366251	42893.8	11.71	33152.1	77.28	9741.6	22.71
2000/01	425454	48893.9	11.49	38865.1	79.48	10028.8	20.51
2001/02	444052	50445.6	11.36	39330.6	77.96	11115	22.03
2002/03	473546	56229.7	11.87	42587	75.73	13642.7	24.26
2003/04	517993	62331	12.03	48173	77.28	14158	22.71
2004/05	566579	70122.7	12.37	54104.7	77.15	16018	22.84
2005/07	630301	72282.1	11.46	57430.4	79.45	14851.7	20.54
2006/07	696989	87712.2	12.58	71126.7	81.09	16585.5	18.90
2007/08	781262	107622.5	13.78	85155.5	79.12	22467	20.88

Source: Appendix I

The data on table 4.3 shows that the contribution of tax revenue in the total revenue is almost 80 percent of the total revenue and never declined below 75 percent except in the FY 1991/92. Thus, role of tax revenue in domestic resource is highly significant.

Figure 4.1

Composition of Tax Revenue and Non-Tax Revenue



Source: Table 4.3

In the figure 4.1, the multiple bar-diagram shows that the share of tax revenue is very high in comparison to the non-tax revenue. The amount of total revenue has grown in increasing trend from FY 1990/91 and the tax revenue has followed the path as well.

4.2.3 Composition of Tax Revenue

The contribution of tax revenue in the total revenue is significant from the very beginning. The major components of tax revenue are direct tax and indirect tax. Which are shown in table below:

Table 4.4

Contribution of Direct Tax and Indirect Tax in Total Tax Revenue

(FY1990/91 to FY2007/08)

(Rs. in Million)

Fiscal Year	Direct Tax	DT as % of TR	Indirect Tax	IDT as% of TR	Total Tax Revenue
1990/91	1369.7	16.75	6806.6	83.24	8176.3
1991/92	1595.2	16.15	8280.4	83.84	9875.6
1992/93	2036.2	17.45	9626.3	82.54	11662.5
1993/94	2855.3	18.57	12516.2	81.42	15371.5
1994/95	3849.3	19.57	15810.7	80.42	19660
1995/96	4655.5	21.48	17012.5	78.51	21668
1996/97	5340	21.86	19084.3	78.13	24424.3
1997/98	6187.9	23.85	19751.9	76.14	25939.8
1998/99	7516.1	26.14	21236.8	73.85	28752.9
1999/00	8951.5	27.00	24200.6	72.99	33152.1
2000/01	10159.4	26.14	28705.7	73.85	38865.1
2001/02	10597.5	26.94	28733.1	73.05	39330.6
2002/03	10105.8	23.72	32481.2	76.27	42587
2003/04	11894.6	24.70	36260.4	75.29	48155
2004/05	13071.8	24.16	41032.9	75.83	54104.7
2006/07	13968.1	24.32	43462.3	75.67	57430.4
2006/07	18980.3	26.68	52146.4	73.31	71126.7

2007/08	23087.8	27.1	62067.8	72.9	85155.5

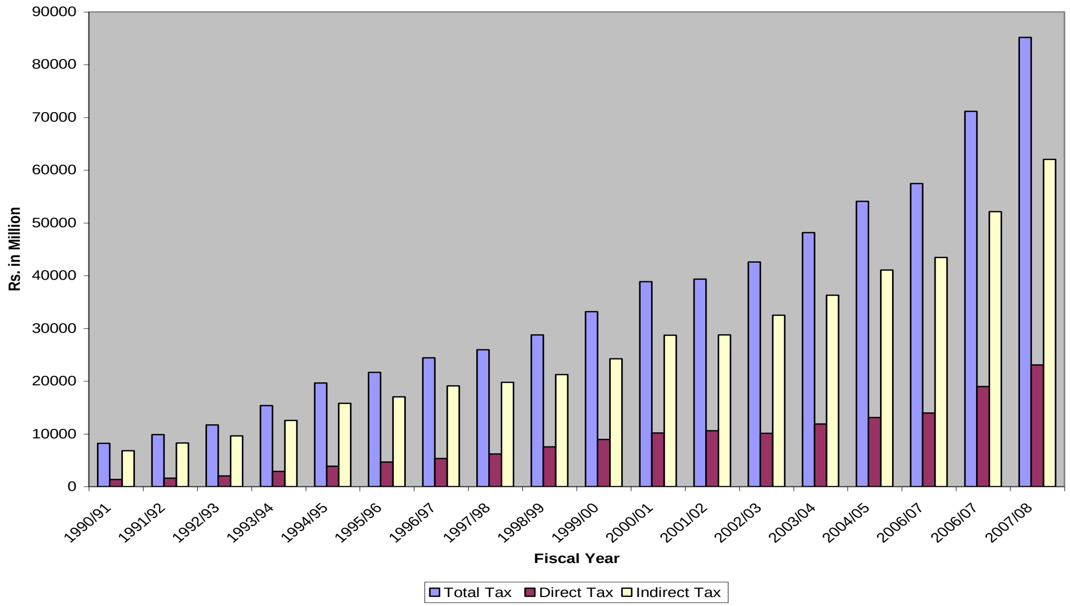
Source: Appendix I

The table 4.4 shows, there has been simultaneous increment in both direct tax and indirect tax in absolute term during the study period. The amount of tax revenue was Rs.8176.3 million in the FY 1990/91. In which, the share of direct tax was 16.75 percent whereas 83.24 percent of indirect tax. After that it reached to the amount of Rs.85755.4 million in the FY 2007/08. But the share of direct tax and indirect tax vary from year to year. The figure in the table shows the share of direct tax declined ranged from 27 percent in FY 1990/91 to 16.2 percent in FY 1991/92 and then again reached to 27.1 percent in FY 2007/08 increasing continuously except some fluctuation in few years.

Similarly, the share of indirect tax was 83.24 percent in FY 1990/91 and started to decline continuously except FY1991/92and FY1992/93 and reached FY72.9 percent in FY 2007/08. The share of indirect tax is in decreasing trend due to the adaptation of the liberalization policy by the nation. This has sought that country should try to mobilize the resources through direct taxation rather than indirect taxation since the country is already a member of WTO and SAFTA.

Figure 4.2

Trend of Tax Revenue



Source: Table 4.4

In figure 4.2 the multiple bar diagram shows the growing trend of total tax revenue. But in the case of components, direct tax has taken pace only in the last few years of study period. There is always the dominant role of indirect tax in the total tax revenue.

4.2.4 Contribution of Various Taxes in the GDP

During the study period the contribution of total revenue has increased from 9.2 percent of GDP in FY 1990/91 to 13.8 percent in FY 2007/08, this shows the increasing trend of revenue at a slower pace. Contributions of all kinds of taxes are in increasing trend though not satisfactory in some cases that are given below:

Table 4.5

1.2.1.1 Contribution of Various Taxes in the GDP

(FY1990/91 to FY 2007/08)

(Figures are in Percentage)

Fiscal Year	Total Rev.	Custom Duties	Sales Tax/ VAT	Excise Duties	Land Rev. & Reg.	Income Tax
1990/91	9.2	2.6	1.7	1.0	0.5	0.6
1991/92	9.3	2.3	2.0	1.0	0.4	0.6
1992/93	9.2	2.4	2.1	0.9	0.5	0.7
1993/94	10.2	2.7	2.4	0.8	0.4	1.0
1994/95	11.7	3.3	2.9	0.8	0.4	1.3
1995/96	11.7	3.1	2.7	0.8	0.4	1.4
1996/97	11.3	3.1	2.6	0.9	0.4	1.5
1997/98	11.4	2.9	2.5	1.0	0.3	1.7
1998/99	11.3	2.9	2.7	0.9	0.3	1.9
1999/00	11.7	3.0	2.8	0.9	0.3	2.0
2000/01	11.4	2.9	2.9	0.8	0.1	2.2
2001/02	11.3	2.8	2.7	0.8	0.2	2.1
2002/03	11.8	3.0	2.8	1.0	0.2	1.8
2003/04	12.0	3.0	2.7	1.2	0.3	1.9
2004/05	12.3	2.7	3.3	1.1	0.3	1.9
2005/06	11.4	2.4	3.4	1.0	0.3	1.8
2006/07	12.5	2.3	3.7	1.3	0.3	2.3

2007/08	13.8	2.7	3.8	1.4	0.4	2.4

Source: Appendix I

The contribution of custom duties was about 2.6 percent of GDP in the FY 1990/91 and in the succeeding year its contribution was not encouraging which was more or less 3 percent of GDP. In the FY 2007/08 its share in GDP was only 2.7 percent. The contribution of land revenue and registration was very low. The contribution of land revenue and registration remained about 0.4 percent of the GDP in most of the year. Table 4.5 shows; the major taxes that contributed significantly in the revenue are sales tax/VAT, exercise duty and income tax during the study period. Their contribution was 1.7, 1.0 and 0.6 percent of GDP in the FY 1990/91 and reached 3.8, 1.4 and 2.4 percent of GDP in FY 2007/07.

4.2.5 Composition of Indirect Tax

After the restoration of democracy in 1990, Nepal adopted the policy of liberalization and the concept of open economy then the share of sales tax and income tax rose significantly. After the introduction of VAT in Nepal in 1997, the resource mobilization through VAT became the backbone of the Nepalese economy.

Nepalese tax revenue mainly depends on taxes on international trade and sales tax on goods and services supplemented by tax on income and property to some extant. Nepalese tax structure is highly dependent on indirect tax. The composition of indirect tax is shown in table below:

Table 4.6

Composition of Indirect Tax

(FY1990/91 to FY 2007/08)

(Rs. in Million)

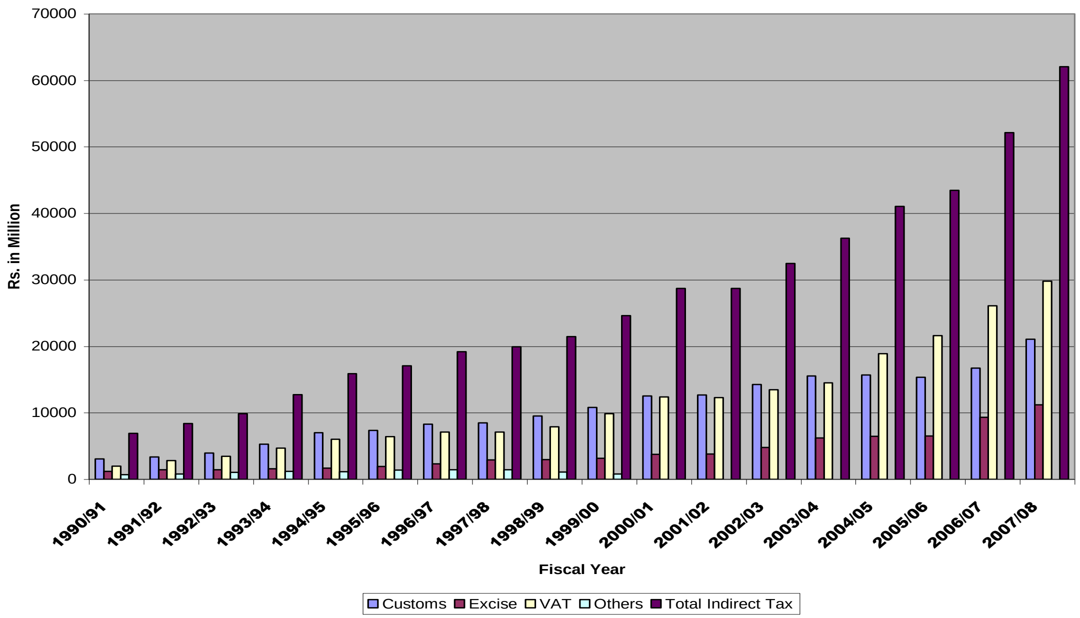
Fiscal Year	Customs	% of ID	Excise	% of ID	VAT	% of ID	Others	% of others	Total Indirect Tax
1990/91	3044.3	43.94	1200.3	17.33	1996	28.81	687.5	9.92	6927.6
1991/92	3358.9	40.04	1419.3	16.92	2836	33.81	774.4	9.23	8388.5
1992/93	3945.1	39.91	1452.6	14.69	3438	34.78	1049	10.61	9885.3
1993/94	5255.2	41.33	1592.3	12.52	4693	36.91	1173	9.23	12714.1
1994/95	7017.9	44.19	1675.5	10.55	6038	38.02	1150	7.24	15881
1995/96	7327.4	42.89	1945.9	11.39	6432	37.65	1378	8.07	17082.8
1996/97	8309.1	43.30	2302.1	12.00	7127	37.14	1453	7.57	19190.5
1997/98	8499.9	42.69	2886.5	14.50	7109	35.70	1416	7.11	19911.3
1998/99	9517.5	44.36	2952.5	13.76	7883	36.74	1104	5.14	21456.2
1999/00	10813.3	43.96	3132.7	12.74	9850	40.05	801.3	3.26	24597.3
2000/01	12552.1	43.73	3771.2	13.14	12382	43.14	0	0.00	28705.7
2001/02	12658.8	44.06	3807	13.25	12267	42.69	0	0.00	28733.1
2002/03	14236.4	43.83	4785.1	14.73	13460	41.44	0	0.00	32481.2
2003/04	15554.8	42.90	6226.7	17.17	14479	39.93	0	0.00	36260.4
2004/05	15701.6	38.27	6445.9	15.71	18885	46.03	0	0.00	41032.9
2005/06	15344	35.30	6507.6	14.97	21611	49.72	0	0.00	43462.3
2006/07	16707.6	32.04	9343.2	17.92	26096	50.04	0	0.00	52146.4
2007/08	21062.5	33.93	11190	18.03	29816	48.04	0	0.00	62068.2

Source: Appendix I

Table 4.6 shows the composition of indirect tax. The contribution of custom duties in indirect tax declined from 43.94 percent in FY 1990/91 to 33.93 percent in FY 2007/08. The share of custom duty has decreased mainly due to the low tariff rate and increment of direct tax. The sales tax/VAT has become an important source of overall tax revenue with increasing trend. The contribution of tax was increase from 28.80 percent in FY 1990/91 to 48.04 percent in FY 2007/08. The contribution of excise duty in indirect tax was decrease from 17.32 percent in FY 1990/91to 18.03 percent in FY2007/08.

Figure 4.3

Composition of Indirect Tax



The figure 4.3 shows the composition of indirect tax from FY 1990/91 to 2007/08. The space of VAT increased rapidly from the beginning and reached maximum in FY 2007/08. The contribution of customs in indirect tax was significant and is in increasing trend from beginning of the study period. The contribution of excise duty in indirect tax was low. However, it is also in increasing trend.

4.2.6. Contribution of Direct Tax

Nepalese tax revenue is mainly dependent on the indirect taxes such as tax on international trade and sales tax/VAT on goods and services. But in the total revenue the role of direct tax is also significant from the very beginning, which is shown in table given below:

Table 4.7
Contribution of Direct Tax
(FY1990/91 to FY2007/08)

Fiscal Year	Direct Tax	Direct Tax as % of Tax Revenue	Direct Tax as % of Total Revenue	Direct Tax as % of GDP
1990/91	1369.7	16.75	12.76	1.17
1991/92	1595.2	16.15	11.80	1.10
1992/93	2036.2	17.45	13.44	1.23
1993/94	2855.3	18.57	14.58	1.49
1994/95	3849.3	19.57	15.66	1.83
1995/96	4655.5	21.48	16.69	1.94
1996/97	5340	21.86	17.58	1.98
1997/98	6187.9	23.85	18.78	2.13
1998/99	7516.1	26.14	20.17	2.27
1999/00	8951.5	27.00	20.86	2.44
2000/01	10159.4	26.140	20.77	2.38

2001/02	10597.5	26.94	21.00	2.38
2002/03	10105.8	23.72	17.97	2.13
2003/04	11894.6	24.69	19.08	2.29
2004/05	13071.8	24.16	18.64	2.30
2006/07	13968.1	24.32	19.32	2.21
2006/07	18980.3	26.68	21.63	2.72
2007/08	23087.8	27.1	21.44	2.95

Source: Appendix I

The table 4.7 shows the contribution of direct tax in tax revenue, total revenue and GDP respectively. In the beginning of the study period i.e. in FY 1990/91 the amount of direct tax was Rs.1369.7 million. In the FY 1992/93 it increased by more than 4 times and the amount reached to Rs.236 million. Though its growth is not smooth in the early period, after FY 1991/92 the amount of the direct tax has grown significantly. In the FY 2007/08 it reached to Rs.23087.8 million.

Contribution of direct tax to tax revenue is varying from year to year. In FY 1990/91, direct tax had contributed 16.75 percent to the tax revenue and reached to 16.2 percent in FY 1991/92. But after the FY 1991/92, it grew to 27 percent in the FY 1999/00 and again it is declined in subsequent years. However, the contribution of direct tax to tax revenue is 27.1 percent in fiscal year 2007/08.

The share of direct tax to the total revenue is also increasing. In FY 1990/91 the share of direct tax to total revenue was 12.76 percent. It reached to minimum in the FY 1991/92 with 11.8 percent and again it began to increase with some fluctuation. Now, in FY 2007/08 the share of direct tax to total revenue is 21.44 percent.

The contribution of direct tax to GDP is in increasing trend from the very beginning. In the FY1990/1991 direct tax was 1.17 percent of the total GDP and it declined to 1.10 percent in FY 1991/92. But after the FY 1996/97 contribution of direct tax to GDP crossed the 1.98 percent and is now 2.95 percent of the GDP.

4.2.7. Composition of Direct Tax

In the Nepalese tax structure, the major components of direct taxes keep on changing from the beginning. But the major components of direct taxes are income tax, land tax and house and land registration tax. Until the FY 1993/94, vehicle tax was considered as a direct tax and from FY 1994/95 it has been classified under the indirect tax. The composition of direct tax is shown in table below:

Table 4.8

Composition of Direct Tax and Their Share in Direct Tax

(FY1990/91 to FY2007/08)

Amount in Rs. Million

Fiscal Year	Direct Tax	IT	IT as % of DT	Land Rev.	LR as %of DT	House & Land Reg.	HLR as % of DT	Others	Others as % of DT
1990/91	1369.7	746.2	54.47	82.2	6.00	456.6	33.33	0	0
1991/92	1595.2	855.1	53.60	64.9	4.06	567.3	35.56	0	0
1992/93	2036.2	1124.8	55.24	79.8	3.91	675.1	33.15	0	0
1993/94	2855.3	1824.3	63.89	63.8	2.23	769.3	26.94	0	0
1994/95	3849.3	2640.6	68.59	36.6	0.95	901.1	23.40	218.7	5.68
1995/96	4655.5	3205.4	68.85	14.2	0.30	1065.4	22.88	300.2	6.44
1996/97	5340	3829.4	71.71	9.5	0.17	1005.9	18.83	388.8	7.28
1997/98	6187.9	4499	72.70	3.8	0.06	1002.9	16.20	509.6	8.23
1998/99	7516.1	5646.5	75.12	0.8	0.01	995.5	13.24	654	8.70
1999/00	8951.5	6755.7	75.47	0.8	0.00	1012.5	11.31	780.7	8.72
2000/01	10159.4	9153.9	90.10	0	0	607.8	5.98	737.6	7.26
2001/02	10597.5	8903.6	84.01	0	0	1121.3	10.58	574.1	5.41
2002/03	10105.8	8132.2	80.47	0	0	1414.2	13.99	559.4	5.53
2003/04	11894.6	9504.4	79.90	0	0	1697.5	14.27	700.4	5.88
2004/05	13071.8	10456	79.98	0	0	1799.2	13.76	806.1	6.16
2006/07	13968.1	10933.6	78.27	0	0	2180.3	15.60	847.6	6.06
2006/07	18980.3	15730	82.87	0	0	2238.7	11.79	1011.6	5.32

2007/08	23087.8	19078	82.63	0	0	2940.7	12.74	1069	4.63

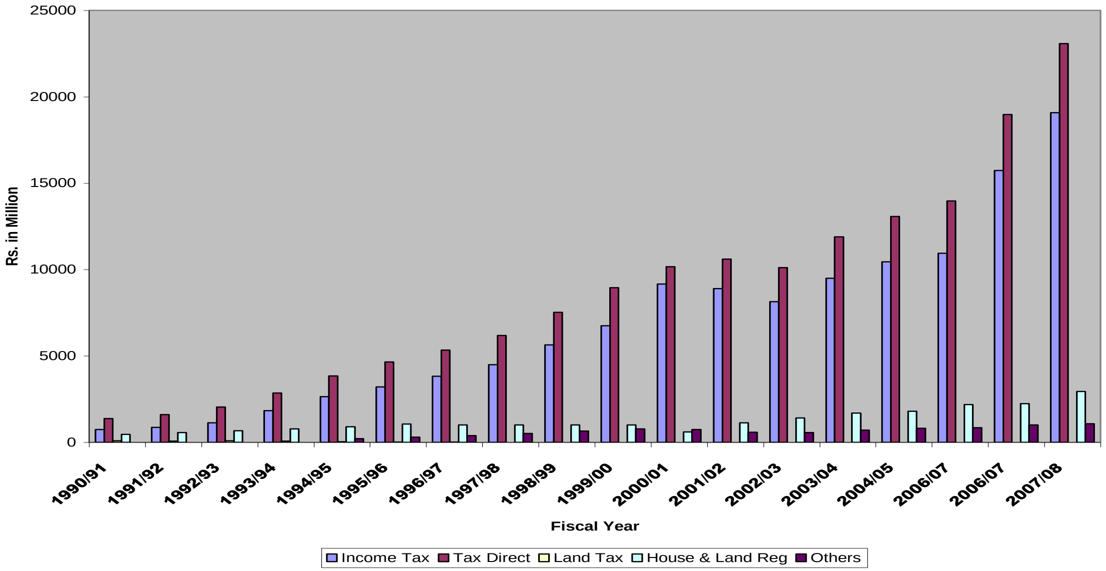
Source: Appendix I

The table 4.8 shows the different heads of the direct tax and their contribution to the direct tax In FY 1990/91 the share of income tax to direct tax was 54.47 percent then its share in direct become maximum i.e. 90.10% in 2000/01 In the FY 2006/07 the amount of income tax was Rs.19078 million which was 82.63 percent of the direct tax.

The contribution of land revenue declined sharply from the early period. But the contribution of house and land registration which was very low in the beginning, changed in the latter days. In the early years of the 1990s, the share of the house and land registration to direct tax highly increased and reached to 35.8 percent in FY 1991/92 but declined then after. It declined sharply again in the FY 2000/01 and then increased to 11.79 percent of the direct tax amounting Rs.2940.7 million in 2007/08.

Figure 4.4

Composition of Direct Tax (FY1990/91 to FY2007/08)



Source: Table 4.8

The figure 4.4 shows the composition of direct tax from the FY 1990/91 to 2007/08. The space of income tax increased rapidly from the beginning and reached maximum in the FY 2007/08. The contribution of house and land registration in direct tax was significant in the beginning of the study period. It was maximum in 1993/94 and minimum in 2000/01.

4.2.8 Share of Income Tax in the Total Revenue in Selected Countries

Modern income tax was first introduced by Britain as a temporary instrument to generate revenue required for the war finance. Now, the tax is major source of revenue in the developed as well as developing countries. The relative importance of tax revenue is shown by the adjoin table only of some selected countries.

Table 4.9

Share of Income Tax in the Total Revenue in Selected Countries

Country	**Taxes on Income, Profits, and Capital gains as % of Total Revenue (2005)**
USA	55
Australia	65
India	35
Pakistan	20
Sri Lanka	13
Switzerland	16
Nepal	11
Thailand	33
Malaysia	47
Peru	24

Source: World Development Indicator

Table 4.9 shows that the contribution of income tax to total tax revenue in Australia is highest which 65 percent of the total revenue were in 2005. Among the selected countries of the world, Nepal has the lowest contribution of income tax in the total revenue that was 11 percent in the year 2005.

In general, the bulk of the income tax revenue comes from the individual income tax in developed countries while corporate tax provides the bulk of the income tax revenue in the developing countries.

4.2.9 Contribution of Income Tax

Income tax was introduced in FY 1959/60 for the first time when it generated revenue of Rs.203 thousands. In FY 1962/63, income tax revenue increased to Rs.2 millions. Income tax was initially levied only on business income and salary. In the FY 1959/60 business tax provided about 80 percent of the total income tax revenue. The contribution of income tax on direct tax revenue, tax revenue, total revenue and GDP is shown in table below:

1.2.1.1.1 Table 4.10

Contribution of Income Tax as Percentage of Different Heads

(FY1990/91 to FY2007/08)

Fiscal Year	Income Tax(IT)	IT as a % of Direct Tax	IT as a % of Tax Revenue	IT as a % of Total Revenue	IT as a % of GDP
1990/91	746.2	54.47	9.126	6.95	0.64
1991/92	855.1	53.60	8.659	6.32	0.59
1992/93	1124.8	55.24	9.645	7.42	0.68
1993/94	1824.3	63.89	11.87	9.31	0.95
1994/95	2640.6	68.59	13.43	10.74	1.25
1995/96	3205.4	68.85	14.79	11.49	1.33
1996/97	3829.4	71.71	15.68	12.60	1.42
1997/98	4499	72.70	17.34	13.65	1.55
1998/99	5646.5	75.12	19.64	15.15	1.71
1999/00	6755.7	75.47	20.38	15.74	1.84
2000/01	9546.5	93.96	24.56	19.52	2.24
2001/02	9465.7	89.32	24.07	18.76	2.13
2002/03	8691.5	86.00	20.41	15.45	1.83
2003/04	10215.1	85.88	21.21	16.38	1.97
2004/05	11272.6	86.23	20.83	16.07	1.98
2006/07	11787	84.38	20.52	16.30	1.87

2006/07	16726.8	88.12	23.52	19.07	2.39
2007/08	20147	87.3	23.66	18.72	2.58

Source: Appendix I

Before 1994/95, the major components were corporate income tax, income tax from individuals and from remunerations. The corporate income tax included income tax from public enterprises, semi-public enterprises and private corporate bodies. Then the amount of income tax grew rapidly and reached to Rs.1824.5 million in the FY 1993/94, which was 63.9 percent of the direct tax, 11.9 percent of tax revenue and 1 percent of the GDP.

In the fiscal year 1994/95, the components of the income tax were again revised. They were corporate income tax, individual income tax, tax on house and land rent and the interest tax. Corporate income tax included government corporate, public limited corporate and private limited corporate where as individual income tax included the tax on the income from remuneration and business, industry and occupation. So that the amount of income tax increased to Rs.2823.5 million in FY 1994/95 form Rs.1824.5 million of previous year which was 73.4 percent of the direct tax, 14.4 percent of total tax revenue and 1.3 percent of the GDP.

Again in the FY 2002/03, the bases of income tax were revised. They are corporate income tax, tax on remuneration, income tax on investment, tax on windfall gain and others. The corporate income tax includes government corporate, public limited corporate, private limited corporate, personal or sole trading and other institutions. Similarly, the components of the income tax on investment are tax on lease or rent, interests, capital gains, dividends and other income from investment. In the FY 2007/08 the amount of income tax was Rs.20147 million which was 87.3 percent of the direct tax, 23.66 percent of the tax revenue, 18.72 percent of the total revenue and 2.58 percent of the GDP.

If we see the increasing trend of Income tax, it is most likely to surpass the custom duties in future and will be the second largest source of revenue whereas the VAT will be the first largest source. The contribution of income tax to direct tax was much lower in the early years of the study period. Income tax contributed only 9.9 percent of the direct tax in the FY 1990/91. Then after, it has been increasing continuously and rapidly. As a result, its share to direct tax has not decreased from 50 percent after 1980. In FY 2000/01, the share of income tax to direct tax was 89.7 percent while in FY 2001/02 it was 84 percent. This decrease in the share of income tax for the period from FY 2002/03 is due to the application of VDIS program in 2001. It had caused sharp increased in the income tax in 2001 and not in that extent after withdrawal of the VDIS in 2002. Also the land tax and house rent tax has been excluded recently from income tax. In the FY 2007/08 the contribution of income tax to direct tax has reached only 76.4 percent.

Recently, the income tax has been divided into corporate income tax remuneration tax, income tax on investments, and tax on windfall gains. Thus, the income tax is one of the prime sources of direct tax in Nepal. But the contribution of income tax to total tax revenue is still lower than the developed countries. The more the revenue generated from income tax, the more progressive and equitable the tax system will be.

4.2.10 Growth Rates of Total Revenue, Tax Revenue, Direct Tax and Income Tax

The growth rates of total revenue, tax revenue, direct tax and income tax is shown in table below:

Table 4.11

Growth Rates of Total Revenue, Tax Revenue, Direct Tax and Income Tax

(FY1990/91 to FY2007/08)

Figures in Percentage

Fiscal Year	Total Revenue	Tax Revenue	Direct Tax	Income Tax
1990/91	-	-	-	-
1991/92	25.94	20.78	16.46	14.59
1992/93	12.1	18.09	27.65	31.54
1993/94	29.26	31.8	40.23	62.19
1994/95	25.51	27.9	34.81	44.75
1995/96	13.5	10.21	20.94	21.39
1996/97	8.89	12.72	14.7	19.47
1997/98	8.44	6.2	15.88	17.49
1998/99	13.09	10.84	21.46	25.51
1999/00	15.15	15.3	19.1	19.64
2000/01	13.99	17.23	13.49	35.5
2001/02	3.17	1.2	4.31	-2.73
2002/03	11.47	8.28	-4.64	-8.66
2003/04	10.85	13.12	17.7	16.87
2004/05	12.5	12.31	9.9	10.01
2005/06	3.08	6.15	6.86	4.57
2006/07	21.35	23.85	35.88	43.87
2007/08	22.70	19.72	21.60	21.28
Average	14.76	15.03	18.61	22.19

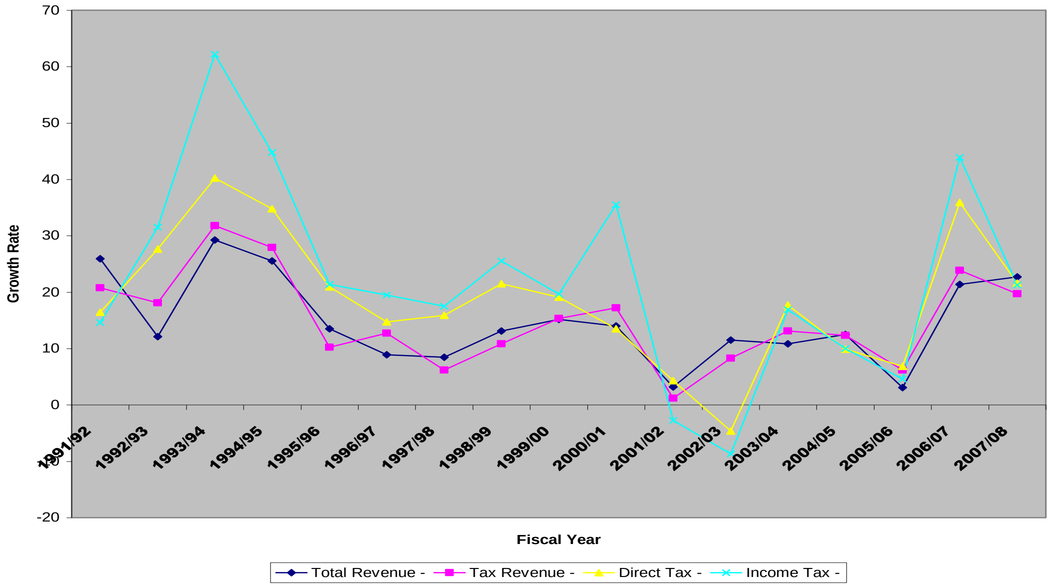
Source: Appendix III

Table 4.11 shows the growth rates of total revenue, tax revenue, direct tax and income tax from FY1990/91 to FY2007/08. The income tax increases by 22.19 percent in an average, which is maximum among all. The growth rate of income tax is followed by direct tax, which increases by 18.61 percent in an average. Total revenue and tax revenues increase by 14.76 and 15.03 percent respectively in an average under the study period.

Figure 4.5

Growth Rates of Total Revenue, Tax Revenue, Direct Tax and Income Tax

(FY1990/91 to 2007/08)



Source: Table 4.11

Figure 4.5 shows the growth rate of total revenue, tax revenue, direct tax and income tax from FY1990/91 to FY2007/08. Among all growth rate of income tax is maximum which is followed by direct tax. In FY2002/03, the growth rate of both income tax and direct tax was negative.

4.2.11 Composition of Income Tax

Until the FY 1993/94, income tax was divided in to corporate income tax, individual income tax and tax on remuneration. But, from the FY 1994/95, income tax revenue was divided into main four groups' viz., individual income tax, corporate income tax, interest tax and house and land rent tax. Of these taxes, corporate tax was collected from government corporations, public and private limited companies and partnership firms. Individual income tax was collected from individuals and proprietorship firms. Interest tax was collected from banks or finance companies that pay interest on all types of deposits and the house rent tax was levied on income obtained from the renting out the house and land in urban areas. Again from the FY 2002/03, it was revised and now the components of income tax are: corporate tax, tax on remuneration, tax on investment, tax windfall gain and others. The corporate income tax includes tax revenue from Government Corporation, Public Limited Corporation, Private Limited Corporation, personal or sole trading and other institutions. Similarly, the income tax on investment includes tax on lease or rent, interests.

Table 4.12

Composition of Income Tax (FY1990/91 to FY2007/08)

Fiscal	Sources of Income Tax

Year	Public Enterprises	Semi-Public Enterprise	Private Corporate Bodies	Individuals		Remuneration
1990/91	162.2	2.7	0	531.2		49.9
1991/92	171.1	5.3	6.1	617.9		54.7
1992/93	255.3	2.6	9.5	800.7		56.7
1993/94	534.1	2.1	19.7	843.2		83.8
	Corporate Income			Individual		Land & House Rent
	Govt. Corporate	Public Ltd. Companies	Private Ltd. Companies	Remuneration	Business/ Industry & Occupation	
1994/95	860.2	440.1	465.5	118.4	754.8	72.8
1995/96	1144.5	563.9	564.2	133.1	799.8	106
1996/97	1231.1	858.4	603.8	168.1	967.5	140.1
1997/98	1317.8	925.1	693.8	322.2	1239.8	187.1
1998/99	15526.5	1155	780.7	396.5	1787.8	204.2
1999/00	2198.8	1340	900.1	451.5	1865.1	251.2
2000/01	2928	1924	1134.2	597.3	1804.8	261.4
2001/02	1769.3	1412	1173.9	835.6	2897.4	348.2

Fiscal Year	Corporate Income Tax	Personal Income Tax	House & Land Rent Tax	Interest Tax	Total Income Tax
2002/03	3655.5	3177.1	381.7	1184.8	8059.5
2003/04	4838.6	3559.4	403.2	753.5	9514.5
2004/05	5327.3	3871.6	496.3	757.3	10452.5
2005/06	5395.7	4234.6	509	757	10896.3
2006/07	11515.8	2510.07	599.3	996.1	15140
2007/08	13181.6	2451	656	1125	17413.6

Source: Barsik Pratibedan

In the table 4.12 composition of income tax is shown from the FY 1990/91 to 2007/08. Initially, the income tax was given in gross amount but, later on, from the FY 1977/78 the category of the different heads under income tax was made. The bases of the income tax were revised twice then, in FY 1994/95 and FY 2002/03. This shows that government is trying to widen the tax base to increase the internal resource mobilization.

The table 4.12 shows that the contribution of different heads of income tax in the total amount of income tax from FY 1990/91 to 2007/08. In which the share of corporate tax is very high then individual tax comes in the second.

Table 4.13

Contribution of Different Heads to Income Tax

(FY1990/91 to FY 2007/08)

Fiscal Year	IT	Corporate Tax	% of IT	Individual Tax	% of IT	Remuneration	% of IT
1990/91	745.9	164.9	22.1	531.2	71.2	49.9	6.7
1991/92	855.4	182.9	21.4	617.9	72.2	54.7	6.4
1992/93	1124.8	267.4	23.8	800.7	71.2	56.7	5.0
1993/94	1824.5	555.9	30.5	1184.8	64.9	83.8	4.6

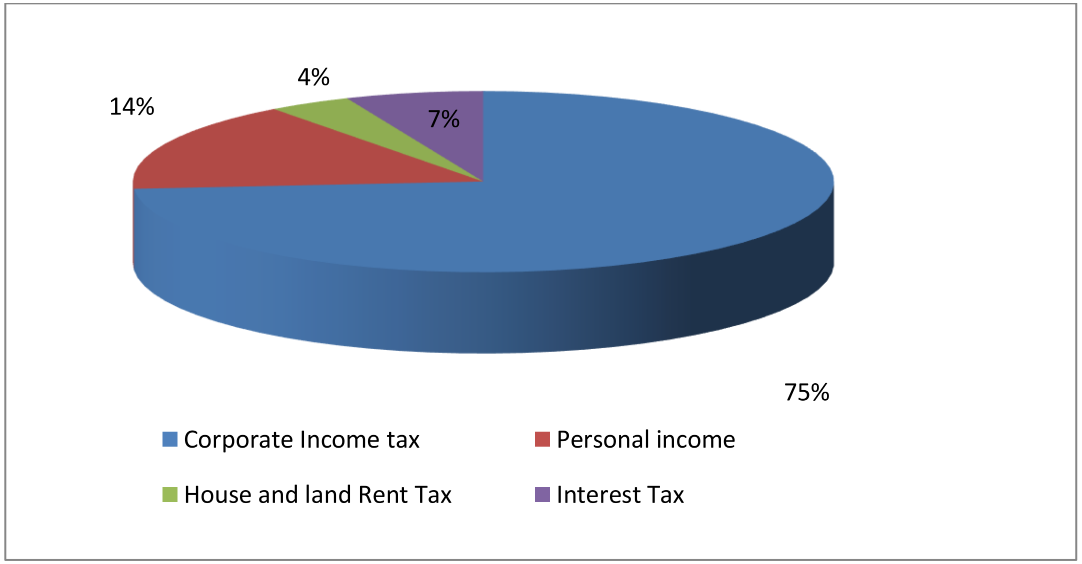
Fiscal Year	IT	% of IT	Corporate Tax	% of IT	Individual Tax	% of IT	H & L Rent Tax	% of IT	Interest Tax	% of IT
1994/95	2823.5	100	1765.8	62.5	873.2	30.9	72.8	2.6	111.6	4.0
1995/96	3431.4	100	2272.6	66.2	932.9	27.2	106.0	3.1	119.8	3.5
1996/97	4123.3	100	2693.3	65.3	1135.6	27.5	140.1	3.4	154.4	3.7
1997/98	4898.1	100	2936.7	60.0	1562.0	31.9	187.1	3.8	212.1	4.3
1998/99	6170.0	100	3462.2	56.1	2184.3	35.4	204.2	3.3	319.5	5.2
1999/00	7420.6	100	4438.4	59.8	2316.6	31.2	251.2	3.4	414.5	5.6
2000/01	9114.0	100	5986.5	65.7	2402.1	26.4	261.4	2.9	463.9	5.1
2001/02	8903.7	100	4355.2	48.9	3732.6	41.9	348.2	3.9	467.7	5.3

Fiscal Year	Corporate Income Tax	% of IT	Personal Income Tax	% of IT	House and Land Rent Tax	% of IT	Interest Tax	% of IT	Total Income Tax

2002/03	3655.5	45.35	3177.1	39.42	381.7	4.73	845.2	10.48	8059.5
2003/04	4838.6	50.85	3539.4	37.20	403.2	4.23	733.3	7.70	514.5
2004/05	5327.3	50.96	3871.6	37.03	496.3	4.74	757.3	7.24	10452.5
2005/06	5395.7	49.51	4234.6	38.86	509	4.67	757	6.94	10896.3
2006/07	11515.8	76.06	2510.07	16.57	599.3	3.95	996.1	6.57	15140
2007/08	13181.6	75.70	2451	14.1	656	3.8	1125	6.5	17413.6

Source: Barshik Pratibedan

Figure 4.6 Composition of Income Tax in FY2007/08



The figure 4.6 shows the composition of income tax at present in the FY 2007/08. The corporate tax has covered 74 percent of the total income tax and personal income tax comes to the second.

4.3 Productivity and Projection of Income Tax in Nepal

4.3.1 Introduction Productivity and Projection

Elasticity and buoyancy are two popular concepts, which are mostly used to measure the responsiveness of taxes in a tax system. The first one measures the automatic response of revenue to the change in income i.e. revenue increase excluding the effect of discretionary change in legal bases, rates, exemptions limit, administrative reforms etc. and the second measures the total response of tax revenue to change in income i.e. revenue increase including the effect of discretionary changes. Elasticity is a static concept where as buoyancy is a dynamic one (Timalsina, 2007: 96).

The elasticity refers to the total change in tax revenue excluding discretionary change, associated with a given percentage change in National Income (NI). Tax buoyancy refers to the ratio of total percentage change in the tax revenue including discretionary changes to a given percentage change in NI. If buoyancy is higher than elasticity, it signifies that discretionary changes can raise additional revenue and vice versa.

The response of tax revenue to changes in income has often been singled out as a vital ingredient in considering the criteria for a tax system in a developing country (Charles, 1972: 425). The ratio of percentage change in the income tax revenue to the percentage change in national income gives the buoyancy coefficient of an income tax under consideration. The term elasticity excludes the discretionary changes i.e. change in rates, bases, exemptions limit, administration reforms etc. The yield effects of normal improvements in administration unaccompanied by legal changes are thus included in this measurement of elasticity. Thus, elasticity is also regarded the method of measurement of automatic response of revenue to income changes.

4.3.2 Calculation of Elasticity and Buoyancy

Elasticity and buoyancy of income tax is calculated here including the data from the FY 1990/91 to FY2007/08. Also, the elasticity and buoyancy of income tax is calculated with respect to non-agriculture GDP as proxy base from the FY1990/91 to FY2007/08.

To calculate elasticity and buoyancy of income tax revenue, the relevant variables are given below:

Table 4.14

Total GDP, Non-agriculture GDP, Total Income Tax, Discretionary Change and Adjusted Income Tax Series (FY1990/91 to FY2007/08)

Amount Rs. in Million

Fiscal year	GDP	Non Agriculture GDP	Income Tax	Discretionary Change	Adjusted Income Tax
1990/91	116127	60759.3	746.2	56.4	746.2
1991/92	144933	79777.1	855.1	0	855.1
1992/93	165350	92259.9	1124.8	13.9	1110.9
1993/94	191596	111007	1824.3	342	1463.982
1994/95	209974	124405	2640.6	144.8	2002.854
1995/96	239388	142492	3205.4	420.3	2112.455
1996/97	269570	160785	3829.4	273.7	2343.313
1997/98	289798	177303	4499	391.8	2513.307
1998/99	330018	197645	5646.5	1601.2	2259.853
1999/00	366251	221120	6755.7	304.6	2581.872
2000/01	425454	269829	9546.5	889.8	3308.39
2001/02	444052	277962	9465.7	271.7	3186.229
2002/03	473546	300743	8691.5	420.5	2784.084
2003/04	517993	331868	10215.1	601.7	3079.389
2004/05	566579	367211	11272.6	1403.6	2975.055

2005/06	630301	418596.6	11787	850.5	2886.352
2006/07	696989	470167	16726.8	1130	3819.28
2007/08	78126	533848	20147	948	4228.4

Source: Economic Survey, Budget Speech and A Handbook of Government Finance Statistics

Table 4.15

Elasticity and Buoyancy of Nepalese Income Tax

(FY1990/91 to FY2007/08)

Statistics→ Income Tax	Estimate β	Standard Error of	R (Correlation Coefficient)	R^2 (Coefficient of Determination)	$\overline{R^2}$ (Adjusted R^2)	F-statistics	T-statistics
Buoyancy	1.776	.080	.985	.971	.969	494.998	22.249
Elasticity	0.827	0.087	0.926	0.857	0.847	89.727	9.472
Difference	0.949						

The responsiveness of any tax system directly relies of the economic structure or bases of that particular country. In this context, base elasticity is highly useful. Here base elasticity and base buoyancy of income tax is calculated taking non-agriculture GDP as the proxy base since the income from the agricultural income is out of tax net.

Table 4.16

Base Elasticity and Base Buoyancy of Nepalese Income Tax

(FY1990/91 to FY2007/08)

Statistics→ Income Tax	Estimated B	Standard Error	R (Correlation Coefficient)	R^2 (Coefficient of Determination)	$\overline{R^2}$ (Adjusted R^2)	F-statistics	T-statistics
Buoyancy	1.583	0.069	0.986	0.972	0.970	519.39	22.790
Elasticity	0.741	0.075	0.931	0.867	0.858	97.410	9.870
Difference	0.842						

4.3.3 Interpretation

The calculation of elasticity and buoyancy of income tax with respect to GDP as well as base elasticity and base buoyancy of income tax with respect to proxy base (non-agriculture GDP) is given above. It consists the period of FY 1990/91 to FY2007/08.

The elasticity of income tax 0.827 is extremely low in comparison with buoyancy 1.776 in the period 1990/91 to 2007/08, which is shown in the above Table. Thus, the income tax is less responsive to change in GDP. The buoyancy of income tax with respect to GDP is 1.776, which means that one percent change in GDP cause 1.776 percent change in income tax yield. This indicates that the government has concentrated more on introducing various discretionary measures rather than broadening the income tax base. Such an income tax structure is not conductive to support growing development activities because it needs frequent changes in the tax rates through legislative procedures. It creates the complication of mobilizing additional revenue. It also adds uncertainty to the existing environment. Exemption of agriculture income from income tax net, continuous decreasing tax rates and more or less constant tax base, low valuation of imported goods, which further lowers the income tax, complication in identifying the income from service sectors etc. are the main reasons of low income elasticity in Nepalese tax system. The inelastic nature of income tax indicates that is still potentiality of raising the income tax through widening tax base, certain administration reforms and may be raising tax rates.

The difference between buoyancy and elasticity coefficients is utilized to know how much percentage change in revenue by one percent change in GDP due to discretionary changes. The higher difference means the high possibility of raising the tax collection through discretionary changes. The difference between buoyancy and elasticity is 0.949.

The values of base elasticity and base buoyancy of Nepalese income tax during FY 1990/91 to 2007/08 are 0.741 and 1.583 respectively. This shows the income tax is inelastic with respect to proxy base also. The low value of base elasticity and base buoyancy coefficient of income tax to base indicates a poor relationship between base and tax. That is change in base only cannot bring desired change in the tax revenue and some other factors are also responsible which are to be applied to bring change in the tax revenue structure. The difference between base elasticity and base buoyancy is 0.842.

The values of correlation coefficient (R) in all cases are more than 0.90 shows that there is strong positive relationship between related dependent and independent variables. The coefficient of determination (R^2) measures the goodness of fit of regression. The R^2 for income elasticity is 0.857 and for buoyancy is 0.971, which indicates that the association between GDP and income tax holds good. Similarly, the value of R^2 in case of base elasticity and base buoyancy are also significantly high. Here R^2 measures the variation in income tax revenue due to the variation in GDP. The value of R^2 is comparatively greater in the case of buoyancy than in the elasticity of relevant variables.

To check whether the variation is due to variation in GDP and in GDP originating from non–agriculture sector, F-test is utilized. The tabular value of F statistics for given degree of freedom at 1 percent level of significant is less than the calculated value in all cases. Since the calculated value is highly significant, the relationship is reliable. Similarly, in case of base elasticity, the calculated value of F is significantly higher than the tabulated value of F statistics. Thus it can be confirmed that the variation in income tax revenue is mainly caused by the variation in GDP as well as GDP originating from non-agriculture sector.

The values of t-statistics, which gives the significance of parameters, are also significant at 1 percent level. The value of d-statistics in all cases are less than 1, this shows that there is positive autocorrelation at given degree of freedom and significant at 1 percent level of significance.

4.3.4 Projection of Income Tax in Nepal

Data about projection of income tax in coming year are not available. The availability of date till 2006/07 only has been major hardly in making projection.

Despite the serious gaps in availability of information for projections as attempt has been made in this study to project income to revenue of Nepal till 2016/17. Such projection should be taken as broad estimation only in view of series limitations. Additional torn effects resulting from policy changes, administrative action and changes in the behavior of taxpayers have not been disaggregated. The most important thing is that we are calculating the historical trend line of total income tax for period of past 18 years (i.e. FY 1990/91 to 2007/08 using secular trend.

4.3.4.1 Calculation of Trend Line

Table 4.17

Calculation of Trend Line of Income Tax (FY1990/91 to FY2007/08)

Amount Rs. in Million

Fiscal Year (x)	Income Tax (Y)	X= (x-1998/99)

1990/91	746.2	-8
1991/92	855.1	-7
1992/93	1124.8	-6
1993/94	1824.3	-5
1994/95	2640.6	-4
1995/96	3205.4	-3
1996/97	3829.4	-2
1997/98	4499	-1
1998/99	5646.5	0
1999/00	6755.7	1
2000/01	9546.5	2
2001/02	9465.7	3
2002/03	8691.5	4
2003/04	10215.1	5
2004/05	11272.6	6
2005/06	11787	7
2006/07	16726.8	8
2007/08	20147	9

Source: Appendix I

We have,

a = 6401.894

and b = 891.873

Then the trend line is:

$Y_c = 6401.894 + 891.873\ X$

4.3.4.2 Calculation of Trend Values of Income Tax

The trend values can be obtained by substituting the respective values of X in the trend line i.e. $Y_c = 6401.894 + 891.873\ X$. The computation of trend values is shown in table below:

Table 4.18

Computation of Trend Values of Income Tax (FY1990/91 to FY 2007/08)

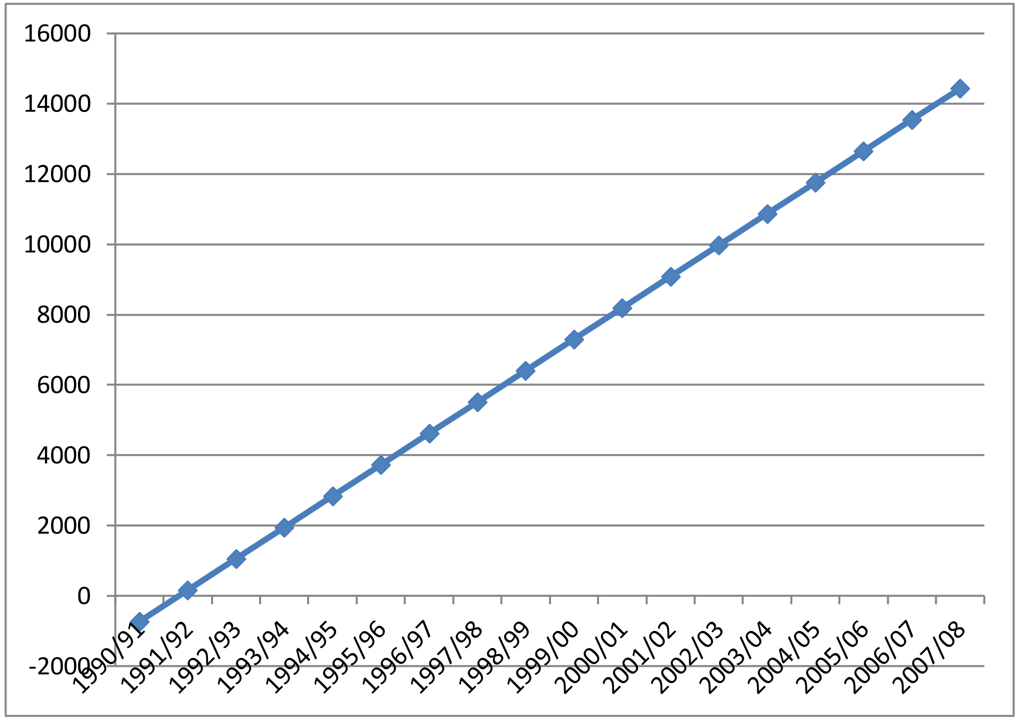
Amount Rs. in Million

Fiscal Year	Income Tax(Y)	X	a	b	Y_c
1990/91	746.2	-8	6401.894	891.873	-733.09
1991/92	855.1	-7	6401.894	891.873	158.783
1992/93	1124.8	-6	6401.894	891.873	1050.656
1993/94	1824.3	-5	6401.894	891.873	1942.529
1994/95	2640.6	-4	6401.894	891.873	2834.402
1995/96	3205.4	-3	6401.894	891.873	3726.275
1996/97	3829.4	-2	6401.894	891.873	4618.148

1997/98	4499	-1	6401.894	891.873	5510.021
1998/99	5646.5	0	6401.894	891.873	6401.894
1999/00	6755.7	1	6401.894	891.873	7293.767
2000/01	9546.5	2	6401.894	891.873	8185.64
2001/02	9465.7	3	6401.894	891.873	9077.513
2002/03	8691.5	4	6401.894	891.873	9969.386
2003/04	10215.1	5	6401.894	891.873	10861.26
2004/05	11272.6	6	6401.894	891.873	11753.13
2005/06	11787	7	6401.894	891.873	12645.01
2006/07	16726.8	8	6401.894	891.873	13536.88
2007/08	20147	9	6401.894	891.873	14428.75

Figure 4.7

Computation of Trend Values of Income Tax



Computation of trend values of income tax is shown in above table. The trend value of income tax is also in increasing trend and its value in FY 2007/08 was Rs14428.75million.

4.3.4.3 Trend Analysis of Income Tax in Nepal

The trend analysis of income tax in Nepal is shown in table below:

Table 4.19

Trend Analysis of Income Tax in Nepal

(FY 1990/91 to FY2007/08)

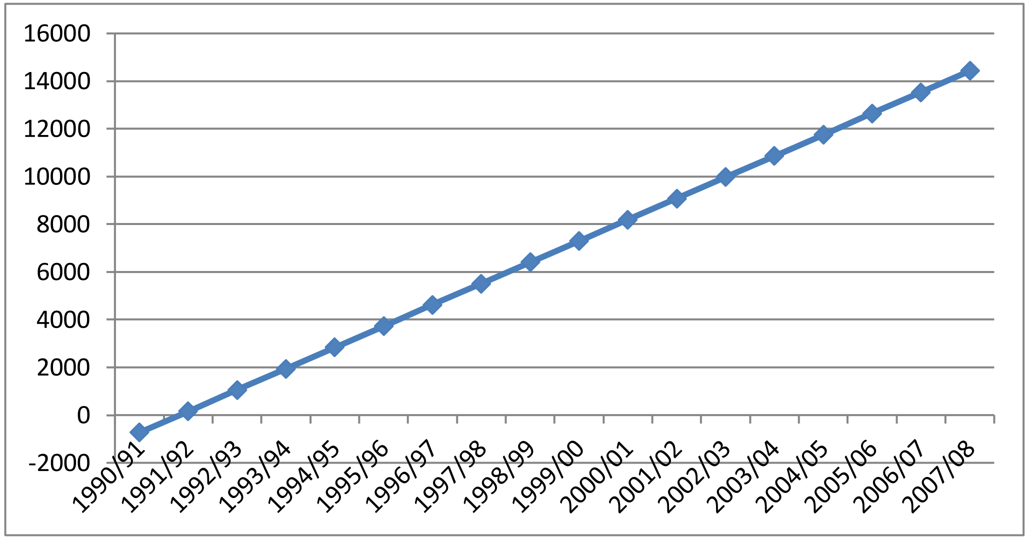
Amount in Rs. Million

Fiscal Year	Income Tax (Y)	Trend Value (Y_c)	Variation ($Y-Y_c$)
1990/91	746.2	-733.09	1479.29
1991/92	855.1	158.783	696.317
1992/93	1124.8	1050.656	74.144
1993/94	1824.3	1942.529	-118.229
1994/95	2640.6	2834.402	-193.802
1995/96	3205.4	3726.275	-520.875
1996/97	3829.4	4618.148	-788.748
1997/98	4499	5510.021	-1011.021
1998/99	5646.5	6401.894	-755.394
1999/00	6755.7	7293.767	-538.067
2000/01	9546.5	8185.64	1360.86
2001/02	9465.7	9077.513	388.187
2002/03	8691.5	9969.386	-1277.886
2003/04	10215.1	10861.26	-646.159
2004/05	11272.6	11753.13	-480.532

2005/06	11787	12645.01	-858.005
2006/07	16726.8	13536.88	3189.922
2007/08	20147	14428.75	5718.25

Figure 4.8

Trend Analysis of Income Tax in Nepal



From Table 4.19 and figure 4.8 it is cleared in trend of income tax there also exist cyclical variations. As per the trend of income tax, it should grow by the rate of Rs 891.894 million per year, But during the reference period 1990/91 to 2007/08, it is not found that the income tax is growing as per its growth rate. In FY 1990/91 income tax was collected amounting Rs. 746.2 million where -733.09 million should be collected.

In FY 1991/92, the income tax amounting RS. 855.1 million was collected which was Rs. 317 million more than its trend value. In FY 1993/94, 1994/95, 1995/96, 1996/97, 1997/98, 1998/99, 1999/00, there was negative collection variation. In FY 2000/01 and FY

2001/02, there was positive variation in income tax collection. There was again negative variation of 1277.886, 646.159, 480.532 and 858.005 million respectively in FY 2002/03, 2003/04, 2004/05 and 2005/06, and there was Rs. 5718.25million excess collection of income tax in FY 2007/08.

4.3.4.4 Future Projection of Income Tax in Nepal

The projection of income tax for coming ten years i.e. FY 2007/08 to FY 2016/17 is shown in table below:

Table 4.20

Projection of Income Tax in Nepal (FY 2007/08 to 2016/17)

Amount Rs. in Million

Fiscal Year	X	a	b	Y_c
2007/08	9	6401.894	891.873	14428.751
2008/09	10	6401.894	891.873	15320.624
2009/10	11	6401.894	891.873	16212.497
2010/11	12	6401.894	891.873	17104.37
2011/12	13	6401.894	891.873	17996.243
2012/13	14	6401.894	891.873	18888.116
2013/14	15	6401.894	891.873	19779.989
2014/15	16	6401.894	891.873	20671.862
2015/16	17	6401.894	891.873	21563.735
2016/17	18	6401.894	891.873	22455.608

Figure 4.9

Projection of Income Tax in Nepal

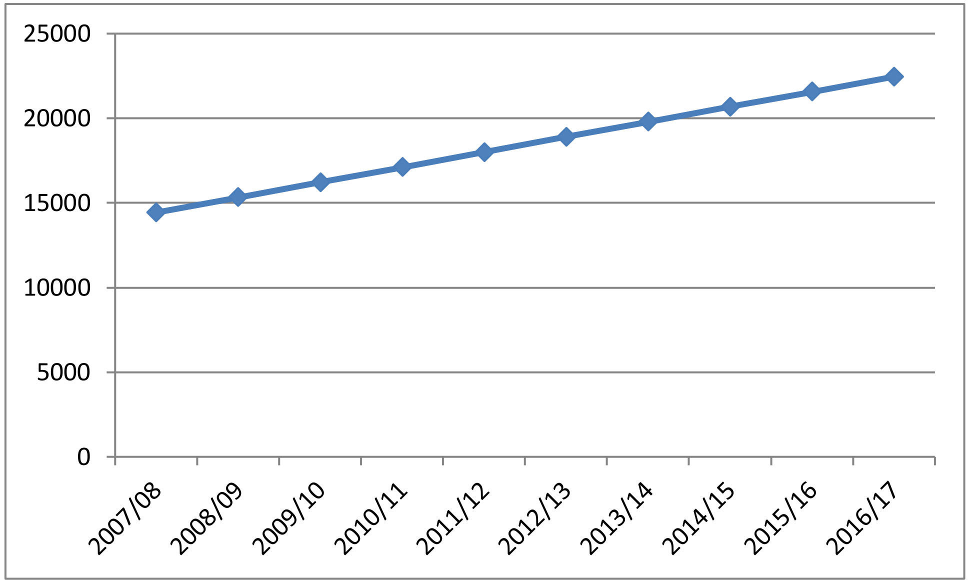


Table 4.20 and figure 4.9 refers the projection of income tax collection for the FY2007/08 to FY2016/17. As per the calculated growth rate, the income tax collected will increase by Rs. 891.873 million per year. In FY 2007/08 Rs. 14428.751 million income taxes will be collected. Likewise in FY 2011/12, income tax amounting Rs. 17996.243 million and in FY 2016/17 income tax amounting Rs. 22455.608 million will be collected.

4.4 Major Findings

The major findings of this study are summarized as follows:

- Resource gap is taken to be the difference between government expenditure and revenue. The resource gap has been increased from Rs 12819 million in FY 1990/91 to Rs 53727.4 million in FY 2007/08, which indicates the poor performance of domestic resource mobilization.
- Tax effort ratio measures the country's economic performance. In Nepal, the contribution of tax revenue to GDP was 10.1 percent and per capita income was only $ 270 in 2005 now is $ 472, which was lowest among the SAARC countries. In USA contribution of tax to GDP was 11.20 during the same period and its per capita income was $ 41440. Though the tax effort ratio is to some extent equal, its amount is very high because of its high GDP.
- Government revenue is the composition of tax revenue and non-tax revenue. There is dominant share of tax revenue in Nepalese government revenue. The contribution of tax revenue to government revenue shows the fluctuating trend as it had contributed 76.20 percent in FY 1990/91, 73.08 percent in FY1992/93 and 79.12 percent FY 2007/08.
- Nepalese tax revenue is the composition of direct tax and indirect tax revenue. There is dominant role of indirect tax. The contribution of direct tax and indirect tax revenue were 16.75 percent and 83.24 percent respectively in FY 1990/91, which contributed 27.1 and 72.9 percent in FY 2007/08.
- Among the various sources of government revenue, custom duties, VAT, income tax and excise duties are the major sources of government revenue. Income tax has occupied third position at present on the basis of its contribution. The contribution of income tax in increasing trend, which shows the bright future of income tax.
- The direct tax consists of income tax, land revenue, house and land registration and others. In the FY 1990/91, the income tax was Rs. 746.2 million and the land revenue was Rs.82.2 million. But in the succeeding fiscal year the amount of land revenue ahs declined and vanished at present. The share of income tax is appeared as the dominant source of direct tax with the amount

of Rs.19078 million contributing 82.63 percent in the direct tax in the FY 2007/08. Income tax has contributed 23.66 percent to the total tax revenue, 18.72 percent to the total revenue and 2.58 percent in the GDP in the FY 2007/08.

- The contribution of income tax on total tax revenue, GDP and total revenue is in increasing trend. Its contribution was 9.12, 6.95 and 0.64 percent in tax revenue, total revenue and GDP respectively in FY 1990/91, which increased to 23.66, 18.72 and 2.58 percent in FY 2007/08.
- Income tax is the composition of corporate income tax, personal income tax, and investment income tax. Corporate income tax is collected from government corporations, public and limited, partnership firms. Individual income tax is collected from remuneration and industry, business, profession. Invested income tax is collected from dividend, interest, royalty, rent etc.
- Within the income tax there is the dominant role of corporate income tax and it is in decreasing trend and it was 75.7 percent of income tax in FY 2007/08. The contribution of personal income tax, house and land rent tax and interest tax was14.1, 3.8, and 6.5 percent respectively.
- The measurement of elasticity and buoyancy of income tax gives the responsiveness of income tax in the tax system. The elasticity measurement of income tax in the period of FY 1990/91 to FY 2007/08 is 0.827; this shows the income tax is inelastic. The buoyancy greater than unity; 1.776 implies that the income tax is buoyant. The value of correlation coefficient greater than 0.9 shows there is strong positive relationship between income tax and GDP. Value of R^2 for elasticity and buoyancy are greater than 0.75 implies dependent variable is well explained by the independent variable.
- Since the income tax is collected from non-agriculture sector only, the base elasticity and base buoyancy have also calculated taking non-agriculture GDP as independent variable taking time from FY 1990/91 to FY 2005/06. The value of elasticity is low 0.741 and buoyancy is 1.583 with strong positive correlation between the variables.

- It is cleared in trend of income tax there also exist cyclical variations. As per the trend of income tax, it should grow by the rate of Rs 891.894 million per year, But during the reference period 1990/91 to 2007/08, it is not found that the income tax is growing as per its growth rate. In FY 1990/91 income tax was collected amounting Rs. 746.2 million where Rs. -733.09 million should be collected.
- As per the calculated growth rate, the income tax collected will increase by Rs. 891.873 million per year. In FY 2007/08 Rs. 14428.751 million income taxes will be collected. Likewise in FY 2011/12, income tax amounting Rs. 17996.243 million and in FY 2016/17 income tax amounting Rs. 22455.608 million will be collected.

CHAPTER - V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Nepal is one of the developing countries with $472 of per capita income and about 30 percent of total population lies below poverty line. So, Nepal needs huge amount of resources for economic development. Despite the various measures adopted by the government to boost the revenue collection, there is still a substantial resource gap between expenditure and revenue.

Because of increasing gap between expenditure and revenue collection, Nepal has to heavily depend upon both external as well as internal debt to meet the budget deficit. Unfortunately, the dependency is still in increasing which is undesirable for the economy. This scenario emphasizes for the mobilization of financial resources through income tax.

Tax is the compulsory payment to the government from a person according to now. Tax is the contributed to the government without expectation of the direct in the board since there are two types of taxes direct and indirect tax. Income tax, property tax, vehicle tax, house and land tax, contract tax, gift tax, interest tax etc. Are the example of direct tax and export/ import duty, excise duty, value added tax, sales tax, entertainment tax, hotel tax etc. are the example of indirect tax. Nepalese tax revenue is the composition of direct tax revenue.

The idea of introduction income tax, in Nepal originated along with the first budget on 2008 (1952). Then the first elected government introduced "Business profit and remuneration tax. Act 2017" to impose income tax on remuneration and business profit in Nepal. Business profit and remuneration tax act. 2017 had so narrow average that income tax was imposed only on business, profit and remuneration. It was replaced by the Nepal income tax act 2019 (1962) after two year. After the income tax 2010 were enacted with the view of implementation the objective of the income tax act 2019 was incapable in fulfilling the needs of the time, it was replaced by another income tax act 2031 (1974). In the causes of development and modernization of income been enacted. Similarly, the new income tax rules 2059 have also been enacted for effective implementation if the objective of the act.

Government revenue is the composition of tax revenue and nontax revenue. There is dominant share of tax revenue in Nepalese government revenue. Nepalese tax revenue is the composition of direct tax and indirect tax revenue. There is dominant role of indirect tax. Among the various sources of government revenue, custom duties, VAT, income tax excise duties are the major source3s of government revenue the basis of its contribution. The contribution of income tax is in increasing trend, which shows the further of income tax.

The need for mobilization of financial resources has been growing rapidly since planned development errors began in Nepal. This need has been specially pronounced the urgent for domestic resource mobilization. The success of development efforts of any country depends on it’s ability to mobilize additional internal resources to finance regular and development expenditure. Tax is considered safer and better means for the mobilization of additional financial resources as compared to other internal and foreign resource as compared to other internal foreign source of defect financing. Income tax is any of the major components in total tax revenue that playas a vital role in internal resources mobilization.

To fulfill the general objective of this study different sources of data are use to find out the accurate and actual conclusion. Mainly the secondary data are collected from economic survey of different fiscal year; published by ministry of finance Nepal government annual report published by Inland revenue department and other publicities. By analyzing the Secondary data it is found that government expenditure is in increasing trends each and every year on the other hand government recipes also increase in resources mobilization. But the expenditure is more than the receipts in each an every year. So there is deficit budget is every year the sources of government receipts are mainly sources government revenue and foreign grants. Foreign is not better sources as receipts, it is not sure in every year. So, the government revenue is better sources of government receipts. The government collects revenue from tax & non-tax revenue. Tax revenue is very important sources of government revenue. Tax revenue includes tax from customs, product of goods & services, Land revenue & registration, Income tax, tax on property profit etc.

Extremely limited tax base, low tax elasticity, relatively higher tax rates, poor voluntary compliance, ineffective tax administration, growing arbitration in assessment, rigid and incomprehensive tax laws and regulations, and numerous tax shelters are the main problems of Nepalese tax system. The problems of taxation differ with respect to individual taxes. The problems of income tax are broadly categorized into three different heads viz. administrative problems, legal problems and structural problems. These three categories of problems are major hardly in resource mobilization through income tax.

5.2 Conclusion

The study on income tax collecting the data from the FY 1990/91 to FY 2007/08 shows that the income tax is very important source of revenue. Its contribution in the total revenue is in increasing trend. The timely changes policies with respect to income tax are very important in the collection of income tax. The future projection of income tax shows the bright future of income tax in government revenue. But the calculation of elasticity and buoyancy of income tax shows the income tax is buoyant rather than elastic. This implies that the role of discretionary power is significant in the collection of income tax.

There are still some problems of resource mobilization through income tax. However, we can solve these problems by the collective effort of people, tax officers, political parties and government. If we solve the problems of income tax in time, no one can deny the fact that income tax is the major tool of financial resource mobilization in Nepal.

5.3 Recommendations

On the basis of above analysis and conclusions, the following specific suggestions have been recommended for the effective and efficient mobilization of additional financial resources through income taxation.

- The growing problem of resource gap in Nepalese finance should be tackled with significant reduction in government expenditure (especially regular expenditure) by utilizing natural resources base effectively and mobilizing additional financial resources internally to meet resource requirements rather than opting for foreign sources of deficit financing.
- As Nepalese revenue structure is heavily dominated by indirect taxes that occupying a share of more than three fourth in total tax. It is necessary to increase the share of direct tax through effective and efficient income taxation.

- Including non-professional agricultural income also within the grip of tax after providing certain exemption should further widen the coverage of income tax. Capital gains and dividends should be fully taxed instead of present partial taxation at present.
- Procedure for income assessment should be simplified. Complex legal formalities and delays in assessment should be avoided.
- A nationwide campaign should be launched to inform and explain tax rules and regulations, tax programs and benefits of paying tax with a view of stimulating public to pay taxes through the media o f radio, television, newspapers and special programs in the educational institutions and public places.
- Account based taxation and self-tax assessment system should be encouraged to make it revenue productive and taxpayer friendly.
- Effective and efficient two-way information system between taxpayers and tax authorities should be developed and maintained. Tax administration should posses a multiple sources information system.
- Income tax evasion and avoidance should be minimized enforcing heavy fines and penalties, controlling widespread illegal business activities and increasing administrative efficiency of the tax authorities and through the awareness programs among taxpayers.
- Up to date record of existing as well as potential taxpayers should be kept. Programs should be formulated and implemented to locate new group of taxpayers. Coordination with other departments and should be developed to find the income earning group.

BIBLIOGRAPHY

Acharya, S. (1994). *Income Taxation in Nepal: A Study of Its Structure, Productivity and Problems.* Kathmandu: An Unpublished M.A. Thesis, submitted to CEDECON, T.U.

Adhikary, R.P. (1995). "Elasticity and Buoyancy in Nepal*" Economic Review.* An Occasional Paper, NRB, No. 8.

Agrawal, G.R. (1978). *Resource Mobilization for Development: The Reform of Income Tax in Nepal. CEDA, T.U., Kathmandu.*

———*(1979).* "Role of Income Tax in Nepal's Tax Structure*" The Economic Journal of Nepal.* Vol. 2, No. 2, CEDCON, T. U.

——— *(1980).Resource Mobilization in Nepal*. CEDA, T. U., Kathmandu.

Amatya, S.K. (2004). *Taxation in Nepal, Income Tax, Property Tax, and Value Added Tax.* Kathmandu: M.K. Publishers.

American Economic Association (1955). *Reading in Fiscal Policy.* London: Arther Smiths and Keith Butters, George Allen and Irwin.

Bajgain, B.B. (2005*). A study on Income Tax: Trend Analysis and Projection.* Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U.

Baral, D.R. (2004). *Study on Internal Resource Mobilization Through VAT in Nepa*l. Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U.

Bhandari, Keshav Kumar (2004). *Inland Revenue Mobilization in Nepal: with special Reference to Income Tax and VAT*. Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U.

Bhandari, L. (2007). *Income Taxation in Nepal: Analysis of Structure and Problems.* An Unpublished M.A. Thesis, submitted to CEDECON, T.U. Kirtipur, Kathmandu.

Bird, R.M. & Oliver, O. (1967). *Readings on Taxation in Developing Countries.* Maryland: The John Hopkins University Press Baltimore.

Bird, R.M. (1974). *Taxing Agriculture Land in Developing Countries.* Cambridge, Harvard University Press.

——— (1970). *Taxation and Development (Lesson from Colombian Experience).* Cambridge, Massachusetts: Harvard University Press.

——— (1992). *Improving Tax Administration in Developing Countries*. IMF, Washington D.C.

Bista, B.G. (1986). *Government Finance in Nepal.* Kathmandu: Laligurans Prakashan.

Bonis, V.D. (1997). *Regional Integration and Factor Income Taxation*. IMF Working Paper.

Dhakal, K.D. (2009). *Tax Laws and Planning.* Kathmandu.: An Unpublished Hand Book.

Dahal, M.K. (1983). "Determinants of Government Revenue Share: A Case Study of Nepal" *The Economic Journal of Nepal*. Vol. 6, No. 4, CEDECON. T.U.

——— (1984). "Built-in-flexibility and Sensitivity of Tax Yields in Nepalese Tax System" *The Economic Journal of Nepal*. CEDECON,T.U., Vol. 7, No. 2, April-June.

——— (1993).*The Future of Nepalese Economy.* NEFAS/FES, Kathmandu.

——— (1999).*The Development Challenges of Nepalese Economy.* NEFAS/FES, Kathmandu.

——— (2000). "Measuring the Responsiveness and Productivity of Tax Yields, a Survey of Contemporary Approaches", *Economic Journal of Development Issues*.Patan Multiple Campus, Vol. 1, No. 2.

——— (2002). "Improving Tax System in Nepal: Agenda for Reforms", *Economic Journal of Development Issues*, Patan Multiple Campus, Vol. 1, No. 3.

Dulal, R. (2004). *Income Taxation in Nepal: A Study of Its Structure and Contribution to Revenue Generation.* Kathmandu: An Unpublished M.A. Thesis, Submitted to CEDECON, T.U.

Easlerly, W. & Sergio, R. (1992). *Marginal Income Tax Rates and Economic Growth in Developing Countries*. IMF Working Paper.

Gautam, G.R. (2006). *Income Tax in Nepal : Analysis of Exemptions and Deductions.* Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U.

Gautam, K.R. (2004). *Contribution of Income Tax to National Revenue of Nepal*. Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U..

Goode, R. (1986). *Government Finance in Developing countries.* New Delhi: Tata McGraw-Hill Publishing Company Limited, India.

Gujarati, D. (2003). *Basic Econometrics.* 4th ed., New Delhi: McGraw Hill Publication.

Gurugharana, K.K. (1993). "Weakness of the Tax Policy and Tax Structure in Nepal", *Rajashwa,* Year 12, Vol.2.

Ishi, H. (2001). *The Japanese Tax System*. 3rd edition. Oxford University Press.

Kandel, P.R. (2001). "Draft of Income Tax Act 2002: Critical Analysis", *Rajaswa.* MOF, Kathmandu.

——— (2004). *Tax Laws and Tax Planning in Nepal*. *(2nd edition).* Kathmandu: Buddha Academic Publishers.

Kanel, N.R. (2003). *Guidelines to Format Theses and Dissertations.* Kathmandu: New Hira Books Enterprises.

Kansakar, D.R. (1987). "Some Theoretical Consideration of Optimal Taxation in the Light of Economic Efficiency Criterion", *The Economic Journal of Nepal.* Vol.12, No. 1, CEDECON, T.U.

Khadka, R.B. (1994). *Nepalese Taxation: A Path for Reform.* Germany: Marburg Consult.

——— (1995). "An Evolution of the Nepalese Income Tax System", *Economic Review.* NRB, Number 8, November.

——— (2000).*The Nepalese Tax System.* Kathmandu: Sajha Publication.

——— (2001). *Income Taxation in Nepal: Retrospect and Prospect.* Kathmandu: Ratna Pustak Bhandar.

——— (2005). *Modernizing Tax Administration in Nepal.* Kathmandu: Pairavi Prakhashan.

Lekhi, R.K. (1998). *Public Finance.* New Delhi: Kalyani Publications, India.

Mallik, B. (2003). Nepal Ko Aadhunik Aayakar Pranali. *(1st edition).* Kathmandu: Mrs. Anita Mallik Publisher.

Ministry of Finance. *Budget Speeches.* Various Issues, Kathmandu.

———. *Economic Survey,* Various Issues, Kathmandu.

Monga G.S. (1984). "Sensitivity of Tax Yields and the Forecasting", *The Economic Journal of Nepal.* CEDECON, TU.

Musgrave, R.A. (1959). *The Theory of Public Finance.* New York: McGraw Hill.

Musgrave, R.A. and Peggy B. Musgrave. (1989). *Public Finance in Theory and Practice.* 5th edition. New York McGraw Hill-Book.

Nepal Planning Commission. *Three Year Interim Plan.* MOF, Kathmandu.

Nepal Rastra Bank (2006). *A Glimpse of Nepal's Macroeconomic Situation.* Kathmandu, Nepal.

———, (2008). *A Handbook of Government Finance Statics*. NRB, Kathmandu.

———*Economic Review*, NRB, (Several Years).

Nepal, S.P. (2002). *Taxation of Income in Nepal.* An unpublished Ph. D. Dissertation submitted to D.D.U. Gorakhpur University.

Neupane, R.R. (2005). *Income Tax as an Internal Source of Resource Mobilization in Nepal.* Kathmandu: An Unpublished Master Degree Thesis Submitted to Faculty of Management, T.U.

Paudel, J. (2002). *Income Taxation in Nepal: A Study of its Structure and Productivity.* An unpublished M.A. Thesis submitted to CEDECON, T.U. Kirtipur, Kathmandu.

Prasad, B. (1999). *Income Tax, Wealth Tax, Gift Tax and Tax Planning.* 13th Revised edition. New Delhi: Konark Publication.

Reejal, P.R. (1976). *Revenue Productivity and Elasticity Aspect of Nepalese Taxation.* CEDA, T.U.

Regmi, Mahesh Chandra (1971). *A Study in Nepal Economic History 1768-1846.* New Delhi: Manjusri Publishing House India.

______ (1988). *An Economic History of Nepal 1846-1901.* Varanasi: Nath Publising.

Regmi, S.R. (2oo7). "Income Tax Evasion is a Crime in Nepalese Legislation", *Rajaswa*. MOF, Kathmandu.

Shrestha, C.L. (1977). *A Case Study of Income Taxation.* An Unpublished M.A. Thesis submitted to CEDECON, T.U.

Shrestha, R. (1985). *Income Taxation in Nepal: A Study of Its Structure and Productivity.* An Unpublished M.A. Thesis submitted to CEDECON, T.U.

Sing, S.K. (1977). *The Fiscal System of Nepal.* Kathmandu: Ratna Pustak Bhandar.

______ (1991). *Public Finance in Developed and Developing Countries.* New Delhi: S. Chand and Company Ltd.

Singh, R.D. (1999). *Domestic Resource Mobilization for Economic Development in Nepal.* An Unpublished Ph.D. Dissertation submitted to CEDECON, T.U., Kirtipur.

Subedi, P. (1982). *An Analytical Study of Income Taxation in Nepal.* An Unpublished M.A. Thesis submitted to CEDECON, T.U.

Tanzi, V. (1980). *The Sensitivity of Yield of U.S. Individual Income Tax and the Tax Reforms of the Past Decade.* IMF Staff Paper, Vol. 3, No.2, January.

Thapa, G.B. (2000). "Nepalko Rajaswako Samrachana, Rajaswako shiti Ra Chunautiharu", *Rajaswa*. MOF, Kathmandu.

Timsina, N. (2007).Tax Elasticity and Buoyancy: A Revisit", *Economic Review.* NRB, Kathmandu.

Timilsina, P. (2007). *Analysis of Structure and Productivity of Income Tax in Nepal.* An Unpublished M.A. Thesis, submitted to CEDECON, T.U. Kirtipur, Kathmandu.

Todaro, M.P. (1991). *Economic Development in the Third World.* Hyderabad: Orient Longman Ltd. In.

Tripathy, R.N. (1992). *Public Finance in Developing Countries.* New Delhi: Indus Publishing Company.

World Bank (2006). *World Development Indicator.* Washington D.C.

——— (2007), *World Development Report.* Washington D.C.

Appendix I
Total GDP, Total Revenue, Tax Revenue, Non Tax Revenue, Direct Tax, Indirect Tax and others Tax Revenue (FY1964/65 to FY 2006/07)

Amount in Rs. Million

Fiscal Year	Total GDP	Total Revnue	Tax Revenue	Non Tax Revenue	Direct Tax	Indirect Tax	Custom Duties	Sales Tax/ VAT	Excise Duties	Land Rev.n Reg	Income Tax
1964/65	5602	192.3	150.8	41.5	53.6	97.2	83.3	0	13.9	46	5.3
1965/66	6909	216.5	177.1	39.4	57.2	119.9	93.5	0.0	20.1	45.1	7.1
1966/67	6411	256.7	225.8	30.9	72	153.8	121.7	12.1	20	59	7.7
1967/68	7173	306.8	283.8	42.2	105.7	178.1	129.7	26.9	21.5	87.4	11.4
1968/69	7985	413	368.3	44.7	108.7	259.6	183.6	48	28	85.1	16.7
1969/70	8768	464	411.3	52.7	128.6	282.7	193.5	51.1	38.1	102.2	19.6
1970/71	8938	459.7	395.7	64	120.3	275.4	156.5	62.3	56.6	90.9	21.2
1971/72	10369	535.4	466.8	86.6	135.4	331.4	198.6	69.1	63.6	100.5	22
1972/73	9969	615.8	521.1	94.7	135.3	385.8	238.2	79.8	67.8	93.1	23.4
1973/74	12808	766.4	642.4	124	180.2	462.2	286.2	98.5	77.4	123.9	32.6
1974/75	16571	1008.4	841.7	166.7	184.5	657.2	328.5	190.5	119.7	126.9	47
1975/76	17394	1115.6	911.2	204.9	236	675.2	358.5	161.9	132.1	135.5	87.2
1976/77	17280	1322.9	1100.1	222.8	295.7	804.4	386.2	222	166.1	139.7	133.3
1977/78	19732	1582	1243.9	338.2	306.2	937.7	458.8	273.1	164.4	141.1	136.8
1978/79	22215	1811.9	1476.8	334.9	253.1	1223.7	626.7	356.8	192.6	110.3	103
1979/80	23351	1880	1528.8	351.2	253.8	1275	608	401.2	215.2	121.2	101.2
1980/81	27307	2419.2	2035.7	383.5	353.2	1682.5	815.8	537.7	242.2	178.5	144
1981/82	30988	2679.5	2211.3	468.2	379.9	1831.4	825.1	597.4	305.7	170	189.8
1982/83	33761	2841.6	2421.1	420.5	445.1	1976	760.9	709.3	365.8	171.5	240.2
1983/84	39390	3409.3	2737	672.3	541.8	2195.2	825.9	770.7	432.1	212.4	290.9
1984/85	44441	3916.6	3151.2	765.5	559.7	2591.5	1064.4	845.8	483.9	218.6	307.3

1985/86	53215	4644.5	3659.3	985.2	661.8	2997.5	1231	985.9	558.7	244.3	364.4
1986/87	61140	5975.1	4372.4	1602.7	768.7	3603.7	1505.7	1143.8	678.6	284	437.5
1987/88	73170	7350.4	5752.8	1597.6	1010.2	4742.6	2214.6	1300.5	825.3	366.9	579
1988/89	85831	7776.9	6287.2	1489.6	1331.4	4955.8	2289.9	1379.7	877.7	401	861.2
1989/90	99702	9287.5	7283.9	2003.6	1435.1	5848.8	2684.9	1650.1	1097	451.7	919
1990/91	116127	10729.9	8176.3	2553.5	1369.7	6806.6	3044.3	1995.5	1200.3	538.8	746.2
1991/92	144933	13512.7	9875.6	3637.1	1595.2	8280.4	3358.9	2835.9	1419.3	632.2	855.1
1992/93	165350	15148.4	11662.5	3485.9	2036.2	9626.3	3945.1	3438.4	1452.6	754.9	1124.8
1993/94	191596	19580.8	15371.5	4209.4	2855.3	12516.2	5255.2	4693.2	1592.3	833.1	1824.3
1994/95	209974	24575.2	19660	4945.1	3849.3	15810.7	7017.9	6037.9	1675.5	937.7	2640.6
1995/96	239388	27893.1	21668	6225.1	4655.5	17012.5	7327.4	6431.7	1945.9	1079.6	3205.4
1996/97	269570	30373.5	24424.3	5949.2	5340	19084.3	8309.1	7126.6	2302.1	1015.4	3829.4
1997/98	289798	32937.9	25939.8	6998.1	6187.9	19751.9	8499.9	7108.7	2886.5	1006.7	4499
1998/99	330018	37251	28752.9	8494.4	7516.1	21236.8	9517.5	7882.5	2952.5	996.3	5646.5
1999/00	366251	42893.8	33152.1	9741.6	8951.5	24200.6	10813.3	9850	3132.7	1013.3	6755.7
2000/01	425454	48893.9	38865.1	10028.8	10159.4	28705.7	12552.1	12382.4	3771.2	607.8	9153.9
2001/02	444052	50445.6	39330.6	11115	10597.5	28733.1	12658.8	12267.3	3807	1121.3	8903.6
2002/03	473546	56229.7	42587	13642.7	10105.8	32481.2	14236.4	13459.7	4785.1	1414.2	8132.2
2003/04	517993	62331	48173	14158	11894.6	36260.4	15554.8	14478.9	6226.7	1697.5	9504.4
2004/05	566579	70122.7	54104.7	16018	13071.8	41032.9	15701.6	18885.4	6445.9	1799.2	10456
2005/06	630301	72282.1	57430.4	14851.7	13968.1	43462.3	15344	21610.7	6507.6	2180.3	10933.6
2006/07	696989	87712.2	71126.7	16585.5	18980.3	52146.4	16707	26095.6	9343.2	2238.7	15730
2007/08	781262	107622.50	85155.54	22467.04	23078.76	62067.82	21062.5	29815.7	11189.58	2940.74	19078

Appendix II

Total Revenue, Tax Revenue, Non Tax Revenue, Direct Tax, Indirect Tax and others Tax Revenue as Percentage of Total GDP (FY1964/65 to FY 2006/07)

Figures are in Percentage

Fiscal Year	Total Revenue	Tax Revenue	Non Tax Revenue	Direct Tax	Indirect Tax	Custom Duties	Sales Tax/VAT	Excise Duties	Land Rev. & Reg.	Income Tax
1964/65	3.43	2.69	0.74	0.96	1.74	1.49	0	0.25	0.82	0.09
1965/66	3.13	2.56	0.57	0.83	1.74	1.35	0	0.29	0.65	0.1
1966/67	4	3.52	0.48	1.12	2.4	1.9	0.19	0.31	0.92	0.12
1967/68	4.28	3.96	0.59	1.47	2.48	1.81	0.38	0.3	1.22	0.16
1968/69	5.17	4.61	0.56	1.36	3.25	2.3	0.6	0.35	1.07	0.21
1969/70	5.29	4.69	0.6	1.47	3.22	2.21	0.58	0.43	1.17	0.22
1970/71	5.14	4.43	0.72	1.35	3.08	1.75	0.7	0.63	1.02	0.24
1971/72	5.16	4.5	0.84	1.31	3.2	1.92	0.67	0.61	0.97	0.21
1972/73	6.18	5.23	0.95	1.36	3.87	2.39	0.8	0.68	0.93	0.23
1973/74	5.98	5.02	0.97	1.41	3.61	2.23	0.77	0.6	0.97	0.25
1974/75	6.09	5.08	1.01	1.11	3.97	1.98	1.15	0.72	0.77	0.28
1975/76	6.41	5.24	1.18	1.36	3.88	2.06	0.93	0.76	0.78	0.5
1976/77	7.66	6.37	1.29	1.71	4.66	2.23	1.28	0.96	0.81	0.77
1977/78	8.02	6.3	1.71	1.55	4.75	2.33	1.38	0.83	0.72	0.69
1978/79	8.16	6.65	1.51	1.14	5.51	2.82	1.61	0.87	0.5	0.46
1979/80	8.05	6.55	1.5	1.09	5.46	2.6	1.72	0.92	0.52	0.43
1980/81	8.86	7.45	1.4	1.29	6.16	2.99	1.97	0.89	0.65	0.53
1981/82	8.65	7.14	1.51	1.23	5.91	2.66	1.93	0.99	0.55	0.61
1982/83	8.42	7.17	1.25	1.32	5.85	2.25	2.1	1.08	0.51	0.71
1983/84	8.66	6.95	1.71	1.38	5.57	2.1	1.96	1.1	0.54	0.74
1984/85	8.81	7.09	1.72	1.26	5.83	2.4	1.9	1.09	0.49	0.69

1985/86	8.73	6.88	1.85	1.24	5.63	2.31	1.85	1.05	0.46	0.68
1986/87	9.77	7.15	2.62	1.26	5.89	2.46	1.87	1.11	0.46	0.72
1987/88	10.05	7.86	2.18	1.38	6.48	3.03	1.78	1.13	0.5	0.79
1988/89	9.06	7.33	1.74	1.55	5.77	2.67	1.61	1.02	0.47	1
1989/90	9.32	7.31	2.01	1.44	5.87	2.69	1.66	1.1	0.45	0.92
1990/91	9.24	7.04	2.2	1.18	5.86	2.62	1.72	1.03	0.46	0.64
1991/92	9.32	6.81	2.51	1.1	5.71	2.32	1.96	0.98	0.44	0.59
1992/93	9.16	7.05	2.11	1.23	5.82	2.39	2.08	0.88	0.46	0.68
1993/94	10.22	8.02	2.2	1.49	6.53	2.74	2.45	0.83	0.43	0.95
1994/95	11.7	9.36	2.36	1.83	7.53	3.34	2.88	0.8	0.45	1.26
1995/96	11.65	9.05	2.6	1.94	7.11	3.06	2.69	0.81	0.45	1.34
1996/97	11.27	9.06	2.21	1.98	7.08	3.08	2.64	0.85	0.38	1.42
1997/98	11.37	8.95	2.41	2.14	6.82	2.93	2.45	1	0.35	1.55
1998/99	11.29	8.71	2.57	2.28	6.44	2.88	2.39	0.89	0.3	1.71
1999/00	11.71	9.05	2.66	2.44	6.61	2.95	2.69	0.86	0.28	1.84
2000/01	11.49	9.13	2.36	2.39	6.75	2.95	2.91	0.89	0.14	2.15
2001/02	11.36	8.86	2.5	2.39	6.47	2.85	2.76	0.86	0.25	2.01
2002/03	11.87	8.99	2.88	2.13	6.86	3.01	2.84	1.01	0.3	1.72
2003/04	12.03	9.3	2.73	2.3	7	3	2.8	1.2	0.33	1.83
2004/05	12.38	9.55	2.83	2.31	7.24	2.77	3.33	1.14	0.32	1.85
2005/06	11.47	9.11	2.36	2.22	6.9	2.43	3.43	1.03	0.35	1.73
2006/07	12.58	10.2	2.38	2.72	7.48	2.4	3.74	1.34	0.32	2.26
2007/08	13.77	10.9	2.88	2.95	7.94	2.70	3.81	1.43	0.38	2.44

Appendix III
Growth Rates of Total Revenue, Tax Revenue, Non Tax Revenue, Direct Tax, Indirect Tax and others Tax Revenue (FY1964/65 to FY 2006/07)

Figures are in Percentage

Fiscal Year	Total Revenue	Tax Revenue	Non Tax Revenue	Direct Tax	Indirect Tax	Custom Duties	Sales Tax/ VAT	Excise Duties	Land Rev. & Reg.	Income Tax
1964/65	-	-	-	-	-	-	-	-	-	-
1965/66	12.58	17.44	-5.06	6.72	23.35	12.24	-	46.60	-1.96	33.96
1966/67	18.57	27.5	-21.57	25.87	28.27	30.16	-	-0.50	30.82	8.45
1967/68	19.52	25.69	36.57	46.81	15.8	6.57	122.31	7.5	48.14	48.05
1968/69	34.62	29.77	5.92	2.84	45.76	41.56	78.44	30.23	-2.63	46.49
1969/70	12.35	11.68	17.9	18.31	8.9	5.39	6.46	36.07	20.09	17.37
1970/71	-0.93	-3.79	21.44	-6.45	-2.58	-19.12	21.92	48.56	-11.06	8.16
1971/72	16.47	17.97	35.31	12.55	20.33	26.9	10.91	12.37	10.56	3.77
1972/73	15.02	11.63	9.35	-0.07	16.42	19.94	15.48	6.6	-7.36	6.36
1973/74	24.46	23.28	30.94	33.19	19.8	20.15	23.43	14.16	33.08	39.32
1974/75	31.58	31.02	34.44	2.39	42.19	14.78	93.4	54.65	2.42	44.17
1975/76	10.63	8.26	22.92	27.91	2.74	9.13	-15.01	10.36	6.78	85.53
1976/77	18.58	20.73	8.74	25.3	19.14	7.73	37.12	25.74	3.1	52.87
1977/78	19.59	13.07	51.8	3.55	16.57	18.8	23.02	-1.02	1	2.63
1978/79	14.53	18.72	-0.98	-17.34	30.5	36.6	30.65	17.15	-21.83	-24.71
1979/80	3.76	3.52	4.87	0.28	4.19	-2.98	12.44	11.73	9.88	-1.75
1980/81	28.68	33.16	9.2	39.16	31.96	34.18	34.02	12.55	47.28	42.29
1981/82	10.76	8.63	22.09	7.56	8.85	1.14	11.1	26.22	-4.76	31.81
1982/83	6.05	9.49	-10.19	17.16	7.9	-7.78	18.73	19.66	0.88	26.55
1983/84	19.98	13.05	59.88	21.73	11.09	8.54	8.66	18.12	23.85	21.11

1984/85	14.88	15.13	13.86	3.3	18.05	28.88	9.74	11.99	2.92	5.64
1985/86	18.58	16.12	28.7	18.24	15.67	15.65	16.56	15.46	11.76	18.58
1986/87	28.65	19.49	62.68	16.15	20.22	22.32	16.02	21.46	16.25	20.06
1987/88	23.02	31.57	-0.32	31.42	31.6	47.08	13.7	21.62	29.19	32.34
1988/89	5.8	9.29	-6.76	31.8	4.5	3.4	6.09	6.35	9.29	48.74
1989/90	19.42	15.85	34.51	7.79	18.02	17.25	19.6	24.99	12.64	6.71
1990/91	15.53	12.25	27.45	-4.56	16.38	13.39	20.93	9.42	19.28	-18.8
1991/92	25.94	20.78	42.44	16.46	21.65	10.33	42.11	18.25	17.33	14.59
1992/93	12.1	18.09	-4.16	27.65	16.25	17.45	21.25	2.35	19.41	31.54
1993/94	29.26	31.8	20.76	40.23	30.02	33.21	36.49	9.62	10.36	62.19
1994/95	25.51	27.9	17.48	34.81	26.32	33.54	28.65	5.23	12.56	44.75
1995/96	13.5	10.21	25.88	20.94	7.6	4.41	6.52	16.14	15.13	21.39
1996/97	8.89	12.72	-4.43	14.7	12.18	13.4	10.8	18.31	-5.95	19.47
1997/98	8.44	6.2	17.63	15.88	3.5	2.3	-0.25	25.39	-0.86	17.49
1998/99	13.09	10.84	21.38	21.46	7.52	11.97	10.89	2.29	-1.03	25.51
1999/00	15.15	15.3	14.68	19.1	13.96	13.61	24.96	6.1	1.71	19.64
2000/01	13.99	17.23	2.95	13.49	18.62	16.08	25.71	20.38	-40.02	35.5
2001/02	3.17	1.2	10.83	4.31	0.1	0.85	-0.93	0.95	84.49	-2.73
2002/03	11.47	8.28	22.74	-4.64	13.04	12.46	9.72	25.69	26.12	-8.66
2003/04	10.85	13.12	3.78	17.7	11.64	9.26	7.57	30.13	20.03	16.87
2004/05	12.5	12.31	13.14	9.9	13.16	0.94	30.43	3.52	5.99	10.01
2005/06	3.08	6.15	-7.28	6.86	5.92	-2.28	14.43	0.96	21.18	4.57
2006/07	21.35	23.85	11.67	35.88	19.98	8.88	20.75	43.57	2.68	43.87
2007/08	22.70	19.72	35.46	21.60	19.03	26.07	14.26	19.76	31.36	21.28