

**VAT EVASION:
AN ANALYSIS IN THE CONTEXT of NEPAL**

A Thesis

**Submitted to the Central Department of Economics,
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By

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RECOMMENDATION LETTER

This thesis entitled “**VAT Evasion: An Analysis in the Context of Nepal**” has been prepared by **Dipendra Subedi** under my supervision. I hereby recommend this thesis for examination by the Thesis Committee as a partial fulfillment of the requirements for the Degree of Master of Arts in Economics.

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Date: November, 2016

APPROVAL LETTER

This thesis entitled “**VAT Evasion: An Analysis in the Context of Nepal**” submitted by **Dipendra Subedi** to the Central Department of Economics, Faculty of Humanities and Social Sciences, University Campus, in partial fulfillment of the requirements for the Degree of Master of Arts in Economics has been found satisfactory in scope and quality. Therefore, we accept this thesis as a part of the said degree.

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The thesis entitled “**VAT Evasion: An Analysis in the Context of Nepal**” has been prepared in the partial fulfillment of the requirements for the Degree of Master of Arts in Economics. The reason behind the selection of the title is due to alarming increasing of revenue leakage specially VAT evasion in the world and Nepal is no exception for this.

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LIST OF ACRONYMS

BTO	-	Big Taxpayer Office
CAP	-	Chartered Accountancy Profession
CNN	-	Cable News Network
DANIDA	-	Danish International Development Agency
DG	-	Director General
EC	-	European Community
EEC	-	European Economic Community
e.g	-	For Example
EU	-	European Union
Fig.	-	Figure
FNCCI	-	Federation of Nepal Chamber of Commerce & Industry
FY	-	Fiscal Year
GDI	-	Gross Domestic Income
GDP	-	Gross Domestic Product
GON	-	Government of Nepal
Govt.	-	Government
GTZ	-	Deutsche Gesellschaft Fu'r Technische Zusammenarbeit
HIID	-	Harvard Institute of International Development
i.e	-	That is
ICAN	-	Institute of Chartered Accountants of Nepal
IMD	-	International Management Development
IRD	-	Inland Revenue Department
IRO	-	Inland Revenue Office
ITC	-	Input Tax Credit
Ltd	-	Limited
M.A	-	Master in Arts

MBS	-	Masters of Business Studies
MIMIC	-	Multiple Indicators Multiple Causes
MOF	-	Ministry of Finance
MTIC	-	Missing Trader Intra-Community fraud
NIC	-	National Information Commission
NRB	-	Nepal Rastra Bank
OECD	-	The Organization for Economic Co-operation and Development
PAN	-	Permanent Account Number
Pvt	-	Private
Rs	-	Rupees
RTI	-	Right to Information
SAARC	-	South Asian Association for Regional Co-operation
SAFA	-	South Asian Federation of Accountants
SEZ	-	Special Economic Zone
S.No.	-	Serial Number
TDS	-	Tax Deducted at Source
TU	-	Tribhuvan University
UK	-	United Kingdom
UN	-	United Nations
USA	-	United States of America
USAID	-	United States Agency for International Development
VAT	-	Value Added Tax
viz.	-	Videlicet
vs.	-	Versus
WEF	-	World Economic Forum

CHAPTER-I

INTRODUCTION

1.1 Background of the Study

Taxation is one of the important elements in managing national income, and has played an important role in civilized societies since their birth thousands years ago (Lymer & Oats, 2009). Adam Smith in his book ‘The Wealth of Nations’ which was published in 1776 suggested that a tax system is based on certain basic principles, namely equity, certainty, convenience and efficiency. Taxes can be classified into two main types: direct and indirect taxes. Direct taxes mean the burden (incidence) of tax is borne entirely by the entity that pays it, and cannot be passed on to another entity; for example, corporation tax and individual income tax. Indirect taxes are typically the charges that are levied on goods and services / consumptions (Barjoyai, 1987), for example VAT (Value Added Tax), sales tax, excise tax and custom duties. Our study is typically focus on VAT and its evasion in the context of Nepal.

Value Added Tax (VAT) is a form of consumption tax. From the perspective of buyer, it is a tax on the purchase price. From that of the seller, it is a tax only on the value added to a product, material, or services, from an accounting point of view, by the stage of its manufacture to distribution, the manufacturer remits to the government the difference between these two amounts, and retains the rest for themselves to offset the taxes they had previously paid on the inputs.

VAT is an indirect tax which is levied on a product or services the incidence of which is borne by the consumers who ultimately consume the product or services, while the immediate liability to pay the tax may fall upon another

person such as manufacturer or provider of services or seller of goods. Since the cost of indirect tax is on the ultimate consumer and therefore, even the economically challenged bear the brunt equally.

The concept of VAT was developed for the first time by Dr. Wilhelm V. Siemens in Germany in 1919. The concept of VAT was developed further in 1949 by a tax mission in Japan headed by Prof. Carls S. Shoup, the tax however remains as only a topic of academic interest until 1953. In 1954, France introduced VAT covering the industrial sector. The tax was however limited up to the wholesale level. By the end of 1960s only eight countries including France, Brazil, Germany, Netherlands, Sweden etc. had introduced VAT. Since then VAT has been introduced by at least one country each year. Finally introduced by the European Economic Community (now the European Union) in the 1970s, VAT is widely applied in the European countries. The value added tax serves as the solution for different problems related to the sales tax system.

In the context of Nepal, the concept of VAT in Nepal was introduced in early 1990s. Government of Nepal indicated its intention to introduce VAT in the eighth plan, subsequently the finance minister declared to introduce a two-tier sales tax system to make the base of implementing VAT from the fiscal year 1992/93. The parliament of Nepal Enacted "Value Added Tax Act – 1995 (2052)", subsequently VAT regulation was made in 1996; the act was passed in 1995. Finance act 1992 and 1994 introduced two tiers sales tax to make the base of implementing the VAT. VAT task force was formulated in 1993 in technical assistance of USAID which suggested the steps to be followed while implementing the VAT in Nepal. In Nepal ,VAT has been introduced to replace sales tax Act, 2033, Hotel Tax Act, 2018, Contract Tax Act, 2023 and Entertainment Act, 2016 (Bhattarai & Koirala, 2007). VAT is levied on the domestic consumption of goods and services, except those that are zero-rated

(such as food and essential drugs listed in annexure 1 of VAT Act, 1995) or are otherwise exempt (such as exports listed in annexure 2 of VAT Act, 1995). It is levied at each stage in the chain of production and distribution from raw materials to the final sale based on the value (price) added at each stage. It is not a cost to the producer or the distribution chain members, and whereas its full brunt is borne by the end consumer.

Value Added Tax (VAT) is considered as one of the most powerful tool of the fiscal policy. From the long experience of VAT in several countries, many economists as well as policy makers have reached in the conclusion that VAT is probably the best in indirect tax. VAT is as the name itself suggests, imposed on the value-added portion in different stage of sales. It is improved version of sales tax. Ultimately, the real and final burden of tax is shifted towards to the consumers who consumes goods and enjoys the services. As goods and services are shifted in the process of production and distribution, one after another stage the tax is also jointly shifted simultaneously. The coverage of VAT in Nepal is based on transfer, sales, supply, imports and exports of goods and services except some special provisions. Every persons or firms or companies who are involved in such transactions are liable to pay and collect tax. The actual coverage is structured by standard and zero rates as well as tax exempted provisions.

Implementation of VAT was not easy in the initial days. It was a matter of great debate. Even after the enactment of law, there were a lot of constraints and difficulties in introducing and implementing VAT in Nepal. A large number of entrepreneurs, traders and business communities were against VAT system. The initial two year of VAT implementation was very turbulent. Now it has become familiar and VAT is currently well receipted by the consumers as well as business and industrial communities of Nepal. This is account based tax system

that leads to transparency and accountability on the both part of tax payers and tax collectors.

VAT is levied on the taxable value of each transaction, which is the total price charged by the seller (including all- related charges). The taxable value does not include the VAT itself, and takes into account any price adjustments (such as discounts or rebates) in effect at that time of the sale. Adjustment that becomes necessary after the time of sale (such as for goods returned) is to be made in subsequent determination of the tax or credits. The taxable value of a transaction is the price paid, which is also consideration for the goods or services, by the recipient to the supplier, provided that the supplier and recipient are independent of each other. The price charged must include all related expenditure borne by the supplier, for example, transport costs, if the goods are delivered to the recipient, or any taxes other than VAT, chargeable on the goods or services.

The key claim made by the advocates of VAT is that it is particularly effective way of raising tax revenue. Cnossen (1990) argues that purely from revenue point of view, VAT is probably the best tax ever invented.

In the case of imported goods, the tax base is the sum of import value, freight, transport costs, insurance, commission, import duties plus any charges paid by the importer. Regarding the taxable goods and services Nepal has adopted two types of tax rates. One is standard rate (currently 13%) and other is zero-rated. The Value Added Tax Act, 1995 has listed exempted goods and services under schedule one. Except this provision, all value added economic transactions are taxable and tax is collected at the rate of 13 %.

Under the Nepalese VAT system, some goods and services are taxed at zero-rate. The objective of this zero rate is to provide the relief on some goods and services

under regular VAT system. Supplies made outside from Nepal or exports are taxable at zero rate. The exporters are allowed to claim input tax credits paid or payable on purchases of goods and services relating to their commercial activities. Exports taxed at zero percent include exports of both goods and services. The list of exempted and zero rated goods and services are frequently changed by Finance Acts (Hassan, 2005).

1.2 Statement of the Problem

In every country, the government collects its revenues through different sources and mobilizes its revenues through budget in development activities for the public welfare and interests. As expenditure of Nepal government is higher than its income, it has been facing the situation of budget deficit or deficit financing for quite a long time. In such a situation, the government manages funds to meet its expenditure either through the change in cash reserves or through domestic borrowings or loans from foreign countries and donor agencies, or any of these measures. Due to inability of Nepal Government to meet its expenditure from receipts of taxes, grants and principal repayment receipt, necessary amount for expenditure is garnered by using various instruments of financing including external and domestic borrowings (MoF, 2015). The ever increasing government expenditure and limited sources of revenue have lead the country to several fiscal crises over many years. The share of foreign aids in development expenditure is more than 50 percent. The burden of foreign debt is increasing year by year (Kharel, 2011).

In FY 2014/15, the contribution of revenue in annual budget is around 80 percent, out of which the share of tax revenue is around 72 percent. The revenue/GDP and tax/ GDP ratios are about 18.4 percent and 16.5 percent respectively but the expenditure/GDP ratio is around 23.3 percent. As per the

government's income and expenditure estimates for current fiscal year, budget deficit to GDP is likely to be 4.86 percent (MoF, 2015). The persisting budgetary deficits and increasing dependency on foreign assistance for financing deficits present a dismal picture of country's prospects. All these facts prove that the volume of collected tax is not enough to meet public financing. Since the level of tax compliance is lower than potential so it needs to develop and apply proper leakage control mechanism. It is necessary to promote tax compliance habit of existing tax payers and bringing potential taxpayers in tax net.

At the same time, everywhere in the world, there are problems related to revenue leakages. Like any tax, the VAT is vulnerable to evasion and fraud. But its credit and refund mechanism offers unique opportunities for abuse and this has been an urgent concern in the European Union (EU) in the past. James and Alley (2004, p.28) define tax evasion as 'the attempt to reduce tax liability by illegal means' while tax avoidance is defined as 'reducing taxation by legal means'. Lewis (1982, p.123) perceived tax evasion as 'any legal method of reducing one's tax bill' and tax evasion is 'illegal tax dodging'. Similarly, Kasipillai, Aripin and Amran (2003, p.135) perceived tax evasion as actions which result in lower taxes than are actually owed. History shows that Nepal seems have been facing the problems of revenue leakages before and since Rana Regime. Noted economic historian Mahesh Chandra Regmi states "for instance the amount assessed at Birgunj was Rs.6120 while not more than Rs. 4673 were collected at Chisapani. Leakage of customs revenue in Nepal, India trade in the central border thus amounted to approximately one fourth of the total amount" (Ghimire, 2006).

1.3 Objectives of the Study

The general objective of the study is to study VAT evasion in Nepal and suggest useful alternative solution to reduce negative impacts of tax leakages, the control of tax evasion and avoidance.

The specific objectives are:

- To review the Nepalese tax structure
- To find out the causes of non-compliance with the law and summarize the vulnerability of VAT to evasion
- To trace out administrative, legal and other constraints in tax (VAT) compliance and enforcement of laws
- To provide suggestions / recommendations for making VAT effective and efficient in Nepal.

1.4 Significance of the Study

According to Bird (2005) over the last few decades, VAT has swept the world. VAT can play an important role in the process of development in developing countries like Nepal which needs higher revenue to fulfill its financing deficit.

Extensive studies have been done on various aspects of the operations of VAT but not so much appear to have been done in study VAT Evasion. There is need of comprehensive study about VAT in Nepal. This study is thus undertaken to add to whatever scarce studies already exist in VAT. So, many empirical and theoretical studies have been conducted to examine the various problems and prospects of VAT in Nepal. In addition, it also finds out the contribution of VAT to GDP and other economic indicators. So the research is significant in the sense

that its thorough study may facilitate the government making policy and solving the implementation problems and VAT related issues.

Moreover, the government is facing many problems for effective implementation of VAT. In spite of regular effort, the transactions are incurred evading VAT. It may be helpful for the businessmen and the consumers as well who are still lost amid the confusion about the proper implication of VAT. The study will be directly beneficial to policy maker, private sector, researcher and general people. Policy maker will be able to identify the areas needed for improvement. It will help the researcher to carry out the research a step ahead about VAT and other researchers who are interested in doing research in this particular topic.

1.5 Limitations of the Study

This study covers only value added tax. Leakages of other taxes and non-tax revenue have been deliberately left because of the time constraints.

The limitations of the study are:

- It is not a complete study of the whole tax system in Nepal.
- The study is based on secondary data that covers the period from 2007/08 to 2014/15. The reliability of such data has not been examined.
- Primary data drawn from survey has also been taken into consideration to draw conclusion.
- The accuracy and reliability of the conclusions of data depends upon the published data, official records and opinion of the respondents.

1.6 Organization of the Study

The study has been organized into six chapters. The first chapter is the introductory chapter that covers general background, statement of the problems, objectives, significance and limitations of the study. The second chapter deals with the conceptual framework and review of literature. The third chapter describes research methodology employed in the study. The fourth chapter deals with VAT in Nepal and Evasion and fifth chapter is the presentation and analysis of data in which all collected relevant data are analyzed and interpreted by the help of different financial & statistical tools. The last chapter depicts overall picture of the study that contains conclusion recommendation and suggestion on the basis of the findings of the study. Besides these chapters, the report consists of a set of questionnaire and reference of materials used in the study.

CHAPTER-II

REVIEW OF LITERATURE

The key claim made by advocates of the VAT is that it is a particularly effective way of raising tax revenue: Cnossen (1990), for example, argues that “purely from a revenue point of view, VAT is probably the best tax ever invented,” Advocates have also long recognized, of course, that the VAT, like any other tax, is vulnerable to evasion and fraud, but stress distinctive features of the VAT that may make it less vulnerable than other forms of taxation. Over the last few years, however, there has been a marked increase in concern with losses of VAT revenue through evasion and fraud. This is especially so in the European Union, where the abolition of internal EU frontiers at the end of 1992 opened up new areas of vulnerability. The European Commission, for example, reports that losses from fraud—most famously, “carousel fraud”—have recently amounted to 10 percent of net VAT receipts in some member states in 2004.

2.1 Theoretical Review

Value Added Tax (VAT) is a major source of indirect taxes. It is improved version of sales tax. It is a tax imposed on value addition on goods and services made by business entities at the successive stages of production and distribution. VAT is a broad based tax on business designed to measure net value generated in a country. Being a broad based tax, it is imposed on producer, wholesaler, retailer and consumers also. It is a modern tax system which enables to efficient collection system, to increase efficiency and to reduce tax evasion (ICAN, 2012).

VAT is an indirect tax on the domestic consumption of goods and services, except those that are zero-rated (such as food and essential drugs) or are

otherwise exempt (such as exports). It is levied at each stage in the chain of production and distribution from raw materials to the final sale based on the value (price) added at each stage. It is not a cost to the producer or the distribution chain members, and whereas its full brunt is borne by the end consumer, it avoids the double taxation (tax on tax) of a direct sales tax.

Value added approach was discussed by scholars as early as 1918, and this tax system was first recommended by William Von Simens in 1919 in Germany. He recommended replacing the existing law of charging multi-stage turnover tax. Simens suggested that the new tax system would reduce the various complicated systems of taxing. Still, the German government decided not to replace existing system. In 1921, VAT was suggested by Professor Thomas S. Adams for the USA. In 1953, the state of Michigan enacted a form of VAT as a compromise between groups seeking and opposing state corporation income tax. In 1962, the European Economic Committee recommended implementation of VAT in all the member countries of the European Union.

Personal end-consumers of products and services cannot recover VAT on purchases, but businesses are able to recover VAT (input tax) on the products and services that they buy in order to produce further goods or services that will be sold to yet another business in the supply chain or directly to a final consumer. In this way, the total tax levied at each stage in the economic chain of supply is a constant fraction of the value added by a business to its products, and most of the cost of collecting the tax is borne by business, rather than by the state. Value added taxes were introduced in part because they create stronger incentives to collect than a sales tax does. Both types of consumption tax create an incentive by end consumers to avoid or evade the tax, but the sales tax offers the buyer a mechanism to avoid or evade the tax—persuade the seller that he (the buyer) is not really an end consumer, and therefore the seller is not legally required to

collect it. The burden of determining whether the buyer's motivation is to consume or re-sell is on the seller, but the seller has no direct economic incentive to collect it. The VAT approach gives sellers a direct financial stake in collecting the tax, and eliminates the problematic decision by the seller about whether the buyer is or is not an end consumer.

In Nepal, the budget speech of F/Y 1993/94 realized the need to change sales tax into VAT gradually. A task force was set up in the sales tax and Excise duty department to make necessary preparations for an early introduction of VAT. The effort of the task force was not fruitful because the government felt the need of further study in this project. During 1994/1995, a new task force unit was formed for re-observation of Nepalese tax system. The task force reached the conclusion that "there is no reliable measure other than changing existing sales tax into VAT." As a result of the study, the VAT Act, 1995 and VAT rules 1996 came (ICAN, 2012).

Tax compliance is a major problem for many tax authorities and it is not an easy task to persuade taxpayers to comply with tax requirements even though 'tax laws are not always precise' (James & Alley 2004, p.29).

2.2 Concept of Evasion

Evasion refers to:

- An act or instance of escaping, avoiding, or shirking something
- The avoiding of an argument, accusation, question, or the like as by a subterfuge
- A means of evading, subterfuge, an excuses or trick to avoid or get around something.

- Physical or mental escape
- An act or instance of violating the tax laws by failing or refusing to pay all or part of one's taxes.

Tax Evasion is an illegal practice where a person, organization or corporation intentionally avoids paying his/her/it's true tax liability. Those caught evading taxes are generally subject to criminal charges and substantial penalties. Tax evasion is the general term for efforts by individuals, firms, trusts and other entities to evade taxes by illegal means. Tax evasion usually entails taxpayers deliberately misrepresenting or concealing the true state of their affairs to the tax authorities to reduce their tax liability, and includes, in particular, dishonest tax reporting (such as declaring less income, profits or gains than actually earned; or overstating deductions).

Tax evasion is the illegal evasion of taxes by individuals, corporations and trusts. Tax evasion often entails taxpayers deliberately misrepresenting the true state of their affairs to the tax authorities to reduce their tax liability and includes dishonest tax reporting such as declaring less income, profits or gains than the amounts actually earned or overstating deductions. Tax evasion is an activity commonly associated with the informal economy. One measure of the extent of tax evasion (the "tax gap") is amount of unreported income, which is the difference between the amount of income that should be reported to the tax authorities and the actual amount reported.

2.3 VAT Evasion

Keen & Smith (2007) in IMF working paper ‘VAT fraud and Evasion: what do we know and what can be done?’ considered fraud and evasion of VAT as follows:

- **Under-reported sales:** A trader may report only a proportion of sales, falsifying records and accounts to match, or may make some sales ‘off the books’ entirely. Under a VAT, they may or may not issue an invoice. If they do, the customer, if registered for VAT, may seek the corresponding credit. The ultimate success of the evasion then depends on the inability of the revenue authorities to discover that more VAT invoices have been issued but not declared by their issuer. For sales to final consumers or exempt businesses, however, there is no gain from issuing an invoice, since no credit would be available: common examples include personal services (hairdressing, home decoration, building contractors working for private customers and so on) for which value added at the final stage is usually large relative to Vatable inputs. Sometimes, of course, the customer is aware that the sale is made without VAT, and may share some of the gains (or believe that they do so).
- **Failure to register:** The commonest such cases under the VAT are relatively small businesses operating close to the level of turnover at which registration becomes compulsory, that fail to register, saving both the VAT for which they would be liable and VAT compliance costs. “Ghosts”—traders wholly unknown to the revenue authorities—may be able to evade income taxes as well as VAT.

- **Misclassification of commodities:** When traders have sales that are liable to VAT, or some of which lie outside the scope of the tax (exempt items under the VAT), they may reduce their liability by exaggerating the proportion of sales.
- **Omission of self-deliveries:** Goods or services produced by the business and consumed by the proprietor or employees, in principle taxable, may not be declared. Generally, however, this is a relatively unimportant category in more developed economies where agriculture, for which this can be a real issue, is less significant. And a VAT with a relatively high registration threshold will exclude many of the smaller businesses for which this is likely to be more of a risk.
- **Tax collected but not remitted:** This may be possible either through false accounting, by engineering bankruptcy before tax is paid, or in other ways. More particularly, the ‘missing trader’ frauds which involve registered businesses charging their customers VAT but disappearing before paying tax to the authorities.
- **Imported goods not brought into tax:** If tax is not levied at the border, then there is a potential gain from purchasing imported goods bearing no tax and then reselling them in the home market. Most VATs, in contrast, bring imports immediately into tax and so are more robust against this type of fraud. As will be seen, however, the risk of such ‘acquisition fraud’ does arise under, and is a major weakness of, the current deferred payment system.
- **Credit facility claimed for VAT on purchases that are not allowable:** This arises in two main forms. First, when traders supply a variety of

outputs, some subject to VAT and others exempt, they have an incentive to allocate inputs to production of the taxed items (in respect of which input tax credit is available) rather than the exempt (for which it is not). While rules are commonly adopted for such apportionment, the borderline inevitably proves contentious—and indeed there may well be no conceptually correct allocation. Second, items bought for private consumption may be misrepresented as business inputs, allowing the VAT to be recovered (and income tax liability reduced).

2.4 International Review

Carl (1969), in his famous book "Public Finance" considered Value Added Tax as the latest and probably the final stage in historical development of general sales tax imposed on the value added by the business firm. He explained VAT as the difference between sales proceeds and cost of materials etc. purchased from others firms, which is the tax base of VAT. He further added, a firm adds value added by processing or handling these purchases items with its labor force and its own machinery, bulking or other capital goods.

While talking about the types of VAT and its practicability i.e. GNP, income and consumption Musgrave and Musgrave (1970), in their book "Public Finance, Theory and Practices" had preferred the latest type of VAT as more applicable and reliable one for both efficiency and quality which was similar to the retail sales tax and seemed to be more practical for poor countries. Likewise, the invoice method for calculation was more preferable and has the advantage of the value added approach.

Regarding the problem of VAT, Musgrave and Musgrave remarked "A sales tax may be imposed on either single or multiple forms. If the later one is

implemented in the value added (rather turnover) sense, it turns to be corresponding single tax. At each and every stage the value of product is increased and this price rises according, which is the "Value Added Tax base".

Goode (1986) in "Public Finance in Developing Countries" describes VAT as the most important innovation in public finance. VAT applies to the tax imposed on the value added at successive stage of production and distribution. VAT, a sales tax on consumption is fairer than an income tax because the later results double taxation of saving is unconvincing but the former lacks the progressiveness, which serves by later.

James and Alley (2004) asserted that non-compliance is more than tax evasion and it also includes some forms of tax avoidance. James and Alley define tax evasion as 'the attempt to reduce tax liability by illegal means' while tax avoidance is defined as 'reducing taxation by legal means. Lewis (1982, p. 123) perceived tax evasion as 'any legal method of reducing one's tax bill' and tax evasion is 'illegal tax dodging'. Similarly, Kasipillai, Aripin and Amran (2003, p.135) perceived tax evasion as actions which result in lower taxes than are actually owed while tax avoidance, denotes the taxpayers' creativity to arrange his tax affairs in a proper manner based on law and regulation (any provision not violated) so as to reduce his tax bill, and this is (or should be) acceptable in view of the tax administrator.

Lewis (1982) outlined two major distinctions in intentional tax evasion: 1) evasion by commission and 2) evasion by omission. Evasion by commission requires an action by taxpayer, for example claiming deductions or rebates which mean that if a taxpayer is making a false claim, he will get a tax saving (a commission on top of his evading actions). Conversely, evasion by omission is intentional and should be classified as seriously as evasion by commission.

Kim (2008) reports the degree of tax evasion for 59 countries and 47 countries according to reports by World Economic Forum (WEF) and the International Management Development (IMD) respectively. The scale for WEF is from 1 to 7 and IMD is 0 to 10. In addition, Kim also concluded that tax evasion across the countries is highly correlated with politics and tax administration.

Lefebvre et al. (2011) conducted study in Netherlands, France and Belgium (Flanders and Wallonia) while examining the behavior of people. He compared the behavior of people regarding welfare dodging and tax evasion. Results indicated that: people adopt less evaded behavior in tax treatment than in welfare treatment; and people evade more tax in Netherlands and France but tax evasion is more in Flemish than Walloons. Uadiale et al. (2010) conducted study in Nigeria while examining relationship between personal income tax evasion and cultural factors like religiosity, trust in government, and legal enforcement. Study found positive impact on personal income tax of trust in government and legal enforcement. However, no significant relationship found between religious variables and tax evasion in Nigeria. Boylan and Sprinkle (2001) conducted study in which he tried to explore the behavioral determinants of tax evasion. He used experiment technique in order to acquire desired objectives such as to identify the factors that motivate the tax compliance and characteristics of noncompliant taxpayers. Pommerehne et al. (1994) conducted study in order to recognize the determinants of tax evasion. They used the presence of grievance in absolute terms in their study. Results indicated that as the sentiments of grievance increased in absolute terms, the level of tax evasion also increased and the level of tax moral belief decreased. Likewise, study found an ambiguous relationship between marginal tax rate or income and tax evasion. Allingham and Sandmo (1972) conducted study in order to examine the behavioral determinants of tax evasion by introducing a seminal theoretical model. In this study, he explained that the behavior of tax evasion was based on level of risk aversion,

amount of penalty imposed, and probability of being audited. Moreover, study found an ambiguous relationship between marginal tax rate or income and tax evasion.

A wide study of the experiences of different countries with VAT across the globe shows that there can be different models of VAT depending upon the circumstances prevailing in each country. Theoretically speaking VAT is mainly of two kinds viz national and sub-national VAT but there is some hybrid types as well.

i. The National Model:

National VAT is considered as an ideal form of VAT. It has been argued that VAT operates more successfully as a national VAT (McLure 1993, Tait 1988). Norregaard (1997) states that the requirements needed to operate VAT are generally best met by the central government. For instance the extensive administrative capability required to manage vat is at best a function of the central government. Similarly the need to make VAT neutral with respect to the spatial allocation of production and consumption and the need to exercise extensive border control between jurisdictions strengthens the belief that it is appropriate to assign value added taxes to the central government.

In fact, a single 'National VAT' is of distinct advantage even if all or some of the proceeds of the tax are to be distributed to the states, either on the basis of estimated consumption or on some formula basis. This approach of intergovernmental transfer may be the best approach to finance sub-central levels of governments. While the total to be transferred is fixed as designated share of VAT collections, the amount to be allocated to each state is determined by a

formula laid down by the central government. This model is in operation in Germany. But it is to be kept in mind that even in Germany the federal issues were not easily resolved and the formula of revenue sharing with sub-national levels could not be implemented without considerable disagreement.

As Tait (1988) argues, “(The) system cannot work in a federal system where the states try to retain more discretion over their own exemptions, rates and revenues.” Thus the successful implementation of VAT (esp the conventional model) in a federal country lacks theoretical backing. In fact Tait (1988) concluded in his study that in a federal system the workability of vat was uncertain. In USA (being a federation of States) VAT has not been introduced due to the fear of Federal Government usurping the States’ power of sales taxation.

ii. The Sub-National Model:

McLure (2000) and Bird and Gendron (1998) discuss the problem of imposition of VAT at two levels of government and that of application of VAT to interstate trade within the same country. Bird (1999, 2000) argues that the conventional model of tax assignment is no longer viable because subnational governments are increasingly being asked to pick up a larger portion of social expenditures on health and education. As a consequence the sub-national VAT is being considered in context of countries like India with important regional governments.

It is to be noted that IP and Mintz (1992) in their subnational vat model recommended that the Federal government should turn over all sales taxes to the provinces to reduce the administrative and compliance costs of taxation and to give more revenue discretion to provinces and hence make them more

responsible for financing more of their own spending on health or education. McLure (2000) also emphasizes the desirability of permitting state governments to set their own VAT rates. But in case of country like Nepal sub national VAT would pose problem as to which state should receive revenues from VAT on imports and which should bear the burden of VAT refunds on exports. The difficulties associated with the levy of VAT at the sub-national level can be judged from the experience of Brazil. According to Norregard (1997), Brazil offers an example of VAT assignment system that is generally believed to have had detrimental effects on economic performance.

In fact international experience suggests that the developed and non-federal countries have a better record of smooth transition to VAT. When VAT is sought to be implemented in a federal state, various problems prop up pertaining to federalism in general and fiscal federalism in particular. Problems are more severe when the country where VAT is sought to be implemented is a developing country in addition to being federal. R.M. Bird have stated that no one has yet found any simple and uniform solution to deal with all cross border shopping problems associated with taxing sales at the two levels of government (Bird 1999). In case of India, there seems to be only one practical solution for interstate taxation and that is 'zero rating of inter-state sales'. This option envisages reduction of rate of tax under CST, initially to 2% and gradually to zero percent.

iii. Dual VAT Model:

Taxonomically Dual VAT is a type of Subnational VAT where each level sets its own rates independently (thus retaining autonomy) but on similar bases. The base for a sub-national VAT system is a well-designed and comprehensive national VAT. In the dual VAT system, the only VAT rate set centrally is that of the central government itself. According to Bird and Gendron (2000) in this

system there is no need for any 'central' edict with respect to either the range or level of state taxes applied to interstate trade since no such taxes are applied. Thus dual VAT approach obviously requires a central VAT (although perhaps one that collects no revenue) and some degree of information exchange and co-operation amongst tax authorities. Bagchi (1997) suggested that the long-run solution should be a concurrent or dual VAT with a nationally-determined base but independently-set federal and state rates. The major constraint in case of India also for applicability of a dual vat is that the system works well when there is a high level of administrative cooperation.

2.5 National Context

Bista (1999) in his M.A. dissertation on "Value Added Tax: It's Issues and Effects" the objective of the study is to examine the importance of VAT with respect to resource mobilization and to identify the problem of VAT and its prospects in developing countries like Nepal. The study basically stands on secondary data. Data analyzing tools are simple statistical tools e.g. percentage, ratio etc. In his study, he found the following facts with respect to his objective.

VAT can mobilize the rest of revenue resources by broadening tax base and tackling all illegal business activities. Tax officers are not specialized or the professionalism is not developed on tax officers. Public awareness is low to make people aware. Paper media commitment towards VAT is weak, open boarder is the main cause of unauthorized trade and unofficial trade. He recommended the following things most necessarily to make the VAT effective. Political parties as well as leaders should show their commitment towards VAT implementation. Government should manage the necessary physical environment so that the VAT administrations can function properly and effectively. There should be good co-operation between government and business community. Talking with India

should solve problem arisen by open boarder. VAT officials should be trained. These were the main recommendation made by him.

Devkota (2000) in his M.A. dissertation on “A Study on Value Added Tax Imposition in Nepal” Basic objectives of the study were to see the effectiveness of present information and communication networking in imposition of VAT. He has collected primary data to gather opinions and views relevant to study objectives. Statistical tools he used are simple as ratio, percentage, average etc. According to him, main problems in implementation of VAT are lack of VAT education to taxpayers and low public awareness level towards VAT. Value Added Tax system has not created positive thinking to taxpayers. The customers do not have habit to collect invoices while purchasing goods and services, which are the most important part of success and failure of the VAT implementation. He also found the communication gap between government and private sector towards VAT. It seems lack of enough preparation for implementation of VAT in Nepal.

Ghimire (1998) in his M.A. dissertation entitled “Value Added Tax Key Issues in Nepal” tries to examine the various issues pertinent to VAT in Nepal. His study is based on primary data by administrating question to VAT in Nepal. Data analysis tools used in his dissertation are simple statistical tools such as average percentage, ratio etc. He has followed analytical as well as descriptive research design. Existence of open boarder and large amount of unauthorized trade from India to Nepal passes a great threat to the success of VAT in Nepal. Illegal imports would help to form a channel resulting in a large scale of tax evasion. He has made some recommendations for the successful implementation of VAT in Nepal. They are strong administration education program to relevant persons, registration extensive training program to VAT personal, technical data base system, combination of various revenue teams, co-ordination of VAT department

with other departments, close co-operation between government and private sector etc.

Silwal (1999) had expressed his practical experiences about VAT. In his words “VAT is in all stages not-cascading tax system. It extends to all levels of production and distribution. Similarly, it covers all stages and services or exempting any of them renders VAT ineffective. The book gives main focus on Nepalese tax system. The book clearly analyzed why the government of Nepal introduced VAT. He suggested that factors affecting VAT design. Poorly designed VAT accompanied by weak administration would just drain the treasury. So, almost care is necessary while designing a VAT. He concluded that the introduction of VAT provides an opportunity to sweep the cobwebs, revamp and substantial part of the tax administration. In every country, where it has been implemented properly, the VAT has proved itself as revenue productive tax. However, the benefit from VAT depends upon its coverage.

The Institute of Chartered Accountants of Nepal (ICAN) in 2012, has published book entitled "Advanced Taxation " for CAP III level, this book has attempted to specify the provision regarding registration and deregistration, transactions covered by tax, method of calculation of VAT under different situation, Market value concept, method of calculation of VAT payable and receivable by person, types of tax invoices, books to be maintained by a registered and non-registered person and effect of tax on financial accounting.

“Reforms Necessary in Nepalese VAT Law”, an article published in <http://talkingforum.wordpress.com/> by Dahal, Rajib who is an Advocate suggests various reforms required in the current VAT system in Nepal. The rates used, zero rated and exempted goods and their consequences in the current revenue is also mentioned in the article.

Neupane (2014) has submitted thesis on "Effectiveness of Value Added Tax in Nepal". The objectives of the study were to examine how effectively VAT regulation has been implemented, to provide guidelines for compliance of prevailing VAT legislation, to study how VAT is assessed in Nepal, to present relevant provisions of VAT act, rules, directives and public circular, to present possible actions to correct loopholes that exists in prevailing legislation on VAT and to study contribution of VAT to the revenue of the country.

Neupane in her thesis concluded that VAT has become one of the major sources of government revenue; VAT has contributed 35% on the total tax revenue of the government in over past 10 years. Major contribution of VAT revenue come through VAT on import levied at the custom point. Out of domestic collection of VAT major contribution is from production sector. The level of awareness of VAT system in Nepal is very low among small business and consumers. 50% of consumers do not know about the VAT system of Nepal. Similarly 13% businessmen do not know about the VAT system of Nepal. The habit for asking for VAT bill among consumers is very less. Consumer's choice is not affected by registration status of seller. Businessmen find various difficulties to deal with prevailing legislation of VAT. Improper VAT charging, unreasonable demands of taxation authority, stringent refund procedures are the major problems faced by the businessmen. There are various loopholes in current VAT legislation. Under invoicing, import smuggling, difficulty in differentiating personal and business use and lower monitoring activities are regarded as major loopholes of current VAT practices in Nepal. Various corrective actions are available for sophistication of current legislation on VAT in order to control revenue leakage as well as wellbeing of the society. The major suggestion of the public are discourage corruption, strengthen the rules regarding issuance of VAT bill, increase surprise visit at business premises and increase awareness on VAT.

Tamrakar (2013), in his dissertation entitled "Value Added Tax in Nepal : Legal provisions, practices and contribution to government revenue" analyzed the definition of the Value Added Tax Act 1995, tax invoice system, tax administration, case laws of VAT, impacts of use of VAT, taxable and non-taxable goods and services, VAT frauds mechanism used by businessmen etc. He has presented the definition of important terms. He has also analyzed some impacts of VAT implementation. He concludes that the major uses of VAT are economic stabilization, economic growth and investments. He has presented the list of VAT exempted goods and services clearly. He identified major means used for VAT fraud are under invoicing, concealment of stock quantity, non-registration by person required to registered, misclassification of commodities , omission of self-deliveries, tax collected and not deposited in government accounts etc.

The major findings are:

- The collection trend of VAT both internal and imports both are in increasing trend every year. Similarly, contribution of VAT to GDP and revenue collection is also increasing.
- The average contribution of VAT in total tax revenue, indirect tax revenue and GDP were 37.57 %, 47.99%, 7.5% respectively in FY 2011/12.
- Average numbers of VAT payers is increasing in each year and it will be high in the future.
- Double book keeping practices are prevalent in Nepal among businessmen for VAT evasion.
- VAT evasion by way of under invoicing, misclassification of commodities, omission of self-deliveries, tax collected but not remitted and concealment of stock position are major issues raising VAT evasion in Nepal.

Pradhan (2010) made a dissertation entitled on “Tax Payers Education Regarding VAT collection in Nepal”. The objectives of the study were to assess the current status of tax-payers education and awareness regarding VAT, to find the relationship between VAT collection and taxpayer’s education, to examine the effectiveness of present management system of VAT, to provide suggestions for improving taxpayer’s awareness in Nepal. Pradhan concluded that VAT is the most important source of the government revenue. VAT has been implemented as a major part of the tax reform programmed. Initially, its process was slow due to opposition from the business community and subsequently to administrative problems. Despite preliminary resistance VAT has been largely accepted by the taxpayers as well as business communities. The major problem or reason behind all the problems is lack of taxpayer’s awareness regarding VAT. This puts forward the need of encouraging taxpayers for voluntary compliance and any reforms of tax administration should also aimed on motivation taxpayers on it. The government needs to take necessary steps to sort out emerging problems in success of VAT implementation. For this taxpayers awareness programmed and tax education plays prime role.

Wagle (2010) submitted thesis titled “Contemporary Issues on VAT System of Nepal”. Wagle concluded that the major source of VAT collection was from the imports. The thesis concluded that awareness level of the general customers regarding the provisions of law of the country is found very poor. Either they feel it a matter of useless things or they are not getting knowledge from the competent authority on such issues. The main problem from the side of revenue administration is they are not friendly with tax payers and even willing to pay tax, cooperation and help from the government official is very low. Under invoicing by the businessman and the corrupted government official are the main causes for not being collected optimum VAT that could be collected. Awareness at consumer’s level is very important so that they feel their duty and

responsibility to pay tax and contribute something towards nation buildings. All the people of Nepal should feel positive towards the system of taxation in Nepal to obtain optimum result from our system. Taxpayers, customers who are ignoring the VAT system should be given proper knowledge about the VAT and its benefits. Knowledge of the people associated with VAT system should be developed well and they should be able to get all the facility given to them by Value Added Tax Act of Nepal.

Parajuli (2010) submitted thesis titled “Revenue Collection from Value Added Tax (VAT)”. The objectives of the thesis were to examine the administrative system and legislative part of the VAT in Nepal, to explore the practice scenario of VAT in Nepal, to find out the tax revenue structure in Nepal, to find out the contribution of VAT in GDP, total revenue and tax revenue, to forecast the VAT revenue and GDP for future 5 years based on the time series analysis. Parajuli concluded that VAT plays a crucial role in the revenue mobilization in Nepal. According to him VAT system, made all kinds of transactions transparent, helps to make the wide area of tax and discourages tax evasion. So VAT is the most important sources of the government revenue. Implementation of VAT was not easy in the initial days. It was a matter of great debate. Even after the enactment of law, there were a lot of constraints and difficulties in introducing and implementing VAT in Nepal. A large number of entrepreneurs, traders and business communities were against VAT system. The initial two years of VAT implementation was very turbulent. Now it has become familiar and VAT is currently well received by the consumers as well as business and industrial communities of Nepal. This is account based tax system that leads to transparency and accountability on the both part of tax payers and tax collectors. One of the key issues is administrative capability and situation. Another issue is Nepalese businessmen are generally found not issuing the VAT bill. Public are also not well educated in this matter.

Neupane (2010), submitted thesis titled “VAT in Nepal: Challenges in its Implementation”. Neupane concluded that Value Added Tax puts greater significances in revenue mobilization in Nepal. The Reason behind this is that VAT system is transparent with broad tax base and discouraging tax evasion. So, it is necessary to say that VAT is the most important source in the government revenue. VAT is a most scientific, innovation and powerful tax system with built in quality of universal application for both developed and developing economies. VAT system makes it possible to broaden the tax base, eliminate the tax evasion and cascading, create an investment friendly environment and finally to increase to government revenue. There is no doubt in the fact that VAT in long run will help to make Nepalese economy stronger. In this sense, the successful implementation of VAT system has a greater significances as well as importance in Nepal.

Karn (2011) submitted thesis titled “VAT Administration and its Effectiveness in Nepal”. Karn concluded that Nepal has different kinds of problem, constraints and challenges in the all sectors of VAT implementation such as administrative, political, geographical, social, and economic and others. VAT is considered to be the best fiscal tool; practically it is also proved that it has many short comings. VAT influences the level of economic activities and other variables like price, wages, foreign trade etc. directly or indirectly. VAT in terms of revenue raised by it cannot be termed successful. The reasons behind this may be numerous including the conflict situation in the country. The following major problems summarized in the thesis was, Lack of enforcement spirit in administration, Lack of taxpayer monitoring by tax administration, Single rate which is high for basic goods and services. It is advantageous too to tax evaders both in not depositing collected tax and evading the tax., Threshold problem which is working as the shield to bring all the tax payers in the tax net., Exemption problem which is helping as the shield to hide the transaction of taxable goods and making the tax

net small. Customs valuation problem which is working as the starting point of under invoicing of the goods. The problem of compliance and prevent evasion in the VAT remain the same. Thus tax investigating and audit should be effective in order to make taxpayer more careful in fulfilling their duties. Most of the officers engaged in the VAT administration are not motivated. Due to lack of motivation many officials are not actively engaged in the implementation of VAT effectively. It is found that the concern bodies do not have clear concept about the VAT. They do not take VAT bills. There is also problem with paying and refunding of VAT. Lack of consumer, Awareness Weakness of government action plan, Administrative inefficiency and under invoicing is the main factor for ineffective implementation of VAT.

Koirala (2011) submitted his thesis titled "A Study on VAT: Implementation, Problem and Its Effectiveness in the Nepalese Economy". Koirala concluded that there are many problems on this field. Level of awareness of the accountant and businessman paying VAT is at low level on some provision of VAT Act. Their knowledge is very important so that proper use and implementation of VAT system can be ensured. Likewise, revenue administration has various issues that can be improved with good attitude of people. The implementations of VAT in Nepal have poor results than expectation. The reasons are poor planning, unaccountable staffs, weak and corrupt bureaucracy etc. Different education programs, seminars etc. should be organized for taxpayers as well as general public in all over the country with the objectives of aware them about VAT which helps to bring more and more tax payers in the tax circumference. Likewise the VAT system can be developing by adopting automatic billing system. In order to make VAT effective, it is essential to create an environment in which invoices are issued properly, accounts are maintained accurately, tax is based on transactions, and fair competition among industrialists and businessmen is established with respect to tax.

CHAPTER-III

RESEARCH METHODOLOGY

3.1 Introduction

Research is a systematic and organized effort to investigate a specific problem that needs a solution. This process of investigation involves a series of well throughout activities of gathering, recording, analyzing, and interpreting the data with the purpose of finding answers to the problem. Thus, the entire process by which we attempt to solve problems or search the answers to questions is called research (Wolf & Pant, 2002).

Research methodology is a research method used to meet the specified objectives. It is a systematic way to find out the probable solution. It refers to the various sequential steps (along with rationale of each step) to be adopted by a researcher in studying the problem with certain objectives in view.

3.2 Research Design

The research design is a plan, structure and strategy of investigation conceived so as to obtain answers to research questions and to control variance. The plan is the overall scheme or program of the research. It includes an outline of what the investigator will do from writing the hypothesis and their operational implications to the final analysis of the data. The purpose of the research design is to provide a maximum amount of information relevant to the problem under investigation. This research study is concerned with past phenomena both numerical as well as opinions. This study is both descriptive and analytical.

3.3 Population and Sample

The population for this study was comprised of the entire person belonging to or associated with Value Added Tax in Nepal including Tax administrators, Experts Companies /Traders / Entrepreneurs and Customers. In order to fulfill the objectives of the study, 50 samples from the population in the Kathmandu Valley were carefully selected. The respondents were divided into four groups. The following table shows the groups of respondents and the size of samples.

Table 3.1: Group of respondents and size of samples from each group

SN	Group of respondents	Sample Size
1	Tax Experts/Auditors	20
2	Tax Administrators	5
3	Companies / Entrepreneurs	10
4	Consumers	15
	Total	50

3.4 Nature and Sources of Data

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

a. Primary Sources

The primary data were collected through following techniques:

- i. Interview
- ii. Questionnaire
- iii. Telephone queries
- iv. Discussion with resource persons
- v. Field Survey

b. Secondary Sources

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

- i. Published and unpublished reports, articles and dissertations on the concerned subject
- ii. Published documents of National Planning Commission
- iii. Publication and annual report of Inland Revenue Department (IRD)
- iv. Different publication of Central Bureau of Statistics.
- v. Publications of Nepal Rastra Bank
- vi. Various books written by tax officers and scholars
- vii. Publications, Budget Speeches and Economic Survey of various fiscal year of Ministry of Finance, the Government of Nepal.
- viii. Newspapers, such as Kantipur Daily, The Kathmandu post, The Himalayan Times Gorkhapatra, The Rising Nepal and so on
- ix. Publications of various VAT Department.
- x. Various Websites

The collected data through secondary sources have been tabulated in different ways according to the requirements of the study.

c. Data collection Procedures

A total 50 sets of questionnaire were collected from selected respondents in order to get actual and accurate information. Distribution work was done personally through email / physically to get accurate and actual information in time.

d. Procedure of Presentation and Analysis of Data

In the process of presentation and analysis of the data, various statistical tools were used in order to get the meaningful result. Collected data from primary and secondary sources were first processed for tabulation and analysis. The tools such as average, percentage, ratio analysis and various established formulas were used to present and understand. In this study, pie-charts, line charts, graph, bar-diagram and trend line have been used to present the facts and information. The conclusion was drawn on the basis of analysis to explain the real crux of the problems.

CHAPTER -IV

VAT IN NEPAL AND EVASION

4.1 History and Development of VAT in Nepal

The concept of Value Added Tax is originated from Germany in 1919. At the meantime, Dr. Whelm Von Simons developed the philosophy and principle of Value Added Tax by recommending it for Germany to replace the turnover tax (multistage sales tax) and to avoid the problems of cascading effect. Professor Thomas S. Adams recommended Value Added Tax for the USA in 1921. A detailed structure of Value Added Tax was designed for Japan in 1949 to replace the existing enterprise and to turnover taxes. Due to the new concept and fear of its complicated nature, these countries could not introduce Value Added Tax immediately. France introduced Value Added Tax for the first time in 1954. Ivory Cost introduced the Value Added Tax in 1960. While Senegal adopted it in 1961, Denmark and Brazil implemented in 1967.

Among the SAARC countries, India introduced MODVAT (Modified Value Added Tax) in 1986 for manufacturing products in order to correct excise duty Pakistan, Bangladesh and Sri-Lanka adopted Value Added Tax in 1990, 1991 and 1998 respectively.

In Nepal the concept of introducing Value Added Tax was developed along with the Eighth Plan (1992-1997) when the government indicated its intention to convert the import/manufacturing level sales tax into Value Added Tax in that document of plan. Preparation of VAT was initiated in September 1993 when VAT Task Force was created in the sales tax and excise department in order to make the necessary preparation for the introduction of Value Added Tax. A VAT

steering committee was also formed to evaluate and monitor VAT preparatory activities. After the deep study on various aspects relating to the structure and operation of VAT, the task force prepared the draft of VAT law in 1994. It was discussed in depth at several stages within the taskforce with concerned parties. After reviewed by the steering committee the draft was sent to various business groups for their comments. Most of the business community showed their dislike to the VAT which was scheduled to be operated two months later. Business persons protested the decision of the adopting of VAT with the slogan “NOVAT” issue of VAT resulting in a conflict between the government and the private sector. Confrontation continued for a long time (Bhattarai & Koirala 2007).

In September 1995, along with the formation of coalition government, committed to introduce Value Added Tax in the same Fiscal Year 1995/96. The VAT bill was presented to the parliament on December 1995 as per parliamentary process, it was referred to the finance committees (a parliamentary committee) and the committee returns the bill to the parliament on same month together with its report for amendments to a few provisions. The lower house of parliament passed the VAT bill on same month while upper house of parliament passed it on January 1996. The royal seal was provided to Value Added Tax act 1995 on 21st March, 1996. For the effective implementation and administration of VAT, the government established one VAT department in center and seventeen VAT offices in different districts by changing the name of sales tax and excise department and its offices as Value Added Tax department and Value Added Tax office respectively in 16th July, 1996.

The act finally came to force as the government specified the date of implementation of VAT by publishing in the Nepal Gazette on 16th November, 1997. However, it could not be implemented in full phase until the Fiscal Year

1998/99 due to political instability and strong opposition from the business community after the compromise with business community; the government has implemented Value Added Tax in full phase since 17th July, 1998. It has been introduced as an improved indirect tax for the replacement of the sales tax. It also replaces hotel tax, entertainment tax and contract tax and has been supported to collect the same revenue as the four taxes it replaced. Nowadays, Value Added Tax is administered through Inland Revenue Department and Inland Revenue Offices as Department of Value Added Tax and Department of Taxation are merged as Inland Revenue Department since 17th July, 2001.

Nepal has adopted broad based consumption type Value Added Tax with credit method. This means, the tax base is domestic consumption only. Some social welfare services, educational goods and services, cultural goods and services etc. are exempted from tax. VAT with single rate of 10 percent has been increased to 13 percent with its effect from 15th Feb., 2004.

4.2 Structure of VAT in Nepal

In Nepal value added tax (VAT) is administered under Value Added Tax Act 1995 and VAT Rules, 1996. It is a tax on goods and services consumed in Nepal. The tax is based on the principle that each producer or distributor adds value, in some way, to the materials they have purchased and it is added value that is taxed at each stage of the production and distribution chain.

4.2.1 Procedures of tax compliance

There are certain incentives given to tax payers to make compliance with the provisions of VAT. The prima fascia commitment of the tax compliance is understood by the tax registration.

4.2.2 Tax registration

It is essential to have registration of all taxable producers, sellers, and suppliers. In other words a person (individuals and legal persons) who is involved in a commercial activities and the turnover exceeds the given threshold is required to register for VAT. However it is not necessary to register who deals only non-taxable goods and services. Similarly those persons who fall below than the defined threshold are not necessary to register. But the thresholds are different for various purposes i.e. Rs.100,000 for consultancy and Rs.10,000 for transportation in specified location. In some extent these provisions have created the confusions. Similarly, the registrant is entitled to collect VAT and utilize the facility of tax credit and refund (IRD, 1995).

4.2.3 Provision of deregistration

A VAT registration may be cancelled by anyone whose total taxable sales for four consecutive calendar quarters is not more than the threshold specified and who has been registered for a full fiscal year or by persons who no longer have a commercial activity. The Act has mentioned other conditions regarding the cancellation of registration. In case of corporate body, the organization is closed or transferred or collapsed, if the business is running under proprietorship and owner is died, if the partnership is dissolved or dead of any partner, if the distributor or producer stops to sale or produce taxable goods or services or if the business is registered by mistake, the it may be deregistered by the tax officer. But the de-registration process is very harassing and very few numbers have been de-registered in against large numbers of registrants have been requested for deregistration (IRD, 1995).

4.2.4 Self-assessment

The registrants are entitled to assess or compute the tax and return the file by themselves. In this system taxpayers determine the tax liability by themselves

and file the return in concern Inland Revenue Office. It is mandatory to file the return whether there is business transaction or not. But if there are no any sales, the registrant should file zero return. Voluntary registrants or who have the sales less than the threshold may file by four-monthly return (IRD, 1995).

4.2.5 Tax refund

The difference between the VAT collected on sales and charged on purchases determines the amount a registrant must remit or the amount that may be claimed as a refund. In other words if the tax on sales is more than the tax on purchases the person remits the difference. If the tax on sales is less than the tax on purchases the person claims a refund for the difference with 15 percent interest. But the interest will be calculated since after 60 days of the application submitted for refund. If a taxpayer has more than 50 percent of export of his gross sales, he is entitled to refund the tax immediately. However the refund process and procedures are lengthy and complicated (IRD, 1995).

4.2.6 Tax payment

The producers, suppliers and sellers are the agents for tax collection on behalf of VAT Department or VAT administration. If the tax return shows the debit balance the registrants should pay the tax at a bank or at concern IRO where he will receive a voucher with number as proof of payment (IRD, 1995).

4.2.7 Tax credit

Tax credit is a facility for taxpayer. Under this system a producer or distributor can deduct the tax paid on input or purchases from the tax collected amount. The difference amount determines the amount of tax to be remitted in treasury or claim for refund (IRD, 1995).

4.2.8 Zero rates on export

On export VAT is imposed on zero rates and tax paid on purchase can be credited or refunded (IRD, 1995).

4.2.9 Taxable price: VAT and treatment of discount and commission

Regarding the taxable price discount, commission and sales bonus are exclusive. For example, if a taxpayer sells its product in cash and he provides the trade discount or cash discount deducting from price and he shows the same in tax invoice, the net price after deducting the discount or commission is taxable (IRD, 1995).

4.2.10 Hire purchase sales system and VAT Collection

Under the hire purchase system purchaser will pay the price value of sold goods in various installment and the supplier should collect VAT when buyer does pay the cash as agreed installments under agreed sales scheme. If there is no any written agreement or sales scheme, the tax should be collected at the time of issuing sales invoice or transfer of goods (IRD, 1995).

4.2.11 Partial use of goods and tax credit

The VAT Act and Regulation also has provided the facility of tax credit on partial use of goods or expenditure. If a producer purchases some raw material and he uses the material to make both taxable and non-taxable goods. If it is possible to identify the used proportions, the producer is entitled to claim tax credit in extent of proportion used for the production of taxable goods, which one is earlier (IRD, 1995).

4.2.12 Second hand goods and treatment of VAT

Regarding the business of used goods, laws have made separate provisions. Under this provision for the calculation of VAT, the taxable value will be

calculated by deducting the purchase from sales. However the taxpayer is not entitled to credit the tax paid on purchase of those second hand goods purchased for resale (IRD, 1995).

4.2.13 Provision of fee and penalties: Interest and Fee

If a registrant fails to pay the any tax during the period prescribed by law or on and before 25th day of next month of tax period, the registrants is liable to pay additional amount of 10-percent/per annum as additional fee. But this fee can be dismissed by Director General (DG) of IRD. In case where, the taxpayer fails to pay any tax to be paid under VAT Act, he is liable to pay interest in due amount at the rate of 15 percent per annum. The taxpayer is also liable to pay interest in the case of appeal to tribunal against tax officer's decision. Regarding the penalties, there are two types of penalties; one is penalty in the term of money and other one is non-economic or not in monetary term. In monetary term the penalties are imposed:

- for failure of registration- Rs.10000 for every tax period and collection of tax,
- for failing to use or mention the registration number-Rs.1000 for every turn,
- for failing to display registration certificate-Rs.1000 for every turn,
- on non-issuing the invoices- Rs.5000 penalty for every turn plus collection of tax,
- for collection of tax by non-registrants-collection of tax plus 100 percent penalty,
- for failing to keep the accounts up-dated Rs.10,000 for every turn,
- for obstruction to visit of tax officers-Rs.5000 for every turn,
- for failing to mention the information such as date and amount of sales, registration number of buyer (if it is registrant)- up to Rs.5000,
- for failing to keep certified purchase and sales books- Rs.10,000,

- for failing to preserve the accounts up to 6 years- up to Rs.5000,
- for failing to file return in due time- 0.05 percent of tax or Rs.1000 (for every tax period) which one is less,
- for under-invoicing-Rs.2000 for every bill/invoice or penalty up to 100 percent of tax which one is less,
- for preparing false accounts, documents or invoices- penalty up to 100 percent of tax or imprisonment up to 6 months or both,
- for evasion of tax- penalty up to 100 percent of tax or imprisonment up to 6 months or both,
- In case of under-invoicing, penalty up to 100 percent of tax or imprisonment up to 6 months or both.

Similarly, every taxpayer is liable to keep the accounts in defined format. Otherwise tax officer may audit the transactions and may impose the penalty (IRD, 1995).

4.3 Weakness and Problems in the Implementation of VAT act in Nepal

Previously hotel tax, sales tax, contract tax and entertainment tax were administered by separate Acts. In 1995, VAT was introduced in Nepal, it replaced other acts and all taxes were incorporated under VAT Act. It is proved experience that VAT is a scientific and modern tax system. It is assumed that it is broad based that has higher enforcement capacity and higher deepening power. But in Nepal, the implementation experiences are not so very strong. Policy inconsistency and frequently change in laws is one of the remarkable shortcoming. Revenue leakage has not been controlled as desired. The mechanism is not functioning properly.

The government has defined different VAT-exemption thresholds to promote small-scale businesses. Businesses with taxable transaction of goods worth up to Rs 2 million of services worth up to Rs 1 million, and of mixed transaction of goods and services worth up to Rs 1 million in the last 12 months are not subjected to VAT. This benchmark for business organizations/vendors is not needed since the value-added-tax in the product/service chain is actually being paid by the end customer. Moreover, this yardstick only allows room for businesses to play foul. In many cases, a business organization doing the buying/selling is registered as numerous sub-organizations on paper. Later, during auditing, the transactions of a single business are distributed among multiple sub-organizations, each showing a transaction less than the demarcated threshold of tax-exemption. VAT avoidance and evasion of similar kinds have caused sizeable tax loss. The VAT-dodging situation is further aggravated by weak law-enforcement at both the customs and Inland Revenue Department (IRD). There are multiple instances of goods being under-declared at customs office and products being under-billed, billed with fake invoices or not billed at all in consumer markets. Forged tax bills are deemed punishable by VAT Act; however, taxes invoices, refund claims and export documents are forged at an alarming rate by many businesses.

Nepal government only recognizes and authenticates valid VAT bills presented during audits. This is good. There is also a provision of identifying VAT payment discrepancies by comparing tax paid on similar transactions between two or more registered VAT payers. But, without coupling these moves with the compulsory use of fiscal printers and electronic cash machines in businesses, desired output cannot be expected. This provision has also hit a bump because a majority of ordinary businesses like tea and vegetable shops aren't required to produce VAT bills. But those who are required to produce such bills do so by intimidating buyers or producing fake bills themselves. Sadly, consumers cannot

differentiate valid bills from forged ones. There are numerous instances when taxes from end consumers through forged VAT bills are not reported to government, causing misappropriations of paid taxes. But the government has been overlooking this aspect. The huge VAT fraud by big companies that surfaced in 2011 substantiates the claim of widespread misuse of VAT system. Misappropriation worth approximately Rs two billion took place in this swindle. Although the government tried to keep defaulters' name secret, reports claimed that around 385 firms were evading taxes by producing counterfeit VAT bills. Many of these firms are big corporate houses of Nepal. If a system that works with minimum glitches in other parts of the world fails in Nepal, the problem surely lies in its implementation: both at the government and consumer level. Lack of consumer awareness and absence of fear of punitive action have contributed to VAT evasion. As corrective measures the government should start cancelling transaction threshold, introduce standardized VAT bills, initiate VAT awareness campaigns and ensure strict monetary and penal actions to those who flout VAT rules. Moreover, businesses shouldn't be allowed to print any type of bills without authorization from Inland Revenue Department. Many people might not know that the VAT Act states a monetary reward equal to 20 percent of the amount of tax recovered to the person who provides evidence of tax evasion by a legit VAT payer. Making such provisions public can also help check tax fraud at citizens' level (Republica, 2014).

The weakness can be listed as:

4.3.1 Weak mechanism of billing enforcement activities

Since VAT is based on bill system, the issuance of proper bill is very important for the successful implementation of VAT. In other words, the success of VAT depends on bill issuance by Traders and compulsory receipt of bill issuance by customers. In case of Nepalese market, billing system is not effective and still not

improved. So the widespread proactive of not issuing VAT registered bill while selling goods is still an impediment in the effective implementation of VAT. The system of asking for bills while purchasing goods has not developed so far despite government's commitment and efforts. Due to the lack of public awareness about the billing system, very few people ask for bills for their purchases.

Businessmen registered in VAT offices, holding VAT certificates, fulfill just formalities but avoid issuing bills for every transaction. Besides that, most of the firms do not issue bills. They issue parallel bills, loose bills and maintain parallel accounts, one for tax purposes and another for business purposes. Consumers too are not much interested in taking bills since the VAT amount is extra charged if they demand a bill. If any consumer asks for a bill, they would charge 13% more as VAT on top of the price. So general consumers do not ask for VAT bills (Koirala, 2011).

4.3.2 Narrow Tax Base/Coverage

The base of VAT is narrow, both legally and administratively. For example, several sources of income including agriculture, export, capital gains, dividends, fringe benefits etc. still have deliberately been kept out of the VAT net. Exclusion of agriculture, the biggest sector, alone cuts the tax base by almost 40% of GDP. An attempt was made to limit the number of exemptions under VAT until the introduction of VAT, but the number of exemptions increased substantially after the implementation of VAT. Many exemptions, deductions and rebates are granted under the Industrial Enterprises Act. Similarly, large numbers of exemptions are granted under the customs duties. Similarly, high exemptions are granted under the house and land tax. Excise duties are currently levied only on domestic products, keeping imports outside the excise net. Almost 70% of the economic activities that account for GDP are virtually out of the tax net.

Economic activities brought under the tax net are also not tapped effectively mainly due to the lack of strong political commitment and weak tax administration. This has been reflected in the low number of taxpayers and low revenue collection (Kandel & Lamsal, 2011).

4.3.3 Smuggling, Under Valuation and Unauthorized Trade

Nepal has long open border with the both neighboring countries India and China. However, the border with China is not being a serious problem due to the geographical inconveniences caused by the mountain area. There is no easy way to pass through the Chinese border and hence level of illegal trade is negligible. But the open broader with India is being most challenging issue and problem is still alarming. People of the India and Nepal may easily enter one another's country and buy goods not paying customs duties for personal use. However, major problem is due to the large volume of smuggling and under valuation transaction by business enterprises, rather than consumer. Once the goods are entered into the country by an undervalued billing, VAT revenue along with customer duties is lost and that cannot be caught up in successive stage of distribution. Similarly, the goods, which are entered through the illegal route, remain completely beyond the VAT net. Thus, a major problem for effective implementations of VAT is created by a large volume of smuggling and under valuation while importing goods from India. Besides that, there is not any measurement of unauthorized trade between Nepal and India. Many Businessmen have claimed that only a little amount of goods from India come through customs. So it seems, unauthorized trade is very much organized and systematic in the border area (Koirala, 2011).

4.3.4 Weak Tax Administration

An effective and efficient administration is crucial for the proper implementation of VAT. But in Nepal, VAT administration is still in traditional nature and corruption is being a major problem. Transparency is being only a nice slogan but lacking in real field. Tax officials are not given specialized training on various aspects of taxation. Some of the Tax Officers are still not familiar with the basic and essential concepts of VAT and even new entrance to the tax administration are directly posted to field officers without being given any basic training for their jobs. There is lack of adequate auditors, treaty negotiators and trained personnel on various aspects of taxations. There is also no system of performance- based evaluation of the tax officials for promotion to higher levels. Due to the weak tax administration, there is a big gap between legal system and its actual operation. Besides that, administrative inefficiency is another most serious problems for implementing VAT for effective implementation, qualified, intelligent, well-trained manpower are necessary. Many Businessmen are illiterate and cannot prepare their accounts properly and they are facing many problems while maintaining accounts. So tax administration must provide basic ideas to the Traders and co-operate private Traders. Previously, under sales tax system, bills/invoices related to hotel and entertainment tax were used after stamped by the concerned tax office. The contract tax used to be deducted at source on contract amount and contract tax used to be certified by the concerned office/officer. At the time of making assessment of income tax of the concerned contractor, the contract amount and contract tax was reconciled by the tax office/officer. But the provisions made under various laws have not been effectively implemented. For example the goods exceeding Rs.10,000 thousands from traders, not having VAT registration, is not likely to be monitored due to prevailing habit in market to issue two types of bills. The tendency of issuing plain bill or not issuing any bill has not been minimized. The provisions of

purchase of under value of goods and suspending the business have not been effectively implemented. Penalty provision for preparing false account or invoice and other documents has not been effectively imposed (Koirala, 2011).

4.3.5 Weak Public Consciousness Level

Public consciousness is a basic element that should be at higher level in the people so that the government policy and program can be guided at the right direction for achieving objectives of any government policies and programs. In the context of Nepal, if has a poor public consciousness has been misinterpreting and also misguiding VAT to the people by saying that VAT certainly raises the price level of goods. But there is no voice against such misguidance and misinterpretation. The Consumers, who are really interested to make the VAT effectively successful, want to get VAT bills on their purchases but they are not getting such bills from the business community. Most of the Consumers do not demand VAT bills when they are asked by the Businessmen to pay a 13 % more amount to get VAT bills. But they do not know the fact that Businessmen are covering the VAT amount into the price of the product indirectly. Thus, by non-issuing proper bills, Businessmen are cheating revenue to the government as they are collecting VAT amount from Consumers indirectly so far as the Consumers remain unfamiliar with the different theoretical aspect and existing rules and regulations of the VAT, the problem will remain in existence. Thus, very weak public consciousness level about VAT is being one of most significant problem, for the proper implementation of Nepalese VAT system. A successfully effective VAT will be the result when issuance of invoices is effective through high level of public consciousness (Koirala, 2011).

4.3.6 Geographical Barrier

Geographical situation of our country has created an important issue about the applicability of VAT in Nepal. The land distribution seems to be extremely unequal. Such geographical condition has arisen several problems in the path of application of VAT in Nepal. In the remote areas where the people must bear the burden of higher prices of commodities due to services rendered by porters, animals and air transport. Besides these, the burden of VAT is higher in the remote areas than in other accessible areas, which is clearly inequitable and unjustifiable. So the higher price level of commodities discourages completely the VAT. In spite of that, there are small –scale business activities in the remote areas. The revenue collection in such areas would be negligible amount as compared to collection cost. Therefore, the high collection cost does not permit VAT to be applicable in some of the districts in Nepal. Similarly, controlling and monitoring system of VAT in far and remote areas is not easy due to the lack of transport, communication etc. It is difficult to control the many functions of VAT like inspections, audit, tax refund, penalty and appeal in the remote area due to the lack of adequate Tax Officer (Koirala, 2011).

4.4 Drawbacks of VAT Act in Nepal

In Nepal, after intense debate and deliberation, it was implemented first in 1997. However, it is felt that its positive impacts are yet to be fully realized even after almost 22 years of implementation. The main problem that the government is facing each year is lack of compliance by all taxpayers due to various reasons.

First, to start with the positive impact that VAT laws bring is taxation at every stage of supply chain and credit to taxes paid on inputs and on input services. Therefore, the foremost good factor that VAT laws bring is the removal of

cascading effects. The term cascading effects refer to 'tax on tax'. Therefore, VAT shuts door for multiple taxation, thereby removing cascading effects in supply chain as every buyer and seller will be entitled to avail input tax credits and adjust its credit with its output tax liability. In principle, we have understood VAT laws to be so.

However, in practice, not necessarily the implementation of VAT laws always removes cascading effects. Therefore, we need to have an effective and good VAT law that alone brings the intended consequences to the tax payers. In practice, what has been observed is the concept called 'exemption of taxes' on 'exempted goods and services' which act as a barrier to smooth supply chain. Mainly, the essential goods and services, for example rice, pulses, flour, fresh fish, kerosene, salt, health services, contraceptives, medicine etc. are exempted from payment of VAT on a simple rationale that these commodities and services are essential for human survival and imposition of taxes will increase the price of these products thereby making it inaccessible and expensive for poor citizen of our poor country. Morally and ethically too, this sounds a great welfare measure taken by the state. But, in practice and in a world which is full of profit making enterprises, this rationale does not work so greatly as think it to be. We can understand the tax exemption behind the agricultural products like wheat, paddy, flour etc. and agricultural tools, shovels, etc. But, Nepalese VAT law even exempts taxes on air travel, gold and silver, mobile phone set etc. which is beyond anyone's understanding and these types of exemptions have only accentuated the obstacles to smooth supply chain.

While the output goods and services are exempted from the payment of taxes for those goods mentioned in Schedule – I of VAT on its output side, it may not be so in case of input goods/services. Therefore, a vendor who purchases raw materials and services, and manufactures an exempted product, say medicine,

cannot utilize its input taxes that it has paid on inputs. Its input tax credit will go to become a sunk cost. In this situation, the only options available to the manufacturer/seller would be to add up the cost of taxes paid in inputs in its final outputs and pass that cost to the customer if manufacturer/seller has to keep its business running. Therefore, while declaring certain goods/services as exempted goods/services, the government is not doing any yeoman's service to its citizens except those few essential goods.

Keeping goods and services exempt will also have another round of disadvantages – that is to the vendor which buys these exempted products and services, utilizes these input goods and services for manufacture and sells its outputs which are taxable in nature. In this case, this vendor will not have any input tax credit and has to collect the tax amount from the public/customers, which will only increase the price of these products.

Internationally, it has always been a moral dilemma among legislators/governments to frame effective VAT laws containing provisions that leave entire supply chain unaffected. Since revenue and fiscal laws stand on the different footing than other laws, they are enacted as per the economic and fiscal needs of the nation unlike other general laws which may be enacted to curb one or the other evils. Government will also make use of tax laws to control the flow of goods and services as per demand of the country on the prevailing economic condition. Therefore, though it may be desirable not to have 'exempted products/services' at all, but practicality, does not allow this to happen. This is fully understandable. Having said so and being fully aware of the government's constraints, the challenges posed by exempted goods and services in supply chain is not that difficult to address if genuine efforts are made and willingness are shown by the government.

Arguably, the easy and effective ways to curb the threat posed by exempt products/services are to make them taxable by declaring the rate of tax at Zero Percentage for these products/services. This is internationally known as ‘Zero – rated goods/services’. Our Nepalese VAT law has already enumerated this concept but only few categories of items and transactions find place in Zero-rated list.

Currently, the exports are Zero – rated which is in consonance with international tax principle that only the products/services be exported and not the taxes so that our products become competitive in international markets. Other Zero rated transactions in the list are the supplies made to industries located at Special Economic Zone (SEZ), battery used in solar power generation and manufactured by domestic manufacturers etc. The need of the hour is to reduce the number of items/services and transactions currently mentioned at Annexure – I of VAT and move them to Annexure – II so that exempt products would be converted to taxable one, i.e. to convert them to ‘Zero-rated’ goods/services.

By introducing the concept of ‘Zero – rated’ for maximum number of goods and services, the goods and services would get taxable life – making inputs utilized for producing these zero rated goods creditable. Though there may not still be output tax liability, the vendor would be able to use the credits that it has accumulated while producing/distributing ‘Zero – Rated Goods’. Therefore, the expansion of this concept in VAT laws will make a good impact on the business community and ultimately, the impact will be felt by the consumers. A small effort from government side can make a big difference.

Another possible remedy that can be injected to streamline the credit mechanism would be rather than making these products exempt, a small VAT should be imposed on them. In Nepal, currently, there are only two VAT rates – 0% and

13%. In this context, a middle path can be found making majority of currently exempt products taxable, say at the rate of 1%-3%. Though imposition of tax may make these products little more expensive and may not go well with 'people – centric!' political class but we must understand that imposition of tax at small rate will not be so burdensome on us- the public and on the other, and helps not to snap the supply chain.

From the point of collection of revenue too, mostly these products are relatively inelastic and therefore, will not have any impacts on their demand. There would be more positives to the economy in the long run with these measures which may not at first glance, look so populist. This second prescription is recommended only when government is unable to declare exempt goods as 'Zero – rated' having constraints due to other economic factors. Whatever government does, however, should be for giving impetus to economic development and should propel our economy to forward direction (Dahal, 2012).

Krishnaswamy and Sinha (n.d.) lays down various anomalies of current VAT Act in the article published in www.nepalcastudent.com. According to them, though various amendments are made from time to time to correct such anomalies but some time even the tax officers are not able to give a correct opinion regarding the effect of conflicting sections, when approached for clarification. Thus, the transparency in the statutory provision is at a discount. Few of such anomalies sighted by the writers in the article are given below in VAT Act, 1995 and VAT Rules, 1996.

Sec. 8(2) of VAT Act, 1995 lay down that when a service is received within Nepal from any unregistered person residing outside Nepal, then the person receiving the service will have to assess the tax on the taxable value and collect the same in accordance with the Act and Rules. This is opposite to the exemption

given to services exported out of Nepal under schedule 2 on the concept that VAT is a consumption tax leviable on the residents of Nepal. Under Sec. 8(2), the importer of services has to collect the tax and pay the same on the taxable value according to the Act and Rules. Sec. 12(1) says that unless otherwise provided in the Act, the cash received by the supplier is the taxable value.

Rule 18(7) of VAT Rules, 1996 lays down the sale for ascertaining the tax on Summary tax. Bills to be calculated as; $\text{Tax rate} / (\text{Tax rate} + 100)$. Now the bill made by the service provider cannot be treated as a Summary tax. Bill which is allowed only to those permitted to make summary bill under the Rules. Even though the importer has to pay the VAT but he cannot collect the tax from the exporter and hence the word “to collect” in Sec. 8(2) is an anomaly and it could be conveniently omitted and words “has to pay” could have been more appropriate.

Regarding Filing of Return by Electronic machines under Sec. 16A(2) even though the provision was introduced by the Finance Act 2063 (which has been explained as not valid), no rules are made and all the instructions for filing, the procedure for getting confirmation are oval only from the officers of the department. There may be many persons who do not know about it. The IRD website also does not give any guidance on the procedure for filing VAT returns electrically – no circular or instruction or notices in this matter. Nobody can find out authoritatively from which date filing of returns electronically was introduced or what type of tax payers are covered and the procedural to be adopted for filing the return and getting acknowledgement.

Anusuchi 5Ka of VAT Rules, 1996 prescribes the Bill format under Rule 17(3) for insurance companies and retail traders as shown under the VAT Act and Rules updated up to 2065 at the IRD web site. There are two formats of

Anusuchi Ka. But Rule 17(3) has been deleted from 2062-6-14 but the Anusuchi Ka has not been deleted.

4.5 VAT Evasion and Avoidance in the context of Nepal

4.5.1 Variables Affecting VAT Evasion and Avoidance

Tax administration's efficiency relates to the increment of enforcement to reduce evasion for which it has the power of assessment, reassessment, imposing fees, fine and penalty. Some variables that determine the collection capability of VAT and at the same time provide loopholes for evasion and avoidance are as follows;

Rate Differentiation:

Multiple rates create scope for misclassification fraud of the kind mentioned above. Moreover, where rate differentials are sufficiently large they can also give rise to refund entitlements for some traders (those using inputs taxed at a high rate to produce outputs subject to a low rate of VAT), which, in turn, creates opportunities for fraudulent abuse.

The level of VAT rates:

High tax rates may persuade some individuals to non-compliance. Therefore, it would be counterproductive and the people complain that VAT rate of 13 percent is very high and it has induced evasion and has diverted trade from official routes to non-official routes.

The broadness of the tax base:

Limitation of tax base is another important factor which effects collection capability. The tax base of VAT has been limited due to several exemptions like agricultural products, electricity and others. The exemptions are so large, the collection will never likely to be near final consumption/expenditure.

Registration thresholds:

The number of firms that have to be handled by the VAT administration can be sharply reduced by setting a high turnover threshold. The revenue lost by setting a high threshold may be small compared to the saving of administration costs to the authorities and compliance costs to the taxpayer, because the potential tax base is commonly very strongly concentrated in the largest companies. Moreover, firms not registered for VAT nevertheless face a non-zero effective rate of tax, because they cannot reclaim the VAT paid on inputs.

4.5.2 Methods of VAT evasion

Methods of evasion of value added tax are non-issuance of tax invoices to the buyers, under declaration of goods value at the customs points, fixation of low ex-factory price in internal production and further under valuation by whole seller and retailers. There is no reliable valuation data base either to control valuation fraud in import or in internal production. False claims for credit or refund are the most obvious way to exploit the credit mechanism: “A VAT invoice...” as Bird (2005) puts it, is “a check written on the government.” And such fraud can be extensive. It was known that 44 percent of all VAT fraud found in an investigation in the Netherlands took the form of false claims for tax paid at previous stages, for example by presenting forged invoices for non-existent or exaggerated purchases (Keen & Smith, 2007).

4.5.3 International Aspects of VAT Fraud / Evasion

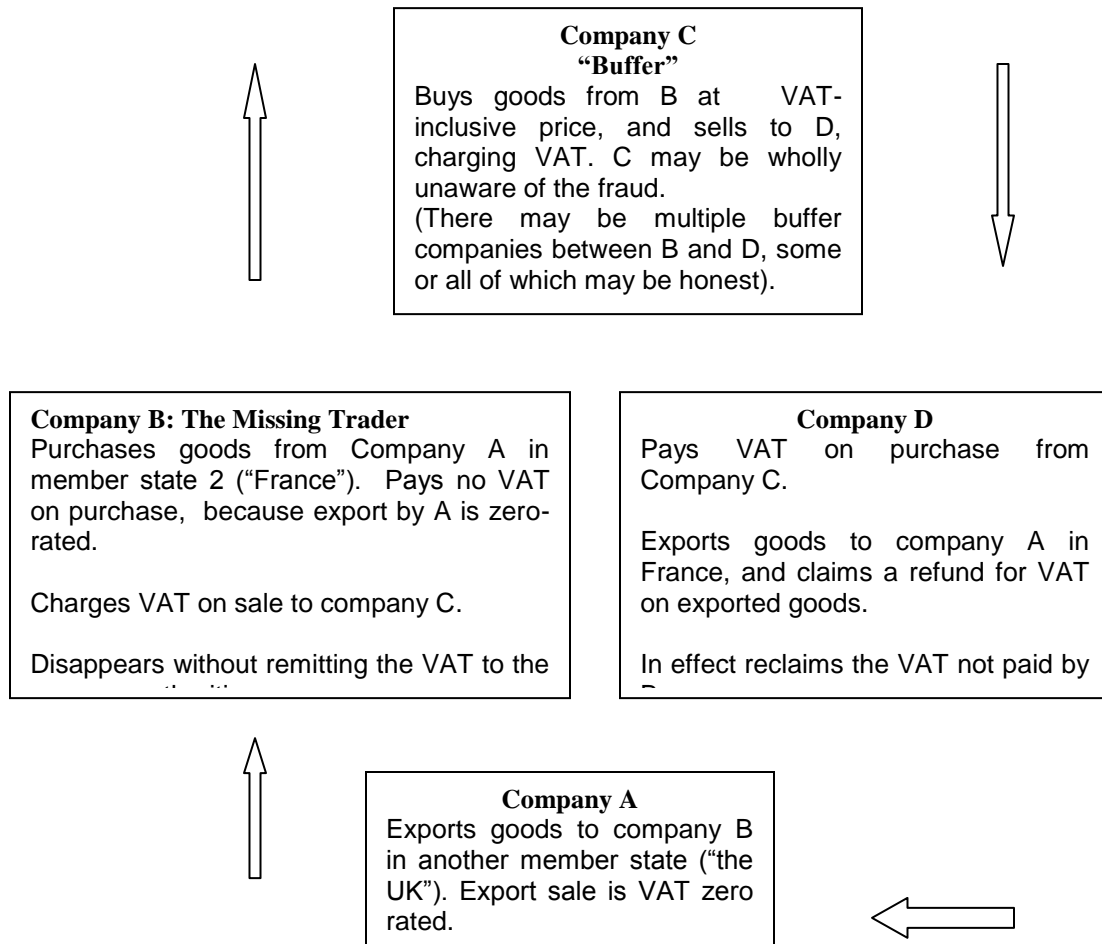
As discussed above, the frauds most distinctive to the VAT exploit are the crediting of tax paid on purchased inputs against the tax due on sales. And it is the zero-rating of exports that has proved the feature most vulnerable to fraud, or at least which has proved especially attractive to deliberate criminal attack. The difficulty with zero-rating exports is that it not only breaks the VAT chain but does so “at a particularly vulnerable spot: the interface of domestic and foreign

tax administrations” (Ainsworth, 2006, p.445). This creates a number of opportunities for fraud, as outlined above. But the best known form of deliberate attack on the VAT system is the “carousel” fraud that has attracted such attention in the EU over the last few years.

“Carousel fraud”—a special case of what is termed in the United Kingdom “missing trader intra-community fraud” (MTIC)—exploits the zero-rating of exports combined with the “deferred payment” mechanism for collecting VAT on imported goods. Under the latter, adopted in the EU with the removal of fiscal frontier formalities in 1992, 15 VAT on imports from another member state is collected not at the border but at the time of the next periodic return.

In the simplest case, illustrated in Figure 1, carousel fraud works as follows:

Figure 4.5.3.1: Working of Carousel Fraud



Andreas and Friedrich (2012) developed a time series of tax evasion (in % of official GDP) for 38 OECD countries over the period 1999 to 2010 based on MIMIC model estimations of the shadow economy. Considering indirect taxation as the driving forces of tax evasion, they observed a declining trend of tax evasion between 1999 and 2010 for all countries. The average size of tax evasion across all 38 countries over the period 1999 to 2010 is 3.2% of official GDP. The country with the highest average value is Mexico with 6.8%, followed by Turkey with 6.7%; at the lower end the United States and Luxembourg with 0.5% and 1.3%, respectively.

4.5.4 Implementation status of provisions of VAT Act to control evasion

Various anti leakage provisions made under the VAT Act 1995 have not been implemented perfectly and such provisions are mainly related to control tax leakage and increase tax compliance. For example the goods exceeding Rs.10,000/ from the traders, not having VAT registration, is not likely to be monitored due to prevailing habit in market to issue two types of bills. The tendency of issuing plain bill or not issuing any bill has not been minimized. The provisions of purchase of under value of goods and suspending the business have not been effectively implemented. Penalty provision for preparing false account or invoice and other documents have not been effectively imposed. Currently issuance of fake VAT bills has been new means of VAT fraud (Ghimire, 2006).

4.5.5 Cases of VAT Evasion under investigation of IRD, Nepal

Inland Revenue Department completed investigation against 468 firms out of a total of 518 cases of Value Added Tax (VAT) fraud scam. The department slapped Rs 4.55 billion taxes and fine to the 468 firms that were involved in evading VAT compliance by producing fake invoices. Revenue worth Rs 794 million has been collected so far out of Rs 4.55 billion. A total of 112 firms have, however, approached the Administrative Review Committee led by director

general of Inland Revenue Department. Out of 112, the committee has already finalized 71 cases, according to the ministry. The taxpayers can file review against the decision at the Administrative Review Committee under the department, if they could not be satisfied with the decision.

Article published in Kantipur (2011) titled “VAT scam: Government makes public companies, firms under scanner” gives the information about the report made public about the fake VAT bill scam by the government. The report has listed names of 385 firms that issued fake VAT bills, their Permanent Account Numbers (PAN) and names of companies that used the bills issued by such firms. The report has also disclosed 35 companies that used fake bills and their PAN numbers. The report has included names of 10 companies that were referred to the authorities concerned for investigation. It, however, does not mention the amount of tax evaded as investigations were on when the report was prepared. However, it has included names of seven firms that received money from the state coffers under the tax return facility. The Inland Revenue Department (IRD) had directed the Inland Revenue Offices concerned to probe 518 companies, including 52 mentioned in the report, terming their transactions suspicious as of mid-April 2011. Of them, probe on 365 firms has already been completed, according to the IRD. The department has slapped tax bills of Rs 3.45 billion on them. As many as 65 taxpayers have applied to the administrative review committee headed by the IRD Director General for a review of the tax bills. As per existing provisions, firms that are not satisfied with the tax amount slapped on them can ask for an administrative review within 60 days of the determination of the fine. They can apply for the review after putting up one third of the total amount that the tax office sought to recover from them. The taxpayers can further apply to the Revenue Tribunal by putting 50 percent bail amount of the total amount of the fine.

Firms that got tax returns on the basis of fake VAT bills

Sarita Enterprises	Rs 5.04 m
Sarita International Business	Rs 5.31 m
Ashutos Impex	Rs 17.22m
Shivashakti Impex	Rs 16.95m
Digambar Trade House	Rs 11.26m
Digambar Trade International	Rs 45.60 m
Bhimeshwor Trade House	Rs 14.33 m

Taxpayers being probed are Morang Auto Works ,BM Enterprises, United Distributors, Him Electronics, Associated Automobiles, Himalayan Enterprises Pvt Ltd, AIT Pvt Ltd, Arun Intercontinental Traders, Wheels Auto, Surya Automobiles, Jyoti Overseas, Shakti Commercial Enterprises, United Shayam Sundar and Danfe Construction JV, United Lama Shyam Sundar JV, United Builders, Bishwokarma Cement, Bama Motors, CGGC Cameliya Project Department of Nepal, Jagadamba Steels, Barun Developers , Bhatbhateni Department Stores, Maruti Cement, CG Electronics, CG Impex, CG Foods , Rasuwa Construction Company, Rajesh Sanitary Ware, CTCE/Kalika JV, Shree Dugar Brothers and Sons, Shree Dugar Auto Clinic, Chandan Wala International, Guras Engineering , M Trade House, Usma Traders, Nistha Traders.

Thirty-one out of fifty-two companies under investigation of Inland Revenue Department (IRD) have been found to evade tax using fake VAT bills. Among those, twenty-four companies had evaded 2.7 billion Nepalese Rupees in VAT and income tax through transactions in fake bills while they had taken back VAT amount of 890 million Nepalese Rupees by submitting fraudulent certification of payments (CNN, 2011). The VAT scam involves large conglomerates such as Chaudhary Group, Golchha Organization, Vishal Group, Shanker Group, Varun Developers, all owned by trading community from India called Marwaris, plus

Bhatbhateni Supermarket of a native Nepalese and even the Chinese contractor of Chameliya Hydroelectricity Project. These include the firms of two sitting parliamentarians of Nepal's Constituent Assembly – Binod Chaudhary, Chairperson of Chaudhary Group and Diwakar Golchha of Golchha Organization. UML, the third largest political party had nominated Chaudhary and Diwakar Golchha was nominated by Nepali Congress, the second largest party in the Assembly (CNN, 2011).

Among the 31 firms investigated under the scam, most fake bills have been found in the name of Jagadamba Steels amounting to 800 million Nepalese Rupees, according to the source in the Inland Revenue Department (IRD). The fair payment of VAT would have only been 38% of total amount; however, after investigation, the tax amount has been fixed to 600 million Nepalese Rupees. Tax evasion implies 13% VAT, 25% income tax and fine of the same amount plus interest at 15% per annum payable to the government that makes 75% of the 800 million Nepalese Rupees i.e. 600 million Nepalese Rupees, informed the source (CNN, 2011).

President of the group, Shankar Lal Golyan who came to Nepal without a penny from India 40 years ago now owns 18 industries. Jagadamda Steels is the largest company of the group. Shanker Group's annual transactions come around 26 billion Nepalese Rupees, claims Golyan in his website. After investigation of 52 firms under the scam, the second list of tax defaulters of 480 firms also include other companies of the group. Pawan Kumar Golyan of the same group is also the chairperson of NMB Bank, Nepal's first commercial bank. Under this group, three companies headed by the group's President Binod Chaudhary and one headed by Arun Chaudhary are also involved in the scam. Fake VAT bills worth 60 million Nepalese Rupees have been found from CG Impex and CG Electronics of the group. CG Foods of the same group is also involved in the

fraud. It is one of the five companies in the final list in course of investigation that has evaded tens of millions Nepalese Rupees through fake bills, informed the source in the IRD (CNN,2011).

Chaudhary Group, that recently grabbed international headlines with its decision to open dozens of hotels outside Nepal, sells LG and CG electronic appliances in Nepal through GC Impex and CG Electronics. CG Foods produces Wai Wai Instant Noodles in Nepal and India, with collaboration of Thai Foods Industries, which has gained popularity in Asia and Europe. Fake VAT bills worth 160 million Nepalese Rupees have also been found from Arun Intercontinental of Arun Chaudhary, lawmaker Chaudhary's sibling. (CNN, 2011).

The IRD investigation also found fake VAT bills amounting 60 million Nepalese Rupees of Him Electronics under Golchha Organization headed by parliamentarian Diwakar Golchha. Him Electronics itself is directed by rising 'major entrepreneur' Shekhar Golchha. Last year, another firm owned by the group, Neoteric Nepal, distributor of information technology, communications and entertainment products such as Nokia, HP and the likes, was also found guilty in previous IRD investigation. The company had come under scanner after it issued VAT bills in advance dates. Since then, the IRD had speculated of transactions in fake VAT bills from the company. However, the biggest tax investigation had been started after fake VAT bills of more than 200 companies were found in a raid of a firm in southeast Kathmandu. Not so popular but another large conglomerate, Vishal Group's United Distributors is also involved in the VAT fraud. Listed under multinational companies in the course of the IRD investigation, the company has evaded 100 million Nepalese Rupees through fake bills. United Distributors deals in cosmetic and daily consumer goods imported from India and other countries. With strong political access to the level of Finance Minister, this group has investments in banks and other financial

institution, insurance companies and trading houses. The chairperson of Vishal Group JP Agrawal also chairs the board of NIC Bank while the group's vice-chairs TR Agrawal and Nirmal Agrawal are members of the bank's board too. NIC Bank is the first bank in Nepal to be provided a line of credit by International Finance Corporation (IFC), an arm of World Bank Group under its Global Trade Finance Program. According to the source, the second list of 480 companies for investigation of fake VAT bills fraud also includes other firms of the group (CNN, 2011).

Bhatbhateni Supermarket owned by Min Bahadur Gurung, who has recently imported a Mercedes Benz car through 'air cargo' spending tens of millions Nepalese Rupees, one of the biggest supermarkets of Kathmandu is also involved in the VAT fraud. The investigation found fake bills worth 80 million Nepalese Rupees from the Bhatbhateni Supermarket that runs chain super stores in Kathmandu. Bhatbhateni Supermarket is one of the five companies currently under investigation that are yet to be confirmed for their tax evasion amount, informed the source. It is also liable to pay 75% of the total worth of fake VAT bills, stated the source. Most companies involved in the scam are owned by Marwaris, the trading community from India, it is a surprise how Bhatbhateni Supermarket also got enmeshed in the fraud, one of the IRD officials noted (CNN, 2011).

Another tax defaulter is Varun Developers owned by Indian investor Ravi Jajpuria's company RJ Corp that rose to fame with introduction of international fast food chain KFC and Pizza Hut in Kathmandu. Besides KFC and Pizza Hut, the parent company has also invested in Varun Beverages, the producer of popular drink Pepsi in Nepal. Varun Developers sells super-luxurious condominiums named Park View Horizons it built in northeast Kathmandu. The company that has put up for sale a single bungalow for 11.9 million to 25.3

million Nepalese Rupees has been found to evade 150 million Nepalese Rupees through fake VAT bills. The tax payable for the company has been decided to be more than 110 million Nepalese Rupees. China Gezhouba (Group) Corporation (CGGC), the Chinese contractor for civil construction of Chameliya Hydropower Station in Nepal is also enmeshed in the VAT fraud. The CGGC had bought fake bills to increase its variation that amounts to 600 million Nepalese Rupees, stated the source for which the VAT payment of the payment could not be found in books (CNN, 2011).

Article published in Kantipur (2011) titled “NIC issues verdict on multimillion rupees VAT scam” where it stated that The National Information Commission (NIC) recently issued a landmark verdict in the regime of right to information giving directive to the Nepal Government Finance Ministry to impart information about the multimillion rupees Value Added Tax (VAT) scam involving around 518 high-profile business people of Nepal. NIC issued a verdict to provide with a photocopy of the VAT evasion study report-2067 BS including its annexes 1, 4 and 7 free of cost by upholding the spirit of the Right to Information (RTI Act-2007). Taranath Dahal had filed an appeal with the NIC in line with the Right to Information (RTI) Regulation-2008 on August 15 2011, citing dissatisfaction over the Finance Ministry's decision of non-disclosure of information on tax evaders. Through the verdict, the NIC has not only issued directives to the Finance Ministry to uphold the letter and spirit of the RTI as a commitment to promote openness and transparency but also explained the overriding effect of RTI laws on other legal arrangements.

Article in Kantipur (2012) entitled “Revenue recovery drive: IRD to suspend bank accounts, businesses of tax defaulters” states that the Inland Revenue Department (IRD) has suspended bank accounts, businesses and fixed assets of more than 100 firms for not paying taxes as part of its crackdown on tax

delinquency. The IRD started its recovery drive on Jan 15 after outstanding tax dues began piling up for a long time and reached more than Rs 24 billion. According to the IRD, outstanding income tax and excise duty amount to Rs 20 billion and the rest consists of VAT and TDS (tax deduction at source).The Inland Revenue Office, Area No 1 of Kathmandu has suspended the bank accounts of 10 firms in Kathmandu for not paying income tax and VAT. The department has also suspended the bank accounts of two firms listed at the Big Taxpayers' Office (BTO). They owe the government Rs 250 million, according to an IRD official. The Kathmandu Inland Revenue Office, Area No. 3 has frozen the bank accounts of another 17 firms. These firms collectively owe Rs 5 million in income tax and Rs 19 million in VAT.

CHAPTER -V

PRESENTATION AND ANALYSIS OF DATA

Economic development is essential factor for every country and government services and public infrastructure are required for economic development. Lacking in public service provisions subverts the efforts to increase people living standard especially in developing countries and slow down the economic growth. It has also observed that governments of many developing countries have failed to provide adequate public services due to many reasons. The most important of them is the lack of tax revenue. Tax revenue in a country serves as life blood for the government. On the other hand, it is also perceived that both tax avoidance and tax evasion are linked with shadow economy and Schneider and Enste (2000) reported that shadow economy is that economy in which people do not show their real income and taxable income that they have earned through legal activities including barter and monetary activities in order to avoid paying tax. Thus, for underdeveloped country like Nepal, the role of taxation in the process of economic development is considerably significant. In this respect, the tax structure has vital role in development and control of evasion is most necessary.

5.1 Composition of Tax Revenue in Total Revenue

Tax revenue is one of the principle sources of the government revenue. It covers theoretically and practically includes following heads such as persons, organizations, business firms and even foreigners who are doing business of consuming goods or using service in Nepal. The composition of non-tax revenue in Nepalese tax system is of the following factors such as charges, fees, fines, forfeitures, receipts, from sales of commodities and services, dividends, royalty, sales of fixed assets, principle and interest payment etc. while there is some

scope of generating more revenue through the rationalization of non-tax sources, particularly improvement in pricing policies and operational performances, these sources cannot be used effectively as a revenue raise since most of these sources are lived not for revenue purpose (Khadka, 1995).

The contribution of tax revenue used to be almost 80 percent and non-tax revenue almost 20 percent. The shares of tax revenue and non-tax revenue in total revenue have been shown in the following table:

Table 5.1: Share of Tax and non-tax revenue in Total Revenue

Rs. In billions

FY	Tax Revenue		Non-Tax Revenue		Total Revenue	
	Amount	%	Amount	%	Amount	%
2007/08	85.15	79.13	22.46	20.87	107.61	100.00
2008/09	117.00	81.58	26.42	18.42	143.42	100.00
2009/10	155.99	87.79	21.69	12.21	177.68	100.00
2010/11	177.19	89.34	21.14	10.66	198.33	100.00
2011/12	211.72	86.64	32.65	13.36	244.37	100.00
2012/13	259.21	87.57	36.8	12.43	296.01	100.00
2013/14	312.44	87.61	44.18	12.39	356.62	100.00
2014/15	374.7	88.60	48.19	11.40	422.89	100.00

Source: Economic Survey 2014/15

The above table shows that the contribution of tax revenue is around 80 percent and non-tax revenue around 20 percent on average in each year. It is clear that tax revenue has significant role in Nepalese economy.

5.2 Policy contribution to GDP

Gross domestic product (GDP) is the total final output of goods and services produced in the country's territory by residents and non-residents, regardless of its collection between domestic and foreign claims. The Tax /GDP ratio measures the consistency of the growth of Tax revenue with the corresponding growth in Gross National Product. This is an indicator of the utilization of taxable capacity.

The policy contribution to GDP is presented in the following table:

Table 5.2: Policy contribution to GDP %

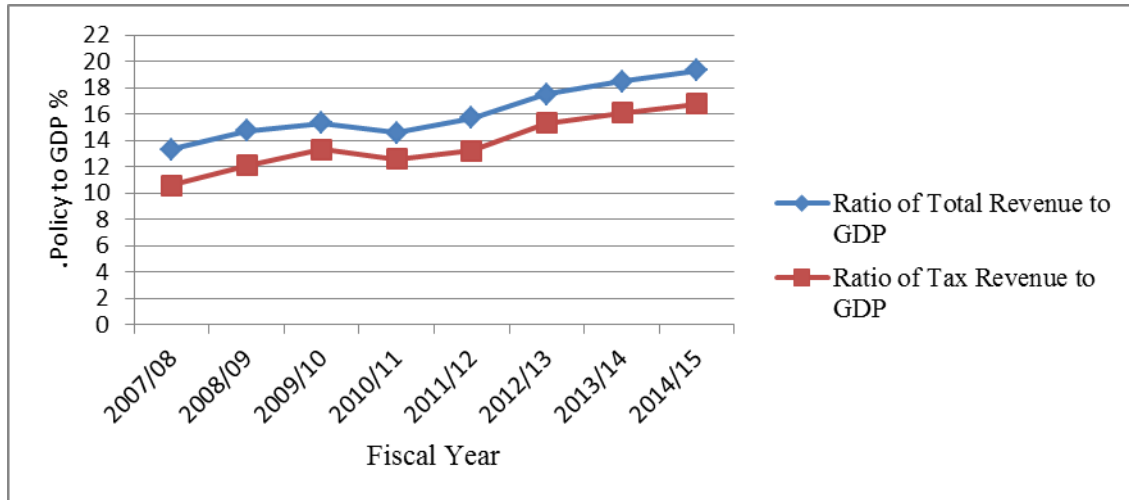
FY	Ratio of Total Revenue to GDP	Ratio of Tax Revenue to GDP
2007/08	13.3	10.6
2008/09	14.7	12.1
2009/10	15.3	13.3
2010/11	14.6	12.6
2011/12	15.7	13.2
2012/13	17.5	15.3
2013/14	18.5	16.1
2014/15	19.3	16.75

Source: IRD Annual Report (2014/15)

Though modern taxation started from FY 2001/02 only, its contribution to Gross Domestic production 16.75% at the end of FY 2014/15, when the contribution of

total revenue to GDP was 19.3%. Ratio of tax revenue contribution to GDP is in increasing trend as shown in the following graph:

Figure 5.1: Policy Contribution to GDP (%)



5.3 Ratio of VAT, Income Tax (IT) and Excise to GDP (%)

The VAT /GDP ratio measures the consistency of the growth of VAT revenue with the corresponding growth in Gross National Product. This is an indicator of the utilization of taxable capacity. Normally, the growth of VAT revenue mobilization in line with the growth in GDP is desirable for the rapid economic development of a country. The collection of VAT revenue is more reliable than the direct tax revenue, non-tax revenue, which facilitates the process of economic planning and development in the country. VAT has been introduced in Nepal to increase the contribution towards revenue generation. VAT / GDP ratio is a measure to check whether the nation generating revenue properly or not.

In developed economies like USA, UK etc. Direct Tax plays a leading role for the internal resource mobilization where as in developing countries like Nepal, Indirect Tax plays pioneering role by dominating Direct Tax with very limited

tax base and narrow coverage, Direct Tax in Nepal seems too less effective to mobilize the domestic resources. Although, it is an inevitable instrument of the fiscal policy, it must be designed and practiced properly. In general, revenue productivity of direct tax goes on increasing as the economy of the country grows over time. If the economy growth increases, per capita income per annum of that country will automatically raise. In depth it means that he/ she possesses the ability to pay direct tax. Thus, the magnitude of direct tax goes up and substitutes in the place of indirect tax's magnitude. Direct tax in Nepalese economy is composed of different taxes namely Income Tax, Land Tax, Property Tax, Wealth Tax and Interest Tax, tax on registration.

Nepal depends heavily on the indirect tax rather than the direct tax because there is not any good alternative especially for the optimum level of revenue mobilization; on hand and on the other hand, wide spread poverty, heavy dependency on agriculture, snail's pace industrialization, low level income and wealth and very wreaked administration. Since 1951, indirect tax had grown rapidly and speedily.

The major component of indirect tax in Nepalese tax structure constitutes custom duty, excise duty, VAT and other tax. Custom duties are composed mainly import duties and export duties. Other component of indirect tax like Sales Tax, entertainment tax, hotel tax, air flight tax, contract tax and other tax contribute very nominal share because they are included in VAT since 1997. Others form of indirect taxes includes remission of Indian excise duties, road bridge tax and other taxes.

According to Keen (2013), in both Asia and Latin America, the average central rate of the VAT increased by about 2% from 1993 to 2012, reaching about 11% and 14%, respectively. Yet the average VAT revenue to GDP rose by 2 % GDP

points in Latin America, while it fell by about 1% in Asia. This remarkable gap in de facto VAT collection can probably be explained by divergent trends in the variation of the actual VAT rates across different economic sectors and VAT enforcement.

The ratio of VAT, IT and Excise to GDP in Nepal is presented in the following table:

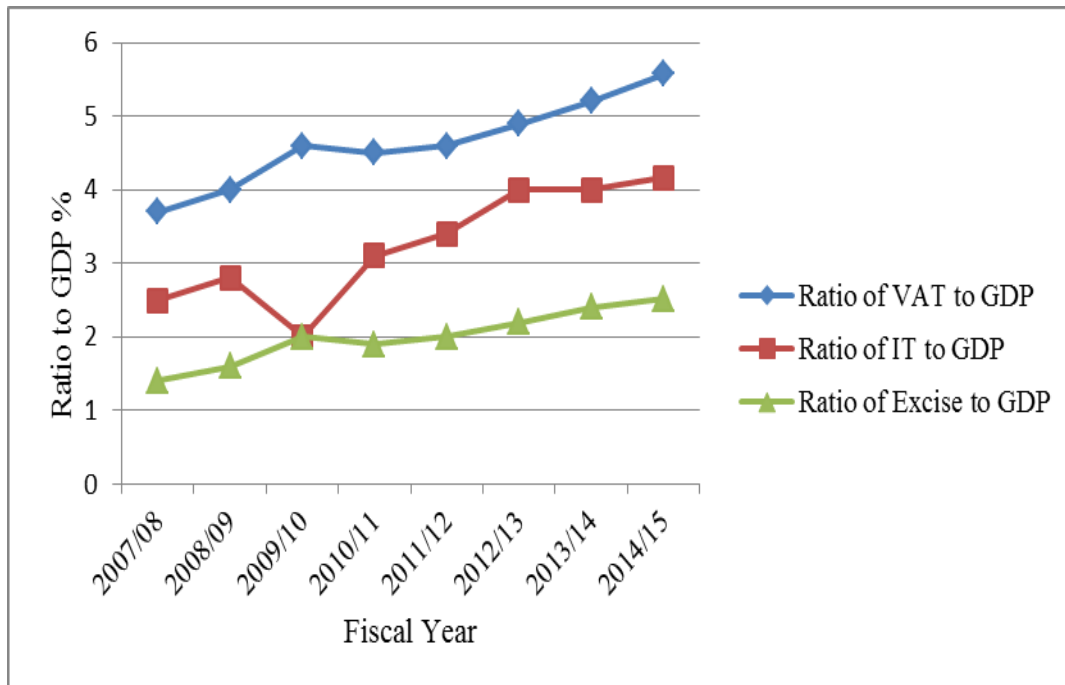
Table 5.3: Ratio of VAT, IT and Excise to GDP %

FY	VAT/GDP	IT/GDP	Excise/GDP
2007/08	3.7	2.5	1.4
2008/09	4	2.8	1.6
2009/10	4.6	2	2
2010/11	4.5	3.1	1.9
2011/12	4.6	3.4	2
2012/13	4.9	4	2.2
2013/14	5.2	4	2.4
2014/15	5.58	4.16	2.52

Source: IRD Annual Report (2014/15)

Contribution ratio to GDP from VAT is highest among Income tax and Excise after implementation of VAT in the country. The share of sales tax/VAT in GDP is 1.90 percent in FY1991/92 and thereafter in increasing trend in all the fiscal year as shown in the following diagram:

Figure 5.2: Ratio of VAT, IT and Excise to GDP %



5.4 Composition of VAT Revenue

VAT is levied on both domestically produced goods and services and imported goods and services. Nepalese economy is agricultural based. More than 60% people are farmer and the farming is unorganized. Agriculture production through unorganized sector is exempted from VAT. Most of the products and services are imported from neighboring countries and third world countries. Thus import generates more VAT revenue than domestically produced goods and services.

The composition of VAT revenue collection from imports and domestic products are shown in the table below.

Table 5.4: Composition of VAT revenue

Rs. In Millions

Fiscal Year	Total VAT Revenue	Domestic Product	Imports
		Amount	Amount
2007/08	29,816	10,808	19,008
2008/09	39,701	13,918	25,782
2009/10	54,921	20,380	34,541
2010/11	61,700	22,390	39,310
2011/12	72,180	25,640	46,540
2012/13	83,500	28,490	55,010
2013/14	100,967	34,397	66,570
2014/15	118,490	39,550	78,940

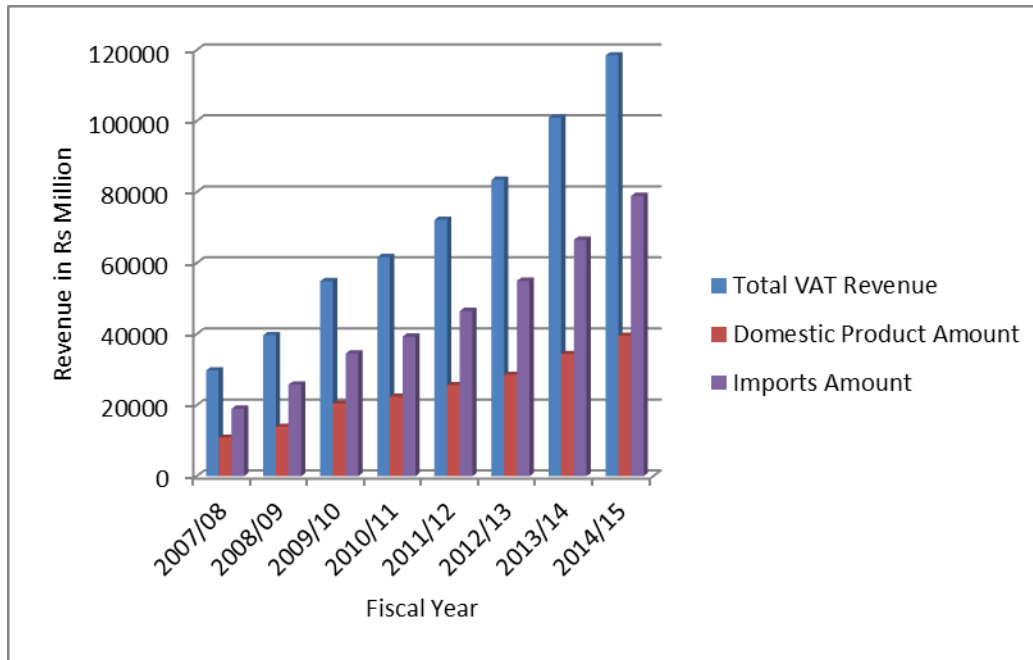
Source: IRD Annual Report (2014/15)

The share of VAT collection from domestic products has been around 33 to 37 % whereas collection from imports has been around 62-66 %. The VAT revenue has been increasing gradually in absolute term, but the increasing rate is not so much satisfactory that ranges only from 15- 20 % comparing to previous years.

There is no. of factors such as ineffective billing system, under valuation of goods and services, the negative growth rate of economy for small rate of growth of VAT revenue collection.

The above data has been shown in the following diagram:

Figure 5.3: Composition of VAT revenue



5.5 Measurement of VAT Performance in Nepal

5.5.1 Present Status of Estimated VAT Efficiency (VAT Gap)

For the purpose of estimating tax compliance habit, it is necessary to estimate potential collection which would be achieved, if there were the situations of cent percent voluntary compliance of tax laws and tax rates. Collection capability is the amount of tax collection under the existing system with optimum verification effort by tax administration. Therefore, potential collection is higher than collection capability and collection capability is higher than actual collection. The difference between potential collection and actual collection is tax evasion.

The gap between potential collection and collection capability is the policy related leakage and the gap between collection capability and actual collection is related to administrative capacity.

The diagnostic tools for the VAT performance include efficiency ratio and C-efficiency ratio (Ebrill et al. 2001, pp. 40-42). Efficiency ratio (E) is defined as the share of the VAT in GDP divided by the standard VAT rate. In general, the higher the ratio E, the better the performance of the VAT. The C-Efficiency ratio is defined as the share of the VAT in consumption divided by the standard VAT rate. This statistic based on consumption rather than GDP is a more reliable diagnostic tool than the efficiency ratio E.

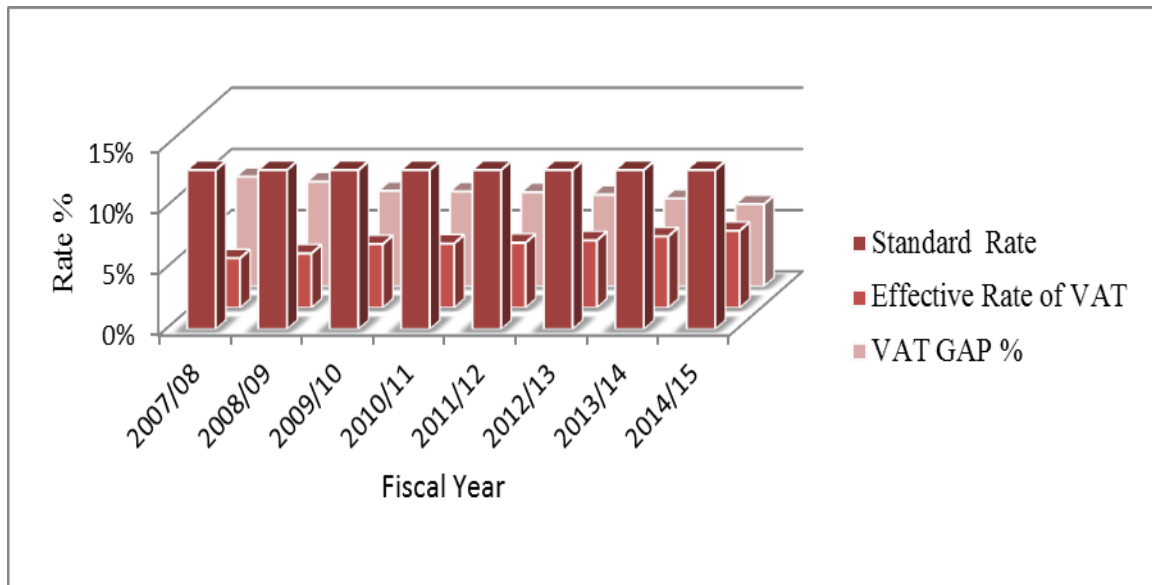
Table 5.5: Present Status of Estimated VAT Efficiency (VAT Gap)

Year	GDP (Rs. In Billion)	Consumptions (Rs. In Billion)	VAT Collection	Standard Rate	Effective Rate of VAT	VAT GAP %
2007/08	815.7	735.8	29.8	13%	4.05%	8.95%
2008/09	988.3	895.4	39.7	13%	4.43%	8.57%
2009/10	1192.8	1056.8	54.9	13%	5.20%	7.80%
2010/11	1366.9	1175.5	61.7	13%	5.25%	7.75%
2011/12	1527.3	1359.3	72.2	13%	5.31%	7.69%
2012/13	1695	1515.3	83.5	13%	5.51%	7.49%
2013/14	1941.6	1730.0	101.0	13%	5.84%	7.16%
2014/15	2124.6	1882.4	118.4	13%	6.29%	6.74%

Source: Economic Survey (2014/15) & IRD Annual Report (2014/15)

The figures in above table show the magnitude of VAT gap, generally termed as VAT leakage / gap indicating high non-compliance of VAT. The effective rate of VAT was hovering around 5-6 % when the standard rate was 13%. The same has been presented in the below diagram:

Figure 5.4: Present Status of Estimated VAT Efficiency (VAT Gap)



5.5.2 VAT Registration and Compliance

Compliance parameter such as timely registration, timely submission of returns, and accuracy of returns and magnitude of the voluntary declaration of sales income, production and value of goods, debit returns, credit returns, zero returns are used to evaluate the level of compliance. Regarding the tax compliance habit, everybody including tax payers acknowledge the need for levying and paying taxes, but at the time of payment many people do not like.

The status of registration of income tax payers and return submitted by them has been presented in table below that shows the magnitude of non-compliance in terms of filing returns has gone up-to 64.6 percent.

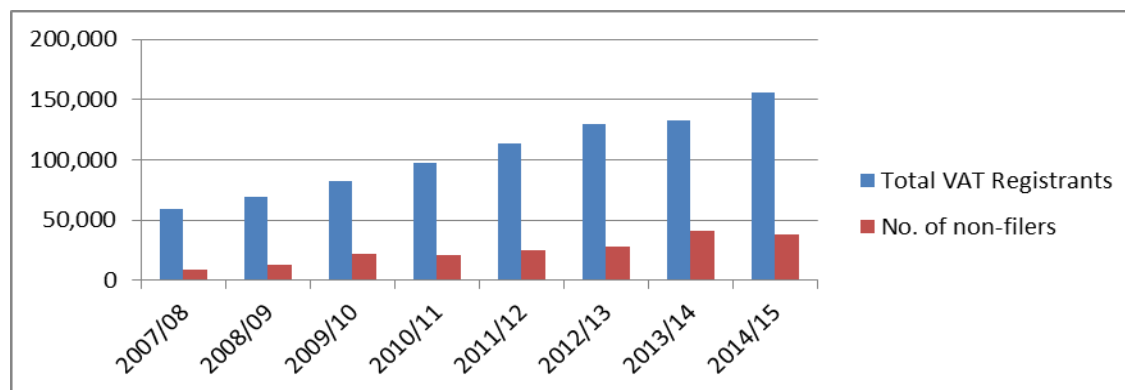
Table 5.6: VAT Registration and Compliance

Fiscal Year	Total VAT Registrants	Rate of Registrants Increase (%)	No. of non-filers	% of non-filers	% of non-filers Increase/ (decrease)
2007/08	59,741	12.5	9,050	15.15	27.92
2008/09	69,708	16.66	13,040	18.71	44.09
2009/10	82,684	18.35	22,341	27.02	71.33
2010/11	97,731	18.2	20,768	21.25	(7.04)
2011/12	113,919	16.56	25,404	22.30	22.32
2012/13	129,713	13.86	27,914	21.52	9.88
2013/14	133,178	3.38	41,259	30.98	47.81
2014/15	155,797	16.98	37,703	24.20	(8.62)

Source: IRD Annual Report (2014/15)

The above table shows that the no. of VAT registration have been increasing in each year. But, the trend in VAT compliance is decreasing. During the year 2007/08, the compliance rate of VAT was 84.85 percent and it decreased to 75.8% for the year 2014/2015. The percentage of non-filers increased from 15.15 percent to 24.20 percent during the same period. Thus, the percentage of compliance is not so much satisfactory in terms of measurements of compliance on the basis of voluntary filing of tax returns by taxpayers that has been shown in the below diagram:

Figure 5.5: VAT Registrants and Non-Filers of Return



5.6 Presentation and analysis of primary data

5.6.1 Billing System of VAT

Billing system is one of the most important aspects of the VAT system. All the Businessmen have to receive the bills of actual transaction price while importing and buying of goods services. The price of the goods and services with and without VAT has to be mentioned explicit in the bill. While selling goods, purchaser has to compulsory been given the same type of bill. The Businessmen have to pay the amount of difference between tax collected in sale and tax paid on purchase to the VAT office. He has to pay the income tax as well on the profit of his transaction. Thus, the billing system plays crucial role in the field of VAT system. But in Nepal, the billing system has been one of the major problems. So, the question is designed to show the comments on billing system of VAT. The outcome of the field survey in this aspect is given below:

Table 5.7: Adequacy of billing system in Nepal

Respondents	Yes		No		Don't know		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	12	60	8	40	0	0	20
Tax Administrators	5	100	0	0	0	0	5
Companies / Entrepreneurs	5	50	3	30	2	20	10
Consumers	4	27	3	20	8	53	15
Total	26	52	14	28	10	20	50

(Source: Field Survey, 2016)

From the above table, it was found that 60% of tax experts and auditors feel that prevailing bill system is adequate whereas 40% claimed that the billing system is still not adequate for proper implementation of VAT. All the tax administrators claimed that that current billing system is adequate. Among entrepreneurs /

companies 50% gave the view that VAT billing system is adequate and 30% gave the view that the current billing system is not adequate at the same time 20% had no idea regarding the adequacy of billing system. Among the consumers interviewed 27% had the view that current billing system is adequate, 20% argue that the billing system is not adequate where as 53% are still unknown about it.

5.6.2 Susceptibility of VAT billing system to evasion

The respondents were also asked questions about whether VAT billing system was susceptible to fraud and evasion and the views and opinion obtained are given in the table below:

Table 5.8: Susceptibility of VAT billing system to evasion

Respondents	Yes		No		Don't know		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	15	75	5	25	0	0	20
Tax Administrators	2	40	3	60	0	0	5
Companies / Entrepreneurs	5	50	3	30	2	20	10
Consumers	5	33	4	27	6	40	15
Total	27	54	15	30	8	16	50

(Source: Field Survey, 2016)

Among the tax experts/Auditors interviewed 75% gave positive opinion and 25% gave negative opinion on VAT billing system susceptible to evasion and fraud. 60 % of the tax administrators interviewed opined that the VAT billing system is not susceptible to evasion and 40% gave it is susceptible to evasion. 50% of the Companies/ entrepreneurs gave negative opinion whereas 30% gave positive opinion. Most of the consumers interviewed i.e. 33% gave the view that VAT

billing system is susceptible to VAT whereas 27% gave negative view and 40% had no idea about the issue.

5.6.3 Obtaining bills on purchase

The customers are found to have neglected taking or ever asking for the bills after they have purchased goods or services. Likewise, the salespersons also don't bother to provide them with any bills. VAT calls for the issuance of the bills. So, this habit can be taken as the critical problem for the smooth implementation of VAT system. Even if some give bills, it is not guaranteed that they are proper ones or are not fake ones. The respondents gave following answers when asked about this.

Table 5.9: Obtaining bills on purchase

Respondents	Yes on every purchase		Yes, on Above Rs 5000		No, never take any bill		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	10	50	10	50	0	0	20
Tax Administrators	3	60	2	40	0	0	5
Companies / Entrepreneurs	3	30	5	50	2	20	10
Consumers	2	13	3	20	10	67	15
Total	18	36	20	40	12	24	50

(Source: Field Survey, 2016)

In total 36% of people take bills on every of their purchases and aware about the types of VAT bills. About 20% of people have the habit of taking bills on purchases of above Rs.5,000 and 20% doesn't obtain bills or they complain that they are not given any bill when they buy goods or services .It is a liability of every salesman to produce the bill whereas demand for bills is the lawful right of every customer.

5.6.4 Additional amount paid to obtain VAT bill

VAT is levied on value added on each stage and it is finally realized from the final consumer and is deposited to the government account. The value of the goods purchased is inclusive of the VAT amount and the purchaser does not have to pay additional amount for VAT. We asked question to various people whether additional amount is paid to obtain VAT bills and the response received is in the table given below.

Table 5.10: Additional amount paid to obtain VAT bill

Respondents	Yes		No		Often		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	0	0	20	100	0	0	20
Tax Administrators	0	0	5	100	0	0	5
Companies / Entrepreneurs	0	0	8	80	2	20	10
Consumers	10	67	3	20	2	13	15
Total	10	20	36	72	4	8	50

(Source: Field Survey, 2016)

About 20% of the total respondents told that they were charged additional amount for obtaining VAT bills and all those respondents were consumers. Even 8% of the businessmen/entrepreneurs said that they had paid additional amount to obtain the VAT bill often.

5.6.5 Awareness about fake VAT bill scams

Recently issues and cases of fake VAT bills are in light and IRD have conducted various reviews and investigation about the fake VAT bill scams. During the survey we asked various respondents whether they were aware about the fake VAT bill scams and received the following responses.

Table 5.11: Awareness about fake VAT bill scams

Respondents	Yes		No		Don't know		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	20	100	0	0	0	0	20
Tax Administrators	5	100	0	0	0	0	5
Companies / Entrepreneurs	7	70	3	30	0	0	10
Consumers	2	13	10	67	3	20	15
Total	34	68	13	26	3	6	50

(Source: Field Survey, 2016)

Cent percent of the tax experts/ auditors and tax administrators were aware about the fake VAT bill scams. 70 % of the businessmen/finance managers and 13% of the consumers were aware about the issue. 87% of the consumers and 30% of the Companies / Entrepreneurs were not aware / don't know about the issue.

5.6.6 Opinion whether customers are cheated on account of VAT

During the survey the respondent were asked question about whether customers are cheated on account of VAT. Unauthentic bills with no PAN number and bill number are given by VAT registered vendors, sometimes the vendors ask for additional money if they are asked for VAT bill. The results are as follows:

Table 5.12: Opinion whether customers are cheated on account of VAT

Respondents	Yes		No		Often		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	10	50	4	20	6	30	20
Tax Administrators	2	40	3	60	0	0	5
Companies / Entrepreneurs	6	60	1	10	3	30	10
Consumers	10	67	2	13	3	20	15
Total	28	56	10	20	12	24	50

(Source: Field Survey, 2016)

About 56% of the total respondents agree that customers are cheated on account of VAT, 20% believe that they are not cheated and 24% believe that the customers are sometimes cheated. Among 67% of the total customers surveyed agreed with the fact that they are cheated on account of VAT. The main cause for such cheating according to their view was lack of proper knowledge about VAT.

5.6.7 Effective means for creating VAT awareness

VAT is newly introduced scientific tax system so everybody should be educated about it. About VAT education, few people are aware of this very term. Customers believe that VAT will increase the price of the goods and services so they don't want to be even educated about it. Businessmen are also against it as they also lack the proper knowledge about VAT. So VAT should be the topic of discussion and matter of concern for the successful implementation. The following feedback has been collected from the survey.

Table 5.13: Effective means for creating VAT awareness

Respondents	Radio/TV		Newspaper/ Booklets/ Pamphlets		Wall Painting/ Banner		Seminars / workshop		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	7	35	5	25	3	15	5	25	20
Tax Administrators	2	40	1	20	1	20	1	20	5
Companies / Entrepreneurs	6	60	1	10	1	10	2	20	10
Consumers	10	67	2	13	1	7	2	13	15
Total	25	50	9	18	6	12	10	20	50

(Source: Field Survey, 2016)

The above table shows that 50% suggest radio and TV as the effective media for creating VAT awareness. Newspaper/booklets/pamphlets might be another

source of education as suggested by 18% of total respondents. About 12% suggest that the wall painting/banners may also be one of the media for VAT education and 20 % suggest seminars could also be media for spreading VAT awareness.

5.6.8 Rate of VAT

VAT rate is very significant and sensitive for revenue mobilization the success of VAT system stands upon the degree of VAT rate. Earlier the tax rate of Sales Tax, which is replaced by VAT, was 15%. Likewise other taxes i.e. contract tax, entertainment tax, hotel tax air flight tax were not below than 15% on average. But VAT rate is now subject to 13%. Due to broader base and coverage, VAT was expected to have a greater revenue yield on present rate structure. However this expectation is not achieved in practice basically due to its weak implementation aspect. In such situation, field survey was conducted to identify the rate structure of VAT. The following table shows the views on this matter

Table 5.14: Rate of VAT

Respondents	Low Rate		High Rate		Normal		Don't Know		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	3	15	10	50	7	35	0	0	20
Tax Administrators	2	40	0	0	3	60	0	0	5
Companies / Entrepreneurs	0	0	8	80	2	20	0	0	10
Consumers	0	0	10	67	2	13	3	20	15
Total	5	10	28	56	14	28	3	6	50

(Source: Field Survey, 2016)

Survey result shows that most of the respondents i.e. 56 % agree with the existing rate of 13% i.e. high rate. However, 28% claims that existing rate is normal. Whereas, 10% consider it as low rate and 6% don't have any idea.

5.6.9 Rising Price Due to VAT System

In the beginning period of VAT implementation there was a strong opposition from the business community. The basic argument behind it was due to rise in the price from VAT. After the implementation of VAT, there was a voice from different people on price rising on commodities. Consumers also complain that businessman charge more prices without following the VAT act. Here, an endeavor has been made to get the information from the respondents to find out whether there will be raised in price due to VAT system. The following table presents the views of respondents on this aspect:

Table 5.15: Price Rise Due to VAT System

Respondents	Yes		No		Don't know		Total
	No.	%	No.	%	No.	%	
Tax Experts/Auditors	5	25	15	75	0	0	20
Tax Administrators	0	0	5	100	0	0	5
Companies / Entrepreneurs	7	70	2	20	1	10	10
Consumers	10	67	2	13	3	20	15
Total	22	44	24	48	4	8	50

(Source: Field Survey, 2016)

In the survey, 44 % respondents reached at the conclusion that there is a rise in price due to VAT system. 48 % claimed for no rise in price and 8 % has no idea at all. The study shows 25% Tax Experts, 70% Companies / Entrepreneurs and 67% Consumers claims that there is a raise in price because of VAT system. When they were asked for the reason of the raise in the price, respondents have different view: due to compliance cost, higher profit, non-awareness of consumer.

5.6.10 Sufficiency of Legal Provisions and Rules of VAT

Before the implementation VAT, the government has prepared VAT act and VAT regulation but the legal provision and rules, in general different to understand by all. The documents of this enactment carry all the matters such as VAT administration and its operation, the Tax Officers and its authorities (duty and responsibility), taxpayers and its responsibility, the procedure of VAT collection, identification of new tax payers, monitoring, cross checking, penalties and punishment. The field survey has been conducted to find out whether the present act and regulation are sufficient or not reference to current VAT system. The outcome / attitude of the respondents on this aspect are present in the table below:

Table 5.16: Sufficiency of Legal Provisions and Rules of VAT

Respondents	Yes		No		Normal		Don't know		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	5	25	5	25	10	50	0	0	20
Tax Administrators	3	60	1	20	1	20	0	0	5
Companies / Entrepreneurs	3	30	4	40	3	30	0	0	10
Consumers	5	33	2	13	3	20	5	33	15
Total	16	32	12	24	17	34	5	10	50

(Source: Field Survey, 2016)

From the above table ,out of the total respondents 32% claimed for its sufficiency or rules and legal provision of VAT, 24% were opposite of this view, 34% had normal view and remaining 10% were unknown about this question. It can be said that the present rules and legal provision are enough to implement VAT system effectively and properly.

5.6.11 Major Weakness of VAT Administration

VAT system has been implemented instead of ineffectiveness of provisions Sales Tax system because the revenue creation of it was not so much significant to the economy with respect to VAT. For the effective and successful implementation of VAT, we have to identify the current weakness of administration. It is reported that there have been various weaknesses behind the non-functioning of VAT system in an expected way VAT administrative reform is weak, inadequate and incomplete which cause problem and challenges in the path of operation of VAT administration. It is found that major weakness of VAT administration in Nepal are lack of expertise, lack of trained man power, weak financial resources, lack of physical resources, lack of physical infrastructure and miscellaneous. The field survey was conducted in this aspect to know the major weakness in VAT administration. The outcome on this view is shown in the following table:

Table 5.17: Weaknesses in VAT administration

Respondents	Lack of expertise		Lack of trained Manpower		Corruption & bribing		Lack of physical infrastructure		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	8	40	5	25	5	25	2	10	20
Tax Administrators	3	60	1	20	0	0	1	20	5
Companies / Entrepreneurs	3	30	2	20	3	30	2	20	10
Consumers	5	33	3	20	4	27	3	20	15
Total	19	38	11	22	12	24	8	16	50

(Source: Field Survey, 2016)

Every study related to VAT suggests that administration is the main problem in Nepal. Unless and until administration is transparent, capable, trained and honest, the government's intention to collect revenue through VAT will be limited to nothing more than just a daydream. Above table shows that 60% of tax

administrators attribute the lack of expertise to the weakness in administration. In total, 37% of people suggest the lack of expertise in VAT administration. About 22% due to the lack of trained manpower ,24 % boldly accused the officials of corruption and bribing while the tax officials remain silent about this and 16 % due to lack of physical infrastructure. According to them, the corruption and bribery is rooted in the Nepalese administration.

5.6.12 Examination of business by tax authority

The businessmen/companies/accountant interview were also asked question about how regularly and at what time interval are physical inspection of their business conducted by the tax authority. The views given by them are summarized in the following table.

Table 5.18: Examination of business by tax authority

Respondents	Yes		No		Sometimes		Total
	No.	%	No.	%	No.	%	
Companies / Entrepreneurs	6	60	0	0	4	40	10
Total	6	60	0	0	4	40	10

(Source: Field Survey, 2015)

Above table shows that about 60% of businessmen answered that their business is inspected by the VAT authorities on regular basis and all their accounts and details as well as their stocks are checked by them. 40% said that their business and books of accounts was inspected sometimes only.

5.6.13 Maintenance of VAT Accounts/Timely submission of returns

The businessmen/companies/accountants were asked whether they keep all the books of accounts as required to be kept by the VAT act like purchase book, sales book and other records and the view expressed by them are as follows.

Table 5.19: Maintenance of VAT Accounts/ Timely submission of returns

Respondents	Yes		No		No Idea		Total
	No.	%	No.	%	No.	%	
Companies / Entrepreneurs	8	80	2	20	0	0	10
Total	8	80	2	20	0	0	10

(Source: Field Survey, 2016)

About 80% of the Companies registered under VAT said that they keep proper books of accounts and submit VAT return on timely basis, 20% said that they do not keep the records required but update on a yearly basis during the time of audit and filing tax return.

5.6.14 Challenging Problems of VAT

It is not a matter how much easy to introduce VAT system but how much effectively and properly to run it because VAT is complicated and advance than other taxes. The taxpayers as well as the tax collectors must be more conscious for the successful implementation of VAT. In the context of Nepalese economy, there are many problems associated with the implementation of VAT. It is found that the further success of VAT basically depends on its effective implementation aspect. The field survey has been conducted to identify the most challenging problem among smuggling and under valuation, lack of proper billings, lack of proper accounting and weak tax administration. The outcomes of different respondents on this aspect are following as presented below:

Table 5.20: Challenging Problems of VAT

Respondents	Under Invoicing		Lack of proper billing		Lack of proper accounts		Weak tax Administration		All		Total
	No.	%	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	10	50	5	25	3	15	2	10	0	0	20
Tax Administrators	2	40	1	20	1	20	1	20	0	0	5
Companies / Entrepreneurs	2	20	2	20	2	20	2	20	2	20	10
Consumers	3	20	2	13	4	27	1	7	5	33	15
Total	17	34	10	20	10	20	6	12	7	14	50

(Source: Field Survey, 2016)

From the field survey, it was found that 50% Tax Experts/ Auditors, 40% Tax Administrators, 20% Companies and 20% Consumers engage that under invoicing is the most challenging problem associated with VAT. Thus out of the total respondents, 34% viewed under valuation and 20% percentage believe lack of proper billing and proper accounts is main challenging problem, 12% identify that weak tax administration is current existing problem; whereas 14% argued that all the factors were responsible.

5.6.15 Problems in the implementation of VAT

Respondents were asked what problem there might be in successful implementation of VAT. Their response is presented in the following table.

Table 5.21: Problems in Implementation of VAT

Respondents	Adm. Incapability		Under Invoicing		Frequent change in Acts		Lack of Public Awareness		Lack of Long term Policy & strategy		Total
	No.	%	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	1	5	3	15	1	15	5	25	10	50	20
Tax Administrators	1	20	2	40	1	20	1	20	-	-	5
Companies / Entrepreneurs	3	30	2	20	2	20	1	10	2	20	10
Consumers	5	33	3	20	2	13	2	13	3	20	15
Total	10	20	10	20	6	12	9	18	15	30	50

(Source: Field Survey, 2016)

Above table reveals that about 30 % consider lack of long term policy and strategy as the main reason for effective VAT implementation. Due to the lack of public awareness, customers hardly demand any bills on their purchase. Total 20% consider administrative incapability as a hindrance to VAT implementation.

5.6.16 Is there VAT evasion in Nepal?

Total 50 survey participants were enquired about whether they are aware about tax evasion in the context of Nepal and what they think about whether or not there is VAT evasion in Nepal.

The response of the participants is tabulated below:

Table 5.22: Is there VAT evasion in Nepal?

Respondents	YES		Often		No		Don't Know		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	10	50	10	50	0	0	0	0	20
Tax Administrators	5	100	0	0	0	0	0	0	5
Companies / Entrepreneurs	3	30	4	40	3	30	0	0	10
Consumers	5	33	2	13	3	20	5	34	15
Total	23	46	16	32	6	12	5	10	50

(Source: Field Survey, 2016)

According to above field survey, out of total respondents, most of the respondent viewed that there is VAT evasion in Nepal, 50% of tax experts / auditors viewed that there is vat evasion and 50 % viewed often vat evasion in Nepal. 100 % tax administrators viewed that there is VAT evasion in Nepal whereas 32% of total respondents viewed that there is often VAT evasion in Nepal but they are not sure about it and 12 % of total respondents viewed that there is no VAT evasion in Nepal. Out of total only 10 % viewed that they have no idea about it.

5.6.17 Means of VAT evasion

VAT is vulnerable to evasion in the context of Nepal. Therefore, sample group were asked about what do you think the medium for VAT evasion that are frequently used in Nepal.

The opinion of the survey group is tabulated in the below table:

Table 5.23: Means of VAT Evasion

Respondents	Under billing / Fake Invoices		Hiding transaction / Mis-classification		Bribing tax administrators		Claiming VAT credit for fake transaction		No idea		Total
	No.	%	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	10	50	5	25	3	15	2	10	0	0	20
Tax Administrators	2	40	2	40	0	0	1	10	0	0	5
Companies / Entrepreneurs	3	30	3	30	2	20	2	20	0	0	10
Consumers	6	40	2	13	3	20	2	13	2	1/3	15
Total	21	42	12	24	8	16	7	14	2	4	50

(Source: Field Survey, 2016)

According to above field survey, out of total respondents 42% viewed for VAT evasion purpose traders under bill the transaction / produce fake invoice, that shows actual VAT payable to government is much higher than that is being paid, out of total respondent 14% viewed that companies VAT credit claim higher than actual is also one of the technique used for VAT evasion, further 16% of total respondent viewed that bribing tax administrators for concealing facts is also widely used for VAT evasion. Only 4% of total respondents have no idea about means of VAT evasion, all of them fall in the consumers' category.

5.6.18 Successful implementation of VAT / Remedy for VAT Evasion

It is necessary to identify the existing problems and solve them successively to make the VAT more successful in future. So that it still help to increase revenue pattern properly. Hence, there are so many options to make VAT more successful. These are strengthening and improve the VAT administration,

improve VAT laws and regulation, trained and educated offices, public awareness. Programs about VAT etc. the opinion survey on this context of different respondents is summarized in the table below:

Table 5.24: Successful Implementation of VAT

Respondents	Improved VAT administration / Scientific Reporting System		Trained educated officers		Improved VAT laws and regulation / Auditing		Conduct public awareness programs		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Auditors	5	25	5	25	5	25	5	25	20
Tax Administrators	1	20	1	20	2	40	1	20	5
Companies / Entrepreneurs	4	40	2	20	2	20	2	20	10
Consumers	6	40	3	20	4	27	2	13	15
Total	16	32	11	22	13	26	10	20	50

(Source: Field Survey, 2016)

According to above field survey out of total respondents 32% viewed that to make VAT effectively successful, there will be need of improvement in VAT administration with the introduction of scientific reporting system. Similarly 22% supported on the need of trained and educated officers. Likewise 26% expressed their view to improve VAT laws and regulations where as 20% opinioned to regulate public awareness programs on this view.

CHAPTER -VI

SUMMARY OF MAJOR FINDINGS, CONCLUSIONS & RECOMMENDATIONS

6.1 Summary of Major Findings of the Study

On the basis of preceding chapter data presentation and analysis, important findings of the research has been presented in summary as follows:

6.1.1 Findings from secondary data analysis

1. The VAT system introduced in Nepal has already been implemented more than 2 decades. Due to various complexities and problems, it has not been able to achieve the expected level of implementation.
2. The contribution of tax revenue used to be almost 80 % and non-tax revenue almost 20 %. The contribution of tax revenue was expected to increase after the implementation of VAT and its contribution to GDP was 16.75 % at the end of FY 2014/15. The share of sales tax/VAT in GDP was 1.90 percent in FY1991/92 and now increased to 5.58 % at the end of FY 2014/15.
3. The VAT revenue has been increasing gradually in absolute term, but the increasing rate is not so much satisfactory that ranges only from 15- 20 % comparing to previous years. There is no. of factors such as ineffective billing system, under valuation of goods and services, the negative growth rate of economy for small rate of growth of VAT revenue collection.
4. The effective rate of VAT was hovering around 5 % when the standard rate was 13%, hence, it was estimated that more than 7 % VAT gap exists in

Nepalese economy. There is wide range of practice of evading tax.

5. Though the no. of VAT registration has been increasing in each year, the trend in VAT compliance is decreasing. During the year 2007/08, the compliance rate of VAT was 84.85 % and it decreased to 75.8% for the year 2014/2015. The percentage of non-filers increased from 15.15 % to 24.20 % during the same period. Thus, the percentage of compliance is not so much satisfactory in terms of measurements of compliance on the basis of voluntary filing of tax returns by taxpayers.

6.1.2 Findings from primary data analysis

1. VAT evasion is emerging as problem for tax administrators in Nepal, most of the respondents strongly viewed that, there is VAT evasion in Nepal.
2. Under billing of the transaction is a widely used tool for VAT evasion, along with taking credit for fake transaction, bribing VAT administrators for concealing actual facts and hiding total transactions from tax purview.
3. Only people who are involved in the profession of tax and VAT are aware about the billing system of VAT. Most of the consumers did not know about the VAT billing system and how it works. They thought it was an additional amount which made goods costlier.
4. Among the people interviewed, they were of the view that VAT system could not be made applicable to all parts of the country due to various difficulties like geographical barrier, lack of education and consciousness, lack of infrastructure etc. More revenue can be generated through VAT by widening its coverage. The small traders which fall in the threshold limit has not been able to brought under VAT net. They should be registered. The revenue can increase by discouraging tax evasion.

5. Most of the consumers do not have the habit of taking bills. Now since the fake VAT bills are in light they are aware about the different business sectors involved in fraud of VAT bills, but only few of them know about the actual VAT bills. This implies that there is very low public awareness and consciousness level towards VAT.
6. There is even practice among the traders to charge additional amount if the consumer ask for VAT bill. This indicates the very need of supervision and rational auditing. About 67 % of the consumers interviewed had paid additional amount for obtaining VAT bills. On the other hand, businessmen do not want to issue bills. The businessmen have the intension of 'malpractice' on VAT. So they don't provide bills to customers or provide ordinary non VAT bills.
7. It was observed that there was little knowledge about VAT to taxpayers and low public consciousness level in Nepal. To educate taxpayers and all the concerned bodies, educational program has to be launched in an effective way. But whatever program has been underway is not sufficient to create its impact on people. Most of the respondents suggest that Radio/TV might be best media to educate taxpayers and consumers. Newspaper / seminars might be another good alternative.
8. It has been noticed that traditional Nepalese businessmen do not have the habit of maintaining their account The expected amount of VAT collection is not possible due to lack of maintenance of proper accounts which is very serious problems. Billing is also a very serious problem regarding VAT collection and has remained a major bottleneck. The potential revenue is severely lacking due to non-operation of billing system in most of the registered firm. Most of the businessman / companies holding VAT certificate issue VAT Bills just for formalities and issue illegal bills for every

transaction. Besides that, most of the business firms do not issue bills; however, they issue parallel bills and other loose bills. On the other hand, they make parallel account one for the tax purpose and other for business purpose.

9. Customers do not have the habit of keeping bills on their every purchase and business does not feel liable to provide bills on their every sale to customers. Even though bills are provided to the customers it is difficult to know about its genuineness. Currently the issue of fake VAT bill scam show how big business houses are evading tax and committing fraud in the name of VAT bills. The inspection conducted by tax authorities should be tightened and should be regular. When asked with Companies during the survey it showed that only 60 % of the businesses were regularly inspected by the tax authorities and in the remaining inspection was either not regular or not conducted at all.
10. Though VAT has been implemented in Nepal in order to generate more revenue, but the efficiency of the Nepalese VAT administration is not satisfactory and not up to the expectation of the general people.
11. Lack of trained manpower and expertise affects the fluency of VAT administration. Physical infrastructure is also lacking. Unless and until administration is made transparent, capable and trained, the government's intention to collect comparatively more revenue through VAT will remain a daydream. There is also lack of proper long term strategy and policy in order to effective collection of VAT.
12. Administrative incapability, under invoicing/not billing and lack of public awareness towards VAT are main problem in the process of VAT implementation in Nepal.
13. For making VAT effectively successful in future, it is necessary to overcome

the current challenging problems like smuggling, under valuation, lack of proper billings, lack of proper accounts and weak tax administration.

14. The VAT rules and acts are not amended as per the requirement and there are still loopholes through which VAT evasion is committed.
15. Successful operation of VAT is extremely challenging for a mushrooming economy like Nepal where, there is long open border, a large segment of the economy is yet to be magnetized, business system is still running in traditional way, geographical structure is rugged, non-adherence of standard norms and codes is wide spread, public consciousness level is very low, existing practice of smuggling and under valuation in the custom is supporting for the under invoicing in the successive stage of production and distribution. Further all the rules and regulation are not seen in real practice, bribing and corruption is wide spread in the tax administration and all other sectors of the economy. These are the facts that exist in Nepalese environment which encourages Businessmen for the tax evading practices and make them less responsible in this system.

6.2 Conclusion

Taxation provides the governments with the funds needed to invest in development, relieve poverty and deliver public services. It offers an antidote to aid dependence in developing countries and provides fiscal reliance and sustainability that is needed to promote growth. Taxation has played an important role in the economic development of each country. VAT is a form of indirect taxation which is levied on the value added goods and services. Like all taxes, VAT is subject to evasion and offers distinctive opportunities for evasion, especially through abuse of the credit and refund mechanism. Revenue may be lost through exaggerated claims for credit for VAT paid on inputs to production.

Moreover, the opportunity exists for outright fraud through the construction of business activities with the sole purpose of defrauding the exchequer, because some categories of business can be entitled to net refunds of VAT from the revenue authorities. Much of this VAT gap reflects revenue lost through relatively mundane forms of evasion – under-declaration of sales, exaggeration of input VAT, non-registration and the like

There is no doubt that the VAT is susceptible to evasion and fraud, running all the way from the occasional concealed sale to sophisticated and large scale attacks by organized crime. Nor is there any doubt that although many of frauds to which VAT is vulnerable arise under, for a retail sales tax, the structure of the tax- notably the payment of refunds, particularly on exports does create distinctive control problems. All taxes face problems of noncompliance, some of these take particularly striking form. The study shows that the effective rate of VAT was hovering around 5 % when the standard rate was 13%, hence, it was estimated that more than 7 % VAT gap exists in Nepalese economy. There is wide range of practice of evading tax.

Though the no. of VAT registration has been increasing in each year, the trend in VAT compliance is decreasing. During the year 2007/08, the compliance rate of VAT was 84.85 % and it decreased to 75.8% for the year 2014/2015. The percentage of non-filers increased from 15.15 % to 24.20 % during the same period. Thus, the percentage of compliance is not so much satisfactory in terms of measurements of compliance on the basis of voluntary filing of tax returns by taxpayers

VAT was introduced as broad based tax system, it has helped to enhance the revenue generation of the government. But it is not free from evasion. The study has helped to put light on the factors that are responsible for VAT evasion.

However, there are several issues in the applicability of VAT in Nepal and which has made way for VAT evasion.

Customers / consumers are unaware about the VAT system and its implication and how it works and even if they know they know only little facts. Still there is general belief among the customers that imposition of VAT has increased the prices of the products and if they do not take VAT bills then they will be charged less. The traders and businessmen are taking advantages of unawareness of consumers and businessmen are earning from this by evading taxes. Customers though they are paying VAT in their purchases due to lack of proper supervision from the tax authorities it is not going to the revenue of government rather it is used by the businessmen themselves for their benefits.

The issues regarding fake VAT bill scams are the examples of VAT evasion. Recently government has tightened the VAT collection system and imposing fines and penalties for those who are evading taxes. If the government make the VAT administration effective and tighten and even punish for the frauds committed and evasion then there will be more revenue generation unlike past years. Apart from tightening the VAT collection system the VAT act, rules and regulation must be updated on regular basis according to the need and application in the practical environment. Effective implementation of VAT in Nepal can be obtained by enhancing administrative capability, introducing more trained manpower and infrastructural development. Media may play a vital role in educating people and spreading awareness about VAT system and its applicability.

Weak tax administrations is the key reason for VAT evasion in the context of Nepal, Tax administrators continue to be staffed by poorly trained and low paid

officials and existing structures which do not encourage an innovative ideas for reducing tax evasion are the reason behind VAT evasion.

Truly, increment of VAT rate has fairly negative influence on general people. Their viewpoint is to broaden the tax base instead of increasing the tax rate. Tax rate has been increased time and again for nothing, but this does not get reflected in real revenue mobilizations. Rates should be continued for a long time for transparency and must be incorporated in VAT act itself. So, the government has to pay serious in increasing the tax base instead of increasing the tax rates. International experience tells us that the gradual lowering of duties or tax rate is an effective tool in achieving desired goals rather than increasing it.

VAT Act and its provisions should be amended on a regular basis to avoid confusion and effective implementation. Loopholes in the VAT provisions must be amended and it should be made practically applicable as well. The registration process should be made easier by extending helping hands to the taxpayers with all the resources and knowledge required about the VAT system. The government should encourage the small traders as well through various schemes so that they come under the tax net. The government should focus not only in the cities, the country sides and villages should also be focused and proper knowledge should be provided to the taxpayers and businessmen there. Regular supervision of the business houses from the tax authorities and department is necessary to avoid evasion that may arise. Further, public awareness campaign should be run throughout the nation regarding prevailing VAT practices and subsequent penal provision for its non-compliance.

In summary, this study found that tax knowledge is an important element to avoid tax evasion in the country Greater tax knowledge is believed to have a positive impact on compliance of tax and to reduce the VAT GAP / Evasion. It

can be attributed to careful planning and the employment of a simple system of record keeping, tax rates and tax administration leading to high compliance levels for adopting model of VAT.

6.3 Recommendations

Against all provisions and existence of many weaknesses for effective tax compliance and proper control of leakages the tax system is surrounded by so many legal, institutional, administrative and policy constraints. For effective policy formulation, knowledge of taxable capacity and tax potential capacity is necessary. Strong political will is essential for the successful enforcement and implementation of tax laws. The control of leakage depends on the effective measure of tax compliance.

On the basis of research, the following corrective measures are recommended for the better administration and implementation of VAT system and tax compliance and leakage control.

1. Nepalese policies are deep rooted by the politicians and leaders of the country who are highly motivated by own benefits that result in formulation of defective policies. Thus, to justify the government should set goals of overall fiscal policy. The policy of taxation should be based on redistribution of income and wealth.
2. The threshold of VAT should be revisited as taxation policy to expand the tax base.
3. The preventive measures should be given priority over repressive action when tackling frauds. This should be the principle of legislation and enforcement. Fraud can be curbed by making tax laws less complex and

leaving less scope for it. The fraud control policy should focus on two issues (a) First; try to make optimal use of information technology. (b) Secondly, the policy should focus on effective tax payer inspection making inspection pyramid to promote tax compliance.

4. The VAT legislations are not simple and understandable as mentioned in preceding chapters. The VAT laws should be amended to make simple and predictable. The complexity in legal system is an incentive to tax avoidance. The complex business transaction is more difficult to legislate too. The complex taxes are more difficult to administer properly. Hence, it is needed to remove the complexities of laws. Unpractical / confusing rules and regulations related with VAT must be amended on the basis of experience gained and practical cases far VAT laws to be effectively implemented.
5. The value added tax (VAT) has greater revenue potential than most other instruments, but realizing this in many cases requires expanding the base by eliminating exemptions, unifying rates, and improving compliance rather than increasing standard rates.
6. Institutional development is integral part of tax policy. The tax institutions should be developed in modern management principles. The institutional reformer should keep in mind that the tax collection cost to be minimized. The functions of top management and field level organization should be specified. The investigation and control agencies need to coordinate their activities by establishing institutional mechanism for exchange of information between different agencies.
7. Taxpayers should be encouraged to be registered and should be provided with proper knowledge of VAT. They should be provided with various facilities so that they will be encouraged for VAT compliance. The tax administration can select genuine business persons and reward them. Regular

training program should also be conducted by the IRD to teach taxpayers about the accounting system and accounting records to be kept so that there will be more and more transparency.

8. The work flow inside the institution need to be properly channeled to increase the institutional efficiency. To create good working environment, the recruitment, transfer and departmental action and firing policy in revenue services should be rationalized.
9. The information technology can help the tax administration to achieve its goal and improve efficiencies through the promotion of tax compliances. The process of automation in tax administration can contribute to service delivery and generate cost saving benefit. The revenue leakage control can be carried out smoothly through the use of automated data along with the development of scientific reporting system.
10. The monitoring system is the focal point of enforcement of the laws and rules. The monitoring system should be designed tax payer-wise, tax-wise and office-wise to ensure tax compliance and control revenue leakage. The periodical monitoring reports are necessary to evaluate the performance of each office and the employees. In order to monitor the property of employee and tax payers, establish economic intelligence in collaboration with central public relation department and increase the no. of auditing to each transaction.
11. The major function of tax administrations is collection of tax. The tax administrator should be the expert implementation not the designer of policy matters. The tax administration systems should be designed to ensure:
 - Continuous monitoring of potential VAT collection with actual VAT collection and tracing out the reasons for short collection
 - Develop information system horizontally and vertically

- Develop and use the working Manuals with International Standard
- Create social environment to develop ethical code and include professional and business ethic in the school curriculum
- Trained, knowledgeable and qualified manpower must be mobilized so that tax administration can be properly handled. Adequate training regarding efficient working and knowledge of system must be given to existing manpower of Tax department
- The tax administration should be very watchful to prevent any kind of malpractice, and tax evasion. Utmost care should be taken to prevent any kind of bribing and corruption. Tax officials should effectively be monitored.

12. The taxpayers are not satisfied with the behavior and slowness of the work of the tax administrators. Therefore it is suggested that tax administrators should be consumer-focused and result oriented. A bold vision, evolutionary leadership, efficient bureaucrats, honest taxpayers plus collectors and graft-free society are the invisible infrastructures required. So all must think from a long-term perspective rather than weighing up immediate pros and cons. The Inland Revenue Department must come up with a forward-moving process, concrete action plan and policies to cope with the global challenges in order to accelerate reduction of VAT evasion.
13. The VAT evasion is known as the inevitable market reaction. It should be controlled by joint efforts of different agencies. It demands the cooperation of politicians, business communities and citizens as a whole.
14. Program should be launched to gain trust of tax payer by educating them raised tax is for the mutual benefit of both nation and citizen development. Social awareness should be started to make the communities aware of negative impacts of VAT evasion and effective use of collected taxes.

15. Taxpayers, customers are ignorant about the VAT system and proper billing system under it. They have lack of proper knowledge about computation of tax liability, taking invoice or bill on their purchases. More emphasis must be given in educating the tax payers and issuance of proper bill for every taxable sale must be made mandatory. Awareness towards VAT system should be created among general public, nongovernmental and government organization. Tax related information should be published regularly through journals, magazines, newspapers, pamphlets, radios, television and cinema, interview programs with professors' researcher, tax expert's economists. It should be conducted and published through media. Similarly, the students at school as well as campus level should be given the knowledge about VAT. The school as well as campus level curriculum should include tax education and social obligation of paying tax. The role of general media, radio, TV, newspaper plays an important one. Emphasis should be given on mass media.
16. While devising a proper and feasible model of VAT for Nepal it should be kept in mind that one of the major lessons of the Canadian experience is simply that there is no need to have single VAT system for whole country. Respecting the regional differences different provinces can be allowed to adopt different variants of VAT. Canada has allowed five different systems to operate in its ten provinces. This probably answers the often raised question as to whether by amending the constitution a Central VAT (the centre levying the VAT and sharing it with states) or a Subnational VAT (VAT being completely in state hands) shall be followed. Thus it is important not to try to formulate a universal and precise conceptual design leading to elimination of the likelihood of evolution of a tax policy that will be able to put up with the regional differences thereby allowing different systems to coexist within same nation. The better part is that it is functioning

well in a federal country like Canada. This however does not mean that the system will necessarily work in Nepal too. In fact differences in political culture, may lead to certain difficulties in permissibility of such solutions in Nepal. This significant issue, therefore, calls for further study and investigation in Nepal context.

Hence, in the words quoted by Wallschutzsky (1989) has suggested that the key elements in such a strategy must be summarized as follows: Keep the tax laws as simple as possible; aim for a global tax with few exemptions, rebates, or deductions; Do not try to use the tax system to achieve too many social and economic goals; Continually monitor the tax system; Concentrate on basic tasks such as collection of taxes at source and ID number system; Do not collect more information than can be processed; actively encourage good record keeping; and, aim, as a long term goal, for self-assessment.

QUESTIONNAIRE FOR THESIS

A. Personal Background

1. Name of Respondent:

2. Name of the organization:

3. Position currently held (*Choose one of the following answers*)

- | | | | |
|-------------------------------|--------------------------|------------------------|--------------------------|
| 1. Company Director | <input type="checkbox"/> | 2. Executive Officer | <input type="checkbox"/> |
| 3. Government/Public Official | <input type="checkbox"/> | 4. Accountant | <input type="checkbox"/> |
| 5. Investor | <input type="checkbox"/> | 6. Owner / Businessman | <input type="checkbox"/> |
| 7. Regulator / Supervisor | <input type="checkbox"/> | 8. Others | <input type="checkbox"/> |

4. Main area where currently involved / economically active (*Choose one of the following answers*)

- | | | | |
|---------------------------------------|--------------------------|------------------|--------------------------|
| 1. Commerce and Industry | <input type="checkbox"/> | 2. Self-Employed | <input type="checkbox"/> |
| 3. Public Administration / Government | <input type="checkbox"/> | 4. Others | <input type="checkbox"/> |

B. For each question, please choose.

1. Have you ever used E filing to file your VAT returns?

Yes No N/A

2. Is VAT return submitted within the 25th day of the following month?

Yes No N/A

3. Have your / your company return examined by the tax offices regularly?

Yes No Others N/A

4. Overall, how satisfied were you with the service you received from Tax Office?

Satisfied Dissatisfied Neither/nor Others if any specify

5. Is the current billing system adequate?

Yes No Don't Know

6. Is the current billing system exposed to fraud and evasion?

Yes No Don't Know

7. Do you take VAT invoice on every purchase?
 Yes No Above NPR 5000 Don't Know
8. Are you aware about the types of VAT bill (TAX invoice and abbreviated tax invoice)?
 Yes No Don't Know
9. Are Purchase Book, Sales Book, VAT Account maintained as prescribed by regulatory?
 Yes No N/A
10. Does the vendor ask for additional amount of money if VAT bill is asked apart from original priced value? Have you come across any such instance? Have you paid the additional amount?
 Yes No Often
11. Are you aware about the VAT bill related scams?
 Yes No Don't know
12. Do you think customers are cheated on levying VAT?
 Yes No Often
13. Effective means for creating awareness related to VAT in your opinion?
 1. Radio/TV 2. Newspaper
 3. Pamphlets/Booklets 4. Wall painting/Banner
 5. Seminars/workshop 6. Others
14. What do you think about the current VAT rate?
 Low High Normal Don't Know
15. Do you think there rise in price due to VAT system?
 Yes No Don't Know
16. Is the prevailing act and regulation sufficient to regulate VAT system of Nepal?
 Yes No Normal Don't Know
17. What are the major problems faced by business sector in relation to VAT?
 1. Registration Process 2. Tax refund process

- | | | | |
|-----------------|--------------------------|---------------|--------------------------|
| 3. Book Keeping | <input type="checkbox"/> | 4. Billing | <input type="checkbox"/> |
| 5. Others | <input type="checkbox"/> | 6. Don't know | <input type="checkbox"/> |

18. What do you think is the major weakness in VAT Administration?

- | | | | |
|------------------------------------|--------------------------|-------------------------|--------------------------|
| 1. Lack of trained manpower | <input type="checkbox"/> | 2. Lack of expertise | <input type="checkbox"/> |
| 3. Lack of Physical Infrastructure | <input type="checkbox"/> | 4. Corruption & bribing | <input type="checkbox"/> |
| 5. Others | <input type="checkbox"/> | 6. Don't know | <input type="checkbox"/> |

19. What do you think are the current challenging problems of VAT?

- | | | | |
|----------------------------|--------------------------|---------------------------|--------------------------|
| 1. Under invoicing | <input type="checkbox"/> | 2. Lack of proper billing | <input type="checkbox"/> |
| 3. Lack of proper accounts | <input type="checkbox"/> | 4. Weak Administration | <input type="checkbox"/> |
| 5. All | <input type="checkbox"/> | 6. Don't know | <input type="checkbox"/> |

20. What are the problems faced in the implementation of VAT?

- | | | | |
|------------------------------|--------------------------|----------------------|--------------------------|
| 1. Admin Incapability | <input type="checkbox"/> | 2. Under Invoicing | <input type="checkbox"/> |
| 3. Frequent changes in Acts | <input type="checkbox"/> | 4. Lack of awareness | <input type="checkbox"/> |
| 5. Lack of policy & strategy | <input type="checkbox"/> | 6. All | <input type="checkbox"/> |

21. Is there VAT evasion in Nepal?

- Yes No Often Don't Know

22. What means are used for VAT evasion?

- | | | | |
|-------------------------------------|--------------------------|------------------------|--------------------------|
| 1. Under Billing | <input type="checkbox"/> | 2. Hiding transactions | <input type="checkbox"/> |
| 3. Bribing Tax offices | <input type="checkbox"/> | 4. Fake Invoices | <input type="checkbox"/> |
| 5. Paying low tax | <input type="checkbox"/> | 6. Not paying at all | <input type="checkbox"/> |
| 7. Cash transactions with no trails | <input type="checkbox"/> | 8. Mis-classification | <input type="checkbox"/> |
| 9. Others | <input type="checkbox"/> | 10. Don't know | <input type="checkbox"/> |

23. What can strengthen effective VAT implementation / discourage vat evasion in Nepal?

- | | | | |
|--------------------------------|--------------------------|--------------------------------|--------------------------|
| 1. Improved VAT administration | <input type="checkbox"/> | 2. Trained Tax Officers | <input type="checkbox"/> |
| 3. Improved VAT laws | <input type="checkbox"/> | 4. Awareness program | <input type="checkbox"/> |
| 5. Auditing | <input type="checkbox"/> | 6. Scientific Reporting system | <input type="checkbox"/> |
| 7. Avoid cash transactions | <input type="checkbox"/> | 8. Don't know | <input type="checkbox"/> |

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