CHAPTER-- 1
INTRODUCTION

1.1 Background of the Study

Nepal is least developed land locked country which has adopted the system of mixed economy for achieving developing goals. The overwhelming majority of people on the frontline of poverty live in rural area. Wide spread rural poverty and the failure to spread the benefits of development more widely is critical for Nepal's development.

In order to improve the quality of people's lives, Nepal has given number one priority to development through planned efforts. Nepal has been pursing planned development for nearly five decades, but the countries poverty ratio still remains one of the highest in the world. Poverty reduction is identifies as major objectives and need for Mobilization of additional resources has been growing (Agrawal, 1978:29).

Economic development has been one of the most popular slogans in almost all the developing countries all over the world. Similarly, achievement of high rate of economic growth, reduction of income disparities and poverty and improvement of living standard of people are some of the development strategies towards which most of the government efforts have been directed in developing countries.

It is known that government needs more revenue for overall economic development and state welfare. Besides this, for meeting day-to-day expenditure, government also requires some sources of income, which is called revenue. The source of government revenue is two types .ie.1) Internals 2) External. These are the challenging tasks, which demand increasing necessity of regular expenditure in general and development expenditure in particular. However, resource mobilization is very low compelling the government to depend on foreign assistance heavily. Development expenditure has been relied on entirely on foreign aid. We know, external assistance is uncertain, inconvenient and not good for healthy development .Foreign aids are not bad for economic development of the nation peruses. But the experience of the most of the developing countries shows that there are negative effects of increasing international grants and loans to finance the public development activities. Thus, the government should depend on its own resources (internal source) for generating revenue to spend these regular as well as development activities.

Government collects revenue from taxable and not taxable sources.(Internal source) Tax is a key source for revenue mobilization. Tax is compulsory contribution, as prescribed by law, to the government for a common benefit upon the residents of the state. Taxes are major fiscal policy instruments and important government policy tools, have an important role in increasing the rate of capital formation and thereby a high rate of economic growth can be achieved. Increase in taxes may be directed to increase in saving through the postponement of consumption. The increase in saving means a higher volume of resource is available for making useful and productive investments. Taxation may also play a dual role. On the one hand, taxation may be used to make the maximum volume of resource available to the public sector. On the other hand, taxation may be used to promote useful investment in the private sector and to prevent the resource from being dissipated over speculative and unproductive investment as well as over lavish and luxurious consumption. Thus, taxes in developing countries are the severe means of raising revenue.

While considering the ration of tax revenue to national production, that tax collection has been insignificant in comparison with tax potential. While little attention is being paid to revenue collection, equal weakness in tax related law, rules, procedures and administration have caused huge leakages in revenue. Taxpayers have not been able to pay taxes due to legal and procedural difficulties. Such problems are made prevalent particularly in the case of direct taxation. Due to this, our dependency on indirect tax has been very high. Nepal government is committed to mobilize revenue in accordance with taxpaying capacity of the people by changing revenue structure and administrative procedure. For this, the government review laws, rules and administrative procedures related to tax.

Due to the limitation of direct tax and its low performance in revenue collection indirect tax has been given preference by Nepal government. So to enhance for revenue mobilization VAT was introduced in Nepal. Income tax and custom administration made more transparent and supportive, attracting all entrepreneurs and the business communities to come under the network of VAT. Since, the VAT is one of the components of indirect taxes developed in past is probably the best tax system that had never been at the top of tax system.

VAT is a sales tax in advance forms. It is imposed on different stages. It is the tax imposed on added value of good and services. Encyclopedia of taxation and tax policy say, "VAT is a broad based tax on business designed to measure net value generated in a country." Indian tax institute define VAT as “a tax imposed on the seller of goods and services based on value added by their respective units." Value Added Tax is also known as goods and services tax or added value tax. It is tax system that aims to minimize tax evasion and increase resource mobilization (Kandel, 2006).

Economic development has been major issue for the countries all over the world. The proof of the Government existence lies in its activity for social and economic upliftment of the nation along with life standard of the peoples. In order to realize goals, the government lunches several economic social, cultural and other development activities. The successful lunching of these activities depends on the sufficiency of various types of resources like man, machines, materials, money etc. The most crucial resources is financial resource. This can be derived internally and externally. Internal resources consist of tax revenue and no tax revenue whereas external resource consist of foreign subsidy, foreign loan etc.

Generally, there are two types of tax, Direct tax and Indirect tax. Direct tax is really paid by a person to whom it is legally imposed while an indirect tax is imposed on one person but partly or wholly paid by another. Income tax, property tax, gift tax, interest tax, expenditure tax etc. are direct tax whereas entertainment tax, sales tax, hotels excise duty, custom duty etc are indirect tax.

Indirect tax is commodity tax. It tends to be shifted an indirect tax which is partly or fully passed on by forward and backward shifting process. Most of the developing and least developed countries including Nepal have been basically depending upon indirect tax for internal revenue generation because of administration inefficiency lack of tax culture and awareness of tax payers very low per capital income etc.

In least developed countries like Nepal, role of indirect tax is seen to be more important. And VAT is the most important innovation of the second half of the twentieth century, which is considered as an effective means to collect revenue as a reformed sales tax of indirect tax system.

The value added tax is of recent origin in the field of taxation. the concept of VAT was developed by 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. Charls S. Shop, the tax however remain 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.

The concept of VAT in Nepal was introduced in early 1990s.Nepal government indicated its intention to introduce VAT in the eighth plan subsequently the finance minister declared to introduced a two -tier sales tax system to make the base of implementing VAT from the fiscal year 1992/93.A VAT task force was created in 1993 under the financial assistance of USAID in order to make necessary preparation for the introduction of VAT. The VAT task force prepared the draft of VAT legislation. Comments on this draft were invited from, inter alia, industry and trade sectors. The VAT task force organized discussion programs on VAT for the representatives of the industry and trade sectors in different parts of the kingdom. It's also prepared a VAT introductory brochure which was distributed widely to the potential taxpayers, tax administrator and other.

The parliament of Nepal enacted “value added tax act 1995(2052)”, subsequently VAT regulation was made in 1996; although the act was passed in 1995 its implementation was delayed due to political instability and strong opposition from business community. VAT with single rate of 10% has been fully implemented with effect from 16 November 1997.It has replaced sales tax, hotel tax, contract tax and entertainment tax. VAT is a new tax system for Nepal, VAT has been justified in the light of government fiscal imbalance and need for extra revenue mobilization through an efficient tax system. The government of Nepal has been increased VAT to 13% with its effect from 15 February 2004 (Magh,1 ,2061).the value added tax its name implies a tax in the value added to a commodity or service. Its special characteristics being that it falls on the value added at each stage of production and distribution.

VAT is indirect tax: This tax is used in product and services for every channel like producer, wholesaler, retailer, and customer. In practical and principle VAT is regressive tax and its final weight bear by a customer. The main objectives of VAT is to mobilized the resources (Dhungana, 2003).

So, our study is concern on: how should the VAT collection and what are the legal provisions regarding to the VAT collection system.

In case of legal provision in Nepal while collecting VAT, the tax payer should pay after 25 day of each month, Otherwise 10 percent delayed charge is added to the VAT due. But, if the taxpayer submits to reasonable reason to the administration this charge will not be charged. There are other lots of provision like registration of small firms, transaction lower the threshold, selling of ownership, agriculture etc. To make VAT transaction and practical it has categorized non VAT items such as agriculture, food etc.

1.2 Role of VAT Collection and Legal Provision

As stated above collection of VAT is affected by the VAT collection system whereas the legal provision concerning to the VAT collection system has crucial part. Through VAT, internal revenue is increased which is very important for the development of nation.

It plays a vital role for the economic development of nation, Resources mobilization is compulsory for the economic development as well as smooth operation of any country. Nepal has adopted planned development since 1956, from that time need for mobilizing additional financial resources has been growing. Financial resources can be mobilized internally as well as externally. External resource includes foreign loan and grants. Internal financial resources can be obtained from tax measure and non-tax measure. Tax measure includes direct tax and indirect tax. Direct tax which is paid by taxpayer directly, whereas indirect tax measure include government charges, fees, fines, forfeitures, receipt from sale of commodities, fix assets and services, dividend, royalty etc.

1.3 Statement of the Problem

Nepal is very poorest country situated between china and India. Like other developing country of the world Nepal is also rapid population growth, increasing unemployment, resources constraints and high dependency on an agricultural, low living standard and poor infrastructure. In order to solve the above problem, it needs huge amount of resources and such resources can be obtained internally as well as externally sources. In Nepal resources mobilization is still poor and is not able to cover the growing expenditure. In order to match expenditure and income foreign loan is increasing, aids are not sound a way of resources collection and such collection will affect economy badly. In loan we should pay interest which huge amount of money.

In fact foreign source should not give priority and should focus on domestic source in order to run economy smoothly. In fact value added tax should be developed as good sources of internal resources.

Due to internal conflict not established government, in this time Nepal is suffering from huge resource gap. Most of developing expenditure has cut and security expenditure has increased, tourism one of the most important areas of economy is declining and due to this reason big part of resources is decreasing. The condition is trades, investment and industries are becoming terrible. Nepal is second richest country in water resources in the world but due to lack of resources only 41% of Nepalese has access of electricity and condition of irrigation is also terrible. These all indicate that Nepal needs huge amount of resource and such resources internally we should focus on various tax. Infrastructure and value added should be developed as an affective source of resources. From early time Nepal is suffering from resource gap and such gap was caused of poor tax system. Now, Nepal has been adopted VAT system was 9 years ago. But it has been not implementation so smooth. There was highly debate and discussion while implementing VAT but now such discussion are not taking place but in order to make VAT effective the concerned body should be listen the suggestion of various concerned sector and should implement such effective and reliable suggestion. This study has tried to answer the following research question:

1. What is the structure of tax in Nepal?
2. What is the revenue collection from VAT?
3. What is the VAT collection problem in Nepal?

1.4 Objectives of the Study

The basis objective of this research study is to examine the practice of value added tax in Nepal. However, the objectives of this study are pointed out as follows:

1) To review the structure of tax in Nepal.
2) To analyze revenue collection from VAT.
3) To examine VAT collection problem in Nepal.
4) To provide appropriate suggestions on the basic of findings of the study.

1.5 Significance of the Study

About nine years have been passed since VAT came into operation, but many Nepalese people are unknown about various aspects of it .VAT being itself a complicated and modern tax system, more efforts should be made on actual circumstances. Theoretical and practical knowledge are required to collect VAT properly and provide detailed information to tax payers. So, this study analysis VAT collection system and legal provision concerning to it in Nepal. Because of this reason the study will directly beneficial to policy maker, private sector, researchers and other general people. It will also provide an idea and knowledge to these persons who are interested but confused about VAT collection system and legal provision. Now days there are so many consumers who do not want to pay VAT and the businessman want to avoid VAT, but the administrators are not responding totally to these problems. This study helps to improve such type of problems and similarly. It will be valuable reference to the further researchers. So, the study has a great significance.

1.6 Limitations of study:

The study has been conducted to the partial fulfillment of MBS degree and time, money and experience of the researcher which may affect the study. Each and every study has its own limitations and boundaries. This study also has various limitations. Some of which are given below:

a. Primary and secondary data have been collected, analyzed and interpreted so that result depends on the reliability of the secondary data.
b. This study confine to Nepalese laws, acts, rules and regulations to VAT.

c. Only those factors which are contributing the government revenue from VAT have been considered.

d. This study has focused the period from 2002/2003 to 2010/2012.

e. Due to time and resource limit data and information which researcher collected are might not be sufficient for the study.

1.7 Organization of the Study

The whole research is divided into five chapters which are as follows:

Chapter - I: This is the introduction chapter. This chapter includes background of the study, statement of problem, objective of the study, limitation of the study, significance of the study, and organization of the study.

Chapter - II: The second chapter review of literature is done to know what research had been done in the related topic in previous days and what is to be done at present or in future. This chapter has been divided into two main aspects conceptual review and review of related materials i.e. review of books , review of thesis and review of research paper and articles etc.

Chapter - III: This is the research methodology chapter. This chapter includes research design, source of data, data gathering procedure, data processing procedure and statistical procedure etc.

Chapter - IV: In this chapter data are presented, analyzed includes government expenditure, revenue and deficit, structure of tax revenue in Nepal, revenue collection form VAT, contribution of VAT in government revenue, VAT registration and empirical findings.

Chapter - V: The final or last chapter contains the summary of the whole study. The conclusions of the study have been presented and at last suitable points are suggested in the form of recommendation. Bibliography and appendixes and other supporting documents have also been incorporated at the end of the study.

CHAPTER - II

REVIEW OF LITERATURE

2.1 Conceptual Review

Tax becomes the main source of revenue of the state. Value Added Tax is the latest innovation in the field of taxation. VAT is considered as the reform tax system of the 21st century, which has already been implemented popularly in more than 135 countries in the world. VAT is multi staged, commodity and services based tax which is levied on the value added of business at different stages of production and distribution. It is imposed on different stages. It imposed on value of goods and services. The value added tax is indirect tax depends upon consumer.

VAT is a broad based tax as it also covers the value added to each commodity by a firm during all stages of production and distribution. It is a modern tax system which enables to efficient collection system, to increase efficiency and to reduce tax evasion. It is also refereed as the backbone of income tax system in Nepal.

VAT plays great role in the revenue mobilization in Nepal. The reason behind VAT system, it makes transparency in all kinds of transaction, helps to make the wide area of tax and discourages tax evasion. So it is needless to say that 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 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 (Source: http://www.ird.gov.np./information).

In practice the VAT is collected from producers and distributors at many points and treated as multiple stage commodity tax. It is different from turnover tax.

According to Indian Taxation Inquire Committee, VAT is a broad based tax on the business designed to measure net value generated in a country. It is a tax system that aims to minimize tax evasion and increase resource mobilization (Subedi, 1998:86).

Value added for a firm is nothing but its gross receipts from sales minus all expenditures on goods and services purchase from other firms. The firm adds value to these purchased materials by processing them with the help of its own factors of production such as labor, land, capital etc. This increase in the value of outputs is the value added by a firm (Khadka, 1997:1-2).

Value added is the value that a producer adds to his raw materials or purchases before selling the new or improved product or service. A tax based on this base is called VAT. Theoretically, value added can be defined in terms of earning of factors of production i.e. land labor, capital and entrepreneur. Each factor receives rent wage, interest and profit respectively (Silwal, 2001).

VAT is indirect tax: This tax is used in product and services for every channel like producer, wholesaler, retailer, and customer. In practical and principle VAT is regressive tax and its final weight bear by a customer. The main objectives of VAT are to mobilize the resources (Dhungana, 2003).

2.2 History & Development of VAT

Tax is collected by government to meet the need of budget. Among the various types of tax, the sales tax is one of the major sources. VAT is the most scientific system of sales tax. In the early days, the tax from the consumption and production is collected as sales tax. But now, it is almost completely replaced by the VAT. The concept of VAT was introduced in 1919 by Dr. Wilhem Von Sieman in Germany. This concept was brought to replace the "Usnatzsterller" (multi stage sales tax) due to its undesirable effects, particularly cascading and vertical integration of the latter tax (MST) for the first time. The Germany knew the administrative complication of the VAT system. So, it has the fear to implement. Therefore, the rate of unsatzsteuer is reduced instead of the implementation of VAT. In 1921, the America was implementing the corporate income tax. Pro. Thomas S Admass suggested the tax for the United State of America to replace the existing tax system. Until early 50s the development of VAT remained limited only in the theory.

France was the first implementer of VAT in 1954 covering only in the industrial sector. The VAT was limited to only up to whole level. But these countries limited the VAT only on import and manufacturing stage.

In late 60s, VAT started to become popular. Countries like Denmark and Brazil adopted this system of tax in 1967. France, the first implementer of VAT, extended it to the retail level for the first time. And Germany also adopted VAT in the same year. In 1969, the countries like Netherlands and Sweden also adopted VAT in their countries. In 1970, 1971 and 1973, Luxembourg, Belgium and Ireland introduced the VAT respectively.

In Asia, Vietnam was the first country to introduce this most scientific tax system. The country adopted VAT in 1973. The trend being VAT popular was increasing all over the world. In 1977, 1984, 1985, 1986, South Korea, China, Indonesia and Taiwan introduced VAT respectively. Similarly, VAT was introduced by Philippine in 1988, Japan in 1989, Thailand in 1992 and Singapore in 1994.

In SAARC region, Pakistan was the first adaptor of VAT. It implemented VAT in 1990.

India introduced VAT first as modified value added tax (MOD VAT) in1996. But actually in India, VAT replaced sales tax on 4 January 2005. Though some state didn't opt for VAT (for political reasons), majority of the state embraced VAT, states like Andhra Pradesh & Maharastra taking the leads. The Empowered Committee, constituted by Government of India, provided the basic framework for uniform VAT laws in the states but due to the federal nature of Indian constitution, States do have a liberty to set their own valuations for the VAT levied in their own territory.

In Nepal, Value Added Tax Act was enacted by 1995 and started to implement only at 16 Nov. 1997. Value Added Tax Act repelled four differences Tax Act such as Sales Tax Act, Hotel Tax Act, Contract Tax Act and Entertainment Tax Act

(Source: http://www.ird.gov.np./information).

2.3 Types of VAT

Where there is discussion about value added tax, we normally bear in mind the broad based consumption type VAT. However the value added tax can be basically classified into three categories namely consumption types VAT, income type VAT and production type VAT. The difference among the types of VAT depends upon the treatment of capital goods purchased from other firms and the treatment of depreciation for the purpose of tax base (value added). That is why discussion is concentrated within the treatment of these two items for all types of VAT (Ghimire, 2009).

2.3.1 Consumption Type VAT

If all capital goods (investments) brought from other firms are excluded from the tax base (value added) in the year of purchase but the depreciation is included in the tax base, it is known as consumption type VAT. It can be expressed in the following equation:

Value-added = wages + Interest + Rents + Depreciation + Profit - capital
Goods purchased from outside (in the year of purchase)

The above equation clearly shows that the tax base is consumption because investments are free from taxation. Under this type of VAT investment are encouraged because it excluded from tax base. Similarly, imports are taxed whereas exports are relieved from tax. Thus, tax base for the nation under this type is equal to the domestic consumption the country. Nepal has adopted it with tax credit mechanics from very beginning (Ghimire, 2009).

2.3.2 Income Type VAT

Under the income type VAT, capital goods purchased from the outside suppliers are included in the tax base in the years of purchase but depreciation is excluded from the tax base. The following equation may be presented to make clear ideas about the tax base under it

Value added = wages + interests + profits + capital goods purchased from
Outside (in the years of purchase)

Or,

Value added (Tax base) = Sales – purchase (Excluding purchase of
capital goods from outside in the year of purchase) – Depreciation.

The above equation clearly shows that the value added is equal to the consumption plus net investment. It means the tax base for the nation is the net National income that comprises the consumption and net investment of all firms with in the country (Ghimire, 2009).

2.3.3 Production Type VAT

The production type VAT includes capital goods purchase form the other firm in the tax base in the year of purchase and also includes depreciation in the tax base. It can be expressed in the following equation.

Value added = wages + interests + Rent + Depreciations + Profits + capital
Goods purchased from outside (in the year of purchase).

Or,

Value added (tax base) = sales - purchases (excluding purchase of capital
Goods from outside in the years of purchase)

The above mentioned equation obviously shows that the tax is imposed both on consumption and gross investment. This means that value added by all forms with in the country constitute the Gross National Product (GNP). That is why; the tax base of this type of VAT is conceptually equal to the GNP. Thus, this type of VAT is also termed as Gross national product type VAT (Ghimire, 2009).

2.4 Methods of Computation of VAT

VAT can be computed by following three methods,

2.4.1 Addition Method

In this method, the tax base is calculated by adding the payments made by the firm to the factors of production employed in turning out the production such as wages, interest, rent, royalties and profits. This method is very close to income type of VAT that includes the rewards to all the factor of production in its base. Because all the payments made for the factors of production have to be added, it creates complexities in calculating them in practice. Virtually no country has based the additive method, however, Argentina and Israel have used it in selected economic activities, such as banking and finances, where value of imputes and outputs are difficult to measure (Ghimire, 2009).

2.4.2 Subtraction Method

Under this method, cost of production is deducted from the sales. In other words, value added is determined as net turnover that is obtained by subtracting the cost of materials from sales proceeds. It is much closed to consumption type VAT. Theoretically, it looks simple and early but it is very difficulty to compute especially where multiple rates of VAT exist. Problems like ascertaining tax value in an accounting period may also arise.

Above two methods are called direct methods because value added is computed directly either by adding the payments made by the firms to the factors of production or by subtracting the cost of production from sales (Ghimire, 2009).

2.4.3 Tax credit Method

Tax credit method is known as indirect subtraction method or invoice method. Under this method Input tax is credited from output tax and passed into next stage up to consumption level. Tax credit method is similar, to some extent, to subtraction method but the major difference among two are:

- In the earlier methods, the tax base is levied in the 'difference amount' of tax on sales and tax on purchase, where as in the latter method; the tax is levied on the 'difference amount' of sales value and purchase value.
- Earlier method requires invoices, while latter does not require.

If the tax rates are same throughout the production and distribution method, all three methods, give the same result. Among the three methods of computation of VAT, the tax credit method is widely used in the world. This is because this method has several advantages over the other two methods, which are:

- The tax liability in this method is attached to the transaction that makes it technically and legally for superior to others methods.
- The tax calculation of value added, which is a difficulty tasks, is not necessary.
- The tax credit method creators a good audit trial making the crosschecking possible.
- It provides an effective way to completely free any product such as exports form tax and makes boarder tax adjustment easier and possible.
- Due its 'catch up effect', undervaluation and evasion at some stages are not possible.

- There will be no revenue loss but to exemptions granted to small firms or products.
- Rate differentiation at different stages for administrative or other reason becomes possible under this system without reducing the total tax paid. If tax rate is reduced at earlier stages; this similarly gives rise to unequally increased tax of later stages.

Thus, the tax credit method is desirable for several remains and has to be adopted by many countries of the world. Nepal has also adopted this method to calculate VAT payable calculation of VAT revenue can be expressed as follow for the above -mentioned different types,

Addition method (T) = t (wages + Rent + profits)

Substation method (T) = t (sales value - purchased value)

Tax credit method (T) = t (tax on Sale) - t (tax on purchased)

Where,

T = VAT percentage rate

The example can be easily understandable by the following imaginary figures:

Table 2.1

Computation of VAT Liabilities under Three Different Methods

(VAT rate.13%)

Detail	**Stages of production; and distribution**			
A. Addition method	**Manufacture**	**Wholesaler**	**Retailer**	**Total**
a. Wages	2400	400	200	3000
b. Rent	800	600	400	1800
c. Interest	200	100	100	400
d. Profit	600	200	100	900
e. Value added (a+b+c+d)	4000	1300	800	6100
f. VAT liability (13% of e)	520	169	104	793
B. Subtraction method				
a. Sales	10000	11300	12100	33400
b. Purchase	6000	10000	11300	27300
c. Value added (a-b)	4000	1300	800	6100
d. VAT liability(13% of e)	520	169	104	793
C. Tax credit method				
a. Sales	10000	11300	12100	33400
b. Tax on sales	1300	1469	1573	4342
c. Purchase	6000	10000	11300	27300
d. Tax on purchase	780	1300	1469	3549
e. net VAT liability(b-d)	520	169	104	793

Source: Arbitrary estimated figures (Ghimire, 2009).

2.5 Principles of VAT

While considering the international trade, the principles of VAT have great significance. Whenever international trade between two countries is considered, cross boarder adjustment is necessary. For the purpose of imposing VAT, principle of Vat can be divided into origin and destination principle. Choice between those two principles largely depends on the goods and the policy of nation, accession of international trade, computing methods and types of VAT (Ghimire, 2009).

2.5.1 Origin Principle

Under this principle, goods and services are taxed at the place where they are produced or rendered irrespectively, whether they are consumed or not. It implies that all exports are taxable and all imports are non-taxable. Where there is border and cross country trade, this principle gives performance to imported goods and services over domestic production. Countries with international boundaries don't prefer to have this principle while taxiing. But these sorts of principle may be beneficial where common trade is existed like European Union. Otherwise rests of the countries do not prefer this principle (Ghimire, 2009).

2.5.2 Destination Principle

Under this principle goods and services are not taxed at the place where they are produced or rendered but the place where they are consumed. Alternatively all imports are taxed while all kind of exports are exempted from tax. The main benefit arising out of this is non-discrimination between import and internal production.

This is the most popular form of principle of VAT, Adopted by large number of countries. This principle supports for export and many countries are eager to be best exporter, therefore they follow this principle. The equal treatment is provided for imports and domestic production, which fulfills the criterion of tax being neutral (Ghimire, 2009).

2.6 Structure of VAT

2.6.1 Tax Base

The tax base may be defined as the set of income and transactions on which direct and indirect taxes are levied. Taxable base of includes all types of expenditure on final consumer goods where the consumption types of VAT are adopted. Tax base explains whether a VAT is levied on all goods and services or on some subject of such comprehensive base (Khanal, 2009).

2.6.2 Tax Exemption and zero-rating

Tax exemption and zero- rating are two popular methods of escaping from value added tax. But there is difference between tax exemption and zero-rating under the VAT system. The transaction of tax exempted goods and services remain outside the purview of VAT. Such transactions do not have to fulfill any formalities, even registration under VAT. Such taxpayers neither have to collect tax on these sales nor can they claim for a refund of the tax paid on purchases or imports. This means that the tax mount incurred on the inputs of tax exempted goods and services go to the consumer inclusive of the cost price.

On the other hand, if the transaction of certain goods and services are under zero-rated tax, such goods and services or transactions will be kept within the purview of VAT system. The transactions of such goods and services have to be registered under VAT and the registrants should collect VAT at the rate of zero percent on their sales and they can deduct the tax incurred on their purchases. This means the zero-rated goods and services do not bear the burden of VAT but should follow all the formalities of VAT.

Neither the output tax can be collected nor the input tax can be claimed on the tax exempted goods and services. But a zero-rated tax, which actually equals to none, is levied and the input tax can be claimed on the zero-rated goods and services. Hence, there is no burden of VAT on the zero-rated goods and services whereas the burden of VAT paid on input remains even through VAT is not levied on the sales in the tax-exempted goods and services. If some goods and services should be kept free from VAT, zero rated VAT should be applied. But, if it is difficult to apply tax on certain goods and services administratively, such goods and services should be kept under tax exemption (Khanal, 2009).

2.6.3 Threshold

VAT is levied on each level of sale from the production and import to distribution of all goods and services except exempted ones. But for small business persons engaged in the sales of goods and services bellow the specified level, it is not mandatory to register under VAT. To keep small business persons outside the tax purview, a threshold has been specified under VAT system. The whole seller, retailers, dealers or producers who sell taxable goods and services below the threshold level do not have to be registered under VAT and neither have they to collect VAT on their sales (Khanal, 2009).

2.6.3 Tax Rates

VAT may be levied on single rate or multiple rates. The choice may depend upon economic nature and social will such as consideration, administrative capacity, nature of product, direction and composition of foreign trade etc. A single rated VAT is desirable in UCDs because it makes VAT less costly, easy to comply with and administer.

Multiple rates make the tax system inefficient from the economic point of view. They give an incentive to producers to divert their resources from higher-rated to lower-rated industries to save on tax payment even when other economic considerations do not justify such reallocations of resources. Similarly, they stimulate the consumer to divert some of his purchase from higher-rated to lower-rated commodities. Thus, multiple rates create scope for tax evasion that may result in considerable revenue loss (Khanal, 2009).

2.7Operation of VAT

2.7.1Registration

All vendors carrying on taxable business are required to register for VAT. However, registration must not be made mandatory for small vendors having an annual turnover below the threshold level which can be determined on both the retrospective basic and prospective basis. Under the retrospective basis, the turnover may be calculated on the basis of the last 12 months' figure while under the prospective basis, the taxpayer has to prove that turnover will be below the threshold for next 12 months.

Small vendors having annual turnover below the threshold may apply for voluntary registration and the VAT officer, if satisfied, may register them for VAT purposes. Like other registered vendors, small vendors, who are registered voluntarily, will be able to claim back input tax paid on their purchases, to hold the collected tax until the data of its payment to the concerned tax offices. The registered vendor must remain registered for a minimum period of two year (Khanal, 2009).

2.7.2Tax Invoice

The tax invoice is a crucial document for VAT as it establishes the seller's liability for tax and the purchaser's entitlement to credit. It should be able to provide necessary information required by the VAT Act and regulation. It is, however, not necessary to specify the format and content of the tax invoice; taxpayers may be allowed to prepare the format of the tax invoice according to their requirements (Khanal, 2009).

2.7.3 VAT Account

It should be made mandatory for a VAT registered vendor to keep clear accounts of his purchase and sales, which are subject to positive rate, zero rate and exemption. Accounts along with all supporting documents should be preserved for four years. In general, accounts must be maintained on the accrual basis because taxpayers might delay payment. Small vendors, public or local bodies and non-profit organization may be allowed to account for their output tax and input tax only upon receipt or payment. This is intended to ease the cash flow problems of small vendors (Khanal, 2009).

2.7.4Taxable Value

VAT should be levied on the gross sales price (excluding VAT) for the supply of goods and the rendering of services. The gross sales price should be considered as the amount of money that the buyer has to pay to the seller under normal conditions. In the case of imported goods, the taxable value should include prices of goods plus all cost unto the point of importation such as commissions, parking, transport, insurance and other costs and all taxes, duties and charges levied except VAT (Khanal, 2009).

2.7.5 Tax Credit

Tax credit is one of the important features of VAT. Taxpayers are allowed to deduct tax under it. This is known as the tax credit or tax invoice method, which is better than other methods of tax computation viz. the addition method and subtraction method.

Net tax liability of a vendor under the tax credit method is obtained by deducting his input tax from his output tax. This calculation is made for a transaction basis. Input tax of the reporting period is deducted from the output tax of the same period (Khanal, 2009).

2.7.6 Tax Refund

Excess of input tax over output tax in any tax period can be adjusted in the following tax period by carrying forward to the next period or can be claimed for refund to the tax office. In the case of exporters, refund should be made within one month from the date of submission of the return. In other cases, if the input tax is more than output tax, the balance should be carried forwarded up to six months period. The excess credits for a continuous period of six months should be refunded to the concerned vendor within a month from the date of submission of the return. It must be remembered that an efficient system of refunds is an integral part of VAT. Many tax administration, however are not well known for providing quick refunds. Refund should be made promptly. Interest should be paid on refunds that are not made within a month of the receipt of a return, provided that the return is completed satisfactorily (Khanal, 2009).

2.8 Value Added Tax Law in Nepal

Nepalese ancient tax system was based on Vedas, Smritis and Purans. Directives propounded by Yagyabalka, Chanakya were main sources of taxation system.

In Nepal, Value Added Tax Act was enacted by 1995 and started to implement only at 16 Nov. 1997. Value Added Tax Act repelled four different Tax Act such as Sales Tax Act, Hotel Tax Act, Contract Tax Act and Entertainment Tax Act.

VAT replaces the old Sales Tax, Contract Tax, Hotel Tax and Entertainment Tax. It is believe that successful implementation of VAT will helps to generate customs duties and income tax also and it is expected to enhance the revenue collection and it is closely associated with the GDP. This Act classifies good and services under three category they are Vat able goods and services, exempted goods and services and zero rated goods and services. It is applied at a single rate (presently 13%, initially 10%) based on addition of value of the goods and services at each stage in the process of supply and delivery of goods and services.

Since then second amendment have already been made on Value Added Tax Act, 1995, and 8th amendment have been made in the Value Added Tax Rules, 1997. Various directives have been issued by the concerned authority to implement the VAT in Nepal.

2.8.1 Introduction of Value Added Tax

VAT applies to supplies of goods and services for consideration other than exempt goods by taxable person. VAT shall be charge on any supply of goods or services. VAT is a tax on trading transaction. The real VAT payer is the consumer not the producer.

The VAT is a broad based tax as it covers the value added to each commodity by a form during all stage of production and distribution. It is a modern tax system to improve the collection of taxes, to increase efficiency and to reduce tax evasion. It is also regarded as the backbone of income tax system.

VAT is levied in the final price of the Supply.

VAT is a indirect tax. However it is not new form of taxation. It is improve and modified form of traditional sales tax.

VAT is levied on value added at each stage of production and distribution activities. The stage may be import, export, manufacturing, wholesaling, and retailing (Source: http://www.ird.gov.np./information).

2.9 Basic Features of Nepalese VAT System

The type of VAT adopted by Nepal in conventional similar to that implemented over 135 countries around the world, it has injected some special features in to vat system to make it uniquely Nepalese. The following are the main features of the Nepalese vat system:

The adoption of consumption type of VAT because VAT is finally borne by the consumer

- The consumption of VAT through tax credit method.
- The principle of destination.
- The level of threshold is Rupees 2 million.
- The facility of tax refund.

- The application of VAT to all business turns over through the retail stages.
- The rate of Vat is single and positive @ 13%.
- The provision of exemption and zero rate for the goods and services.
- The allowance of tax credit for taxable supplies including the zero rate supply.
- Small entrepreneurs are exempted to register in VAT office.
- Self-assessment system

(Source: http://www.ird.gov.np./information).

2.10 Major Legal Aspects of VAT in Nepal

2.10.1 Registrant of VAT

VAT is subject matter of law, for this registrant is most. The criteria for the registration in any business are based on annual taxable turnover or transaction of more than 2 million rupees.

Small venders those who do have less than 2 millions annual turnover may also registered their business voluntarily (Source: http://www.ird.gov.np./information).

2.10.2 Cancellation of the Registration

A VAT registration may be cancelled if one's total taxable sales for four consecutive calendar a quarter is not more than 2 million rupees and who has been registered for a full fiscal year or by persons who no longer has a commercial activity because of bankruptcy, receivership, or cessation of the business (Source: http://www.ird.gov.np./information).

2.10.3 The obligations of the VAT registrant are as follows:

Play the role as the government agent for the purpose of the VAT collection

- Submit VAT return and pay the collected VAT amount within the 25th day of the following month
- Provide tax invoice to their customer.
- Maintain purchase and Sales Book separately for the VAT purpose.
- Keep their VAT record for a period of 6 years
- Inform the Inland Revenue Office of changes to the business including new address, telephone number or a reorganization of a partnership within 15 days.

- Put their Certificate of Registration in the premises where customers may easily see and read it,
- Allow tax officers to enter the business to examine the business records and the stock on hand.

Most business will require only minor modifications to their record keeping. In order to complete his VAT return a taxpayer will need to ensure that his books and records provide:

- The amount of VAT paid on purchases
- The amount of VAT collected on sales
- A method of distinguishing between taxable and exempt sales
- The time the goods and services were supplied and
- Evidences that goods were exported, if any

A taxpayer must keep the records of a purchase book, a sales book and a VAT account. The purchase and sales book should include the following things.

- The invoice number
- The invoice date
- The supplier's name and PAN number in the purchase book
- The customer's name and PAN number in the sales book
- The taxable value, and
- The amount of VAT

(Source: http://www.ird.gov.np./information).

2.10.4 Administrative Review and Offences of VAT

2.10.4.1 Administrative Review

A tax collector who is not satisfied with the Tax Assessment made by Tax Officer may submit an application to the director of IRD (Inland Revenue Department) for review within 30 days from the time of receiving such decision. IRD bound to furnish their verdict within 60 days from the filing of application and IRD fails to do then collector may submit their appeal to the Revenue Tribunal

(Source: http://www.ird.gov.np./information).

2.10.4.2 Offences

Following acts are considered offence and fine and penalty will be imposed.

- No registration within 90 days from the commencement of the Act
- No publication of registration certificate within the business premises publicly.
- Not giving information regarding transfer of location or area of business to the authority within 15 days from such transfer.
- Not issuance of bill.
- VAT collection without registration.
- Not filing of tax statement as per the prescribed period.
- Any kind of cheating forgery or fraudulent transaction.

Creating obstacle to the tax officer during the inspection of business transaction

(Source: http://www.ird.gov.np./information)

2.11 Value Added Tax Rules, 2053 (1997)

In exercise of the power conferred by Section 41 of the Value Added Tax Act, 2052 (1996) His Majesty's Government has framed the following Rules (Source: http://www.ird.gov.np./information).

2.11.1 Preliminary

a). Short Title and Commencement:

(1) These Rules may be called "the Value Added Tax Rules, 2053 (1997)".

(2) It shall come into force on such date as His Majesty's Government by Publishing a notice in the Nepal Gazette may appoint.

b) Definitions: Unless the subject or context otherwise requires, in these Rules,-

(a) "Act" means the Value Added Tax, 2052 (1996).

(b) "Tax Period" means the period for which a Taxpayer is required to furnish Tax Return.

(c) "Tax Return" means a return furnished by a Taxpayer in regard to the tax Payable for transactions carried out during the Tax Period.

(Source: http://www.ird.gov.np./information)

2.11.2 Provisions Relating to Registration

a) Application for Registration:

(1) Any person engaged in any transaction at the time of the Commencement of the Act shall submit an application for registration to the concerned tax Officer, in the format as set forth in Schedule -1 within 90 days of the commencement of the Act.

(2) A person intended to engage in any transaction after the commencement of the Act shall submit an application for registration to the concerned tax officer, in the format as set forth in Schedule -1 prior to the commencement of such transaction.

(3) In case a person making application for registration pursuant to sub-rule (1) or (2) is a partner, the application must be submitted along with the details of the partnership in the format as set forth in Schedule -2.

b) Investigation into Application:

(1) The concerned tax officer may ask an applicant to produce such other additional details and the documents which are deemed necessary in making investigations into the details and documents attached with the application submitted pursuant to Rule 3. It shall be the duty of the applicant to submit such additional details and documents to the concerned tax officer within seven days of such demand.

(2) In cases where anyone has happened to submit an application for registration of the transaction which is not required to be registered as set forth in sub-section

(3) On Section 10 of the Act, the concerned tax officer shall give a notice setting out that he is not required to be registered, to the applicant within seven days of the receipt of the application.

c) To Grant Certificate of Registration:

The concerned tax officer shall, if he deems it proper to register, upon making investigations pursuant to Rule 4 into the application submitted for 2registration pursuant to Rule 3, register the transaction which the applicant has carried out or intends to carry out the transaction and grant the certificate of registration bearing Registration Number as well in the format as set forth in Schedule -3 to the applicant, within thirty days of the date on which the application was submitted.

d) Entrepreneur Carrying out Small Transactions Need not to be Registered:

(1) Notwithstanding anything mentioned in Rule 3, any person carrying out transactions not exceeding one million rupees within the last twelve months as set forth in Section 9 of the Act need not have registered his transactions. Provided that any person who imports into the Kingdom of Nepal goods valued at one hundred thousand rupees or more per annum for commercial purposes shall have to register his transactions.

(2) Notwithstanding anything contained in sub-rule (1), any person carrying out small transactions may submit an application pursuant to Rule 3 if he wishes to register his transactions voluntarily. If an application has been submitted to register the transactions voluntarily, the tax officer shall register the transactions by completing the procedures of investigation referred to in Rule 4.

e) Special Conditions on which Transactions are to be registered:

(1) In case any person has reason to presume that his transactions shall exceed one million rupees in the coming three months, he shall submit an application setting out such conditions, to the concerned tax officer in the format as set forth in Schedule -1 for the registration of the transactions.

(2) If the amount of the transactions carried out by any person exceeds one million rupees in absence of (the) conditions where presumption could not be made as set forth in sub-rule (1), the person carrying out such transactions shall submit an application to the concerned tax officer in the format set forth in Schedule -1 for registration of the transactions within thirty days of the date on which such excess occurs.

f) Determination of Amount of Transactions:

The amount of any transactions shall, for the purpose of the registration of the transactions, be determined on the basis of the value of purchase or sale of the transaction in the last twelve months, whichever is higher. Any registered person shall maintain the records setting out the amount of the transactions in the place of transactions and produce them as and when required by the tax officer.

g) To Give Notification of the Change of Place:

(1) Any registered person who has to change the place of his transactions shall inform the concerned tax officer thereof prior to fifteen days of such change.

(2) The concerned tax officer shall, upon receipt of the information referred to in sub-rule (1), if he deems that the place of transactions to be changed falls within the scope of another Tax Office, notify the concerned office thereof within seven days of the receipt of such information.

h) To Notify for the Change of Nature or Object of the Transactions:

(1) Any registered person shall prior to fifteen days of the change of the nature or object of his transactions notify the concerned tax officer thereof.

(2) Upon receipt of the notice referred to in sub-rule (1), the concerned tax officer shall change the nature or object of the transactions of the registered person and inform such registered person thereof.3

i) Transfer of Transaction:

(1) In case any registered person has fully or partially transferred the transaction being carried out by him to any person, he shall supply the information thereof by setting out all the details in the format set forth in Schedule-4 to the concerned tax officer within seven days of the date on which the transaction was so transferred.

(2) In case the transaction has been transferred pursuant to sub-rule (1), the rights, powers and obligations of the transferor shall be subject to the terms of the transferee.

(3) The concerned tax officer may, get both the parties related to a transfer in his presence to give them necessary instructions in regard to the obligations to be fulfilled by them under the Act and these Rules. It shall be their duty to follow the directions so given.

j) Cancellation of Registration Process:

In case the registration of any registered person be cancelled due to the conditions referred to in sub-section (1) of Section 11 of the Act and such a registered person or his successor in the event of his absence submits to the concerned tax officer an application, setting out the conditions for cancellation of registration, accompanied by the Tax Return referred to in Schedule -11 as well as the payable tax amount, for the cancellation of registration, within thirty days of the date on which the condition for cancellation of registration occurred, or the concerned tax officer is satisfied that the registration of a registered person in existence of the conditions set forth in sub-section (1) of Section 11 is to be cancelled, he (the tax officer) shall cancel the registration of such person, upon getting him to pay the remaining tax amount, and give notice thereof to the concerned registered person or his successor and the Department.

k) Use of Registration Number:

A registered person shall use his registration number in the following documents related to the transactions which he carries out, in addition to the transactions referred to in sub-section (6) of Section 10 of the Act:

(a) Documents relating to income tax;

(b) Documents relating to applications to be submitted to banks and financial institutions for loans exceeding one hundred thousand rupees for commercial and industrial purposes;

(c) Documents relating to import and export.

l) To Issue Duplicates:

(1) In case the certificate of registration of transaction obtained by a registered person under Rule 5 be torn, lost or otherwise destroyed, he must submit to the concerned tax officer accompanied also by one hundred rupees for the duplication fees payable to obtain such certificate, to obtain a duplicate copy of such certificate.

(2) Upon receipt of an application pursuant to sub-rule (1), the concerned tax officer must give a duplicate copy of the certificate of registration of transaction within fifteen days of receipt of the application

(Source: http://www.ird.gov.np./information).

2.11.3 Place and Time of Supply

a) Determination of the Place of Supply of Goods:

The following places shall be deemed to be the place of supply of goods:-

(a) In the case of movable goods transferred by sale, the place where such goods were sold or transferred,

(b) In the case of any immovable goods whose location can't be transferred even if their ownership is changed, the place where such goods are located, 4

(c) In the case of imported goods, the customs point in the Kingdom of Nepal through which such goods are imported into the Kingdom of Nepal,

(d) In case any producer or vendor supplies the goods to himself, the place where the producer or vendor of such goods resides.

b) Determination of the Place of Supply of Services:

The place of supply of a service shall be the place where the benefit of that service is received (Source: http://www.ird.gov.np./information).

2.11.4 Provisions Relating to Invoices and Market Value

a) Tax Invoices:

(1) In supplying any goods or service by a registered person, he shall give tax invoices to the recipient, in the format as set forth in Schedule-5.

(2) Tax invoice shall be written clearly and conspicuously on the front page of the invoice to be given to the recipient under sub-rule (1). Such tax invoices shall be prepared in three copies, and the original copy shall be given to the recipient, the second copy to be separately recorded so that it can be produced as and when asked for by the VAT Office and the third copy be recorded by the registered person for the purpose of his transaction.

b) Abbreviated Tax Invoices:

(1) Notwithstanding anything contained in Rule 17, in case any registered person is to conduct a retail sale of any goods and submits an application to the concerned tax officer setting out such matter, he may grant permission so that such registered person may while conducting retail sale of any goods give an abbreviated tax invoice in the format referred to in Schedule -6 to the recipient, instead of the tax invoice as set forth in Rule 17.

(2) Where several low priced goods have been sold, instead of separately mentioning the names of all the goods, the expression of some goods may grossly be mentioned in the abbreviated tax invoice to be given pursuant to sub-rule (1).

(3) A recipient who receives an abbreviated tax invoice under sub-rule (1) by purchasing the goods shall not be allowed to deduct tax under Section 17 of the Act.

(4) A registered person who gives an abbreviated tax invoice to the recipient pursuant to sub-rule (1), shall maintain records thereof as set forth below:

(a) To prepare and maintain a duplicate copy of the original invoice,

(b) Where a transaction has been carried out by maintaining a duplicate of the roll, the total thereof must be calculated and maintained every day,

(c) To maintain records of the value, including tax, of each transaction.

(5) In case a registered person is found not to have maintained the records required to be maintained pursuant to sub-rule(4), the tax officer may cancel the permission granted to issue an abbreviated tax invoice pursuant to sub-rule (1).

(6) Notwithstanding anything contained in these Rules, where a transaction of value exceeding five hundred rupees has been carried out, an abbreviated tax invoice shall not be allowed; and despite having carried out a transaction of value less than that amount, it shall be the duty of a registered person to provide a recipient who asks for the tax invoice referred to in Rule 17 with such a tax invoice.

(7) The total figure of tax shall be calculated from an abbreviated invoice by multiplying the invoice price by the tax variant.

<u>Explanation</u>: For the purpose of this sub-rule, the term tax variant means the quotient derived by dividing the rate of tax by the total obtained from adding 100 to the rate of tax.

$$\frac{\text{Rate of tax}}{\text{Rate of tax} + 100} = \text{Quotient}$$

c) No Need to Give Tax Invoice:

A person who carries out transactions of used goods of a value exceeding ten thousand rupees, for the purpose of sub-section (1) of Section 14 of the Act, need not issue a tax invoice in such cases where the selling price is less than the buying price of the goods supplied by him.

d) Credit or Debit Note:

(1) Where a registered person issues a credit or debit note owing to a change in the value of the goods or services supplied by him, he must clearly provide the following:

(a) Serial Number,

(b) Date of issue,

(c) Name, address and registration number of the supplier,

(d) Recipient's name, address, and registration number if he is a registered person,

(e) Number and date of the tax invoice connected with the transaction,

(f) Particulars of the goods or services and reason of credit or debit,

(g) Amount credited or debited,

h) Tax amount credited or debited.

(2) A registered taxpayer shall maintain a monthly record of credit or debit notes referred to in sub- rule (1).

e) In the Event of Payment in a Foreign Currency:

While giving the tax invoice of a Supplier upon receiving payment from the recipient in a convertible foreign currency as consideration of the supply of any goods and services, he shall give the invoice by mentioning therein the amount in Nepalese rupees equivalent to the foreign currency according to the rate of exchange prescribed by the Nepal Rastra Bank for the day of transaction.

f) Process of Market Value Determination:

(1) While determining the market value under Section 13 of the Act, the tax officer shall determine the market value by studying the transactions and value of other vendors registered in regard to the transaction of the same nature.

(2) In cases where the market value of any goods or services cannot be determined as set forth in sub-section (3) of Section 13 of the Act, the Director General shall determine the value on the basis also of the

information received in that regard by him from the registered persons of the same nature

(Source: http://www.ird.gov.np./information).

2.11.5 Records of transactions

a) Maintain Records:

(1) A registered person shall for the purpose of the Act and these Rules maintain records of the following information, documents and details:-

(a) Information as referred to in Schedule -7.

(b) Records relating to trade, accounts, cash receipts and payments.

(c) Tax invoices and abbreviated tax invoices issued by him.

(d) Tax invoices and abbreviated tax invoices received by him.

(e) All documents relating to his imports and exports,6

(f) All debit and credit notes substantiating the fluctuations in the values of goods Purchased or sold by him and other documents pertaining there to.

(g) Books of purchases and sales as referred to in Schedules 8 and 9.

(2) Notwithstanding anything contained in sub-rule(1), the Department may so prescribe that a registered person shall maintain some records, among those referred to in that sub-rule, in respect to special types of trade or business.

(3) A registered person may, with the approval of the Department, maintain the records required to be maintained under this Rule by using computers or another similar mechanical system or the method as prescribed by the Department.

(4) The tax officer may inspect the records maintained by a registered person under this Rule at any time during working hours.

Explanation: For the purpose of this Rule, "working hours" means the period between the time of opening and closing of the transactions, except on public holidays.

(5) A registered person shall make available the details and documents relating to the records demanded by the tax officer in the course of inspecting the records pursuant to sub-rule (4), by having them printed at his own expense.

(6) It shall be the duty of a registered person to provide necessary staff in order to assist the tax officer in inspecting the records pursuant to sub-rule (4).

(7) A registered person shall keep the records maintained under this Rule safe for up to six years.

b) Particulars of the Goods Distributed for Sample or Received Free of Cost:

In addition to the records mentioned in Rule 23, a registered person shall also maintain the following particulars relating to his transactions.

(a) Particulars of the goods distributed in the form of samples for the promotion of business.

(b) Particulars of the goods received free of cost.

c) Provision on Certification of Books of Sales and Purchases:

While certifying the books of sales and purchases by the tax officer pursuant to sub-section (3) of Section 16 of the Act, he shall certify as follows:

(a) In case a tax-payer submits an application to the office for certification of the books of purchases and sales,

(b) During the period of tax inspection or audit,

(c) At the time of inspection

(Source: http://www.ird.gov.np./information).

2.11.6 Tax Return and Collection

a) To Submit Tax Return of Tax Period:

(1) A registered person shall submit to the concerned tax officer the tax return of one-month tax period according to the Bikram Era, in the format referred to in Schedule -10, within 25 days of the expiry of that period.

(2) Notwithstanding anything contained in sub-rule (1), in case any registered person applies to the tax officer to have the tax period fixed for a tax period other than the tax period mentioned in sub-rule (1), having maintained the accounts by him using a computer system, the tax officer may, if he so deems proper after investigations, fix, as per necessity, a separate tax period in respect of such registered person.7

(3) The tax period of a taxpayer who has registered voluntarily pursuant to Section 9 of the Act and whose annual turnover is of value up to one million rupees may be fixed at four months.

(4) A registered person whose tax period has been so fixed to be more or less than one month shall submit his tax return of that period to the tax officer in the format referred to in Schedule-10 within 25 days of the date of expiry of that period.

(5) A taxpayer shall, when submitting the tax return for the first time, submit the tax return for the remainder of the period as if the remaining period was the full tax period.

b) To Require to Submit a Tax Return through the Heir or Legal Representative:

In case any registered person dies or becomes mentally or physically incapacitated to submit the tax return, the tax officer may, considering him to have supplied the goods or services till the day preceding his death or becoming mentally or physically unable, require his heir or legal representative to submit a tax return for that period.

C) To Submit a Tax Return Individually or Jointly:

The following persons shall submit the tax return individually or jointly in the following circumstances:

(a) In cases where any taxpayer becomes incapable to submit a tax return or he dies; his heir or guardian,

(b) In cases where any taxpayer is a legal person, any director, executive chef or any employee appointed by the management, on behalf of such a taxpayer,

(c) In case any taxpayer is a legal person and such legal person is dissolved or liquidated by the liquidator,

(d) In other circumstances other than those mentioned above, the person concerned with the taxpayer and prescribed by the tax officer

(Source: http://www.ird.gov.np./information).

2.11.7 Assessment and Recovery of Tax

a) Tax Officer May Assess Tax:

(1) In cases arising from circumstances referred to in subsection (1) of Section 20 of the Act, the tax officer may assess tax on the basis of the grounds as set forth in sub-section (2) of the said Section as well as market price or any other information and notices related to the transactions of which tax is to be determined and the issue tax assessment order in the format indicated in Schedule-12.

(2) The concerned taxpayer shall be given a time limit of seven days to submit evidence in his favors against the tax assessment order issued by the tax officer pursuant to sub-rule(1).

(3) The tax officer, if he deems any evidence submitted by the concerned taxpayer in his favors within the time limit set forth in sub-rule (2) to be appropriate, shall assess the tax pursuant to sub-rule (1) on the basis thereof and issue a tax assessment order. While so issuing the tax assessment order, the order shall also indicate the additional charges chargeable pursuant to sub-section (2) and (3) of Section 19 of the Act up to the date of issue of the order as well as the interest amount chargeable pursuant to Section 26.

<u>Explanation</u>: In calculating interest, it shall be calculated on the basis of one part of twelve parts per month.

b) To Pay Tax, Additional Fees and Interest Amount:

The concerned taxpayer shall deposit the tax, additional fees and the interest amount referred to in the tax assessment order within seven days of receipt of such an order to the concerned Tax Office.

c) Procedure of Sending Notices of Tax Assessment Order:

(1) Notwithstanding anything mentioned in the prevalent laws, while issuing a tax assessment order by the tax officer to a taxpayer pursuant to Rule 29, if the order is sent by tale fax, telex or other similar electronic devises installed at the address of such taxpayer or such order

is delivered to himself or at his office or through registered post to his address, it shall be deemed to have been duly delivered.

(2) In case the tax assessment order could not be delivered under sub-rule (1), the tax officer may inform the concerned taxpayer thereof by broadcasting or publishing a notice of such order through radio, television or in any national newspaper. In such a situation such information shall be deemed to have been received by the concerned taxpayer.

d)Assessment and Recovery of Tax Collected by an Unregistered Person:

(1) In case an unregistered person collects tax, the assessment of tax collected by him under sub-section (2) of Section 15 of the Act shall be done by following the procedures as referred to in Rule 29. (2) The tax assessed under sub-rule (1) shall be paid by the unregistered person having collected such tax within seven days of the issue of the tax assessment order.

e) Method of Tax Assessment of Used Goods:

(1) Tax Assessment of the used goods shall be done only on the saving between the selling and cost price of such goods. The vendor of such goods shall maintain a permanent record as mentioned below at the very time of the buying or selling of such goods:-

(a) Relating to Purchase:

(1) Date of Purchase,

(2) Particulars giving full information of the goods,

(3) Buying price excluding tax,

(4) Rate of tax,

(5) Amount of tax,

(6) Total amount paid.

(b) Relating to Sale:

(1) Date of sale,

(2) Selling price, excluding tax.

(3) Difference between the buying price and the selling price,

(4) Rate of tax,

(5) Amount of tax,

(6) Total amount received.

(2) The buying price referred to in sub-rule (1) means the price including tax.

(3) In case the buying price of every item of used goods exceeds ten thousand rupees, separate records of buying or selling shall be maintained.

(4) In case a registered person is found not to have satisfactorily maintained the records referred to in sub-rules (1), (2) and (3), tax shall be imposed on the total selling price of the goods sold by such taxpayer, and the tax officer may issue a written order requiring him to pay such tax along with the next tax return.9

f) To Submit a Tax Return Prior to Filing Appeal:

Prior to filing an appeal by a taxpayer against a tax assessment order made pursuant to Rule 29, he must submit his tax return of that period to the concerned tax officer.

g) Circumstances beyond Control:

(1) The following circumstances shall be deemed to be circumstances beyond control for the purpose of sub-section (4) of Section 19 of the Act:

(a) In case the person required to pay tax becomes disabled due to falling ill; up to seven days of the date of his recovery.

(b) In case the person required to pay tax is to observe obsequies; up to seven days of the end of the obsequies,

(c) In case a woman required to pay tax delivers a child; up to thirty five days of the date of delivery,

(d) In case the person required to pay tax dies or becomes insane or disappears and his heir or guardian submits an application within thirty five days of the date of such incident; up to seven days of receipt of such application,

(e) In circumstances when the person required to pay tax has not been able to come to the Tax Office because of the closure of a road due to floods, landslides or similar other reasons; up to seven days of opening of the road,

(f) In circumstances when he cannot come to the tax office due to total halt age of transport; up to the next day of the end of such halt age.

(2) In case an additional time limit shall be required to be requested due to circumstances beyond control referred to in clauses (a), (b), (c), (d) and (e) of sub-rule (1); the recommendation of the concerned Village Development Committee or Municipality shall be submitted.

(3) While requesting for an additional time-limit due to the circumstance referred to in clause (f) of sub-rule (1), the recommendation of the Village Development Committee or Municipality concerned with the place where the halt age of means of transport has taken place, shall be submitted.

h) Time -Limit for Applying for Remission of Additional Charges:

(1) For the remission of the additional charges pursuant to sub-section (4) of Section 19 of the Act, an application shall be submitted to the Director General within thirty days of the expiry of time-limit prescribed for payment of tax in the format set forth in Schedule -13.

(2) In case an application is not submitted within the time-limit referred to in sub rule (1), the waiver of additional charges shall not be grouted.

i) Tax Assessment Period:

While calculating the period referred to in sub-section (4) of Section 20 of the Act, in case a petition has been filed with any court in regard to tax, and a stay order has been issued, the period shall be calculated by deducting the period until which the petition is decided.

j) Time -Limit for Collection of Tax:

While calculating the time-limit pursuant to sub-section (2) of Section 21 of the Act, in case an appeal has been filed, the period from the date of filing such appeal to the date of decision shall not be included

(Source: http://www.ird.gov.np./information).

2.11.8 Provisions Concerning Tax Deductions and Tax Refund

a) Tax May be Deducted:

(1) A registered person may deduct the tax paid by him while importing or purchasing any taxable goods or services during the concerned month or before that month from the tax collected by him while supplying any goods or services, in the following circumstances:-

(a) In case the goods or services in respect of which a claim for deduction of tax has been made are directly related with the taxable business.

(b) In the case of internal purchases, tax invoices referred to in Rule 17 have been received.

(c) In the case of imports, there are import documents evidencing the payment of tax at the time of import.

Explanation: For the purpose of this Chapter "import documents" means import declaration forms, cash receipts, invoices of goods and such other documents relating thereto as prescribed by the Department from time to time.

(2) Tax deduction may be made only once under this Rule. When making a tax deduction, there must be invoices or the import documents up to one year before the date of making the claim.

(3) When submitting the tax return of each tax period by a registered person, he must deposit with the tax office the amount left in balance after deducting the tax paid while purchasing or importing the goods from the tax collected by him while selling the goods.

(4) In case the amount of tax paid by a registered person when purchasing or importing is higher than the amount collected by him when selling, he may deduct such excess amount in the next tax period. In a case where the amount allowed to be so deducted in the next tax period remains in balance for 6 months consecutively, he must submit an application to the tax officer in the format as set forth in Schedule 14 for a refund in a lump sum. The tax officer shall upon receipt of such application refund the remaining tax pursuant to Rule 45.

(5) In case any registered person exports amounts to more than fifty percent of his total monthly sale in any month, he must submit an application to the tax officer, enclosing therewith necessary export documents in the format as set forth in Schedule -15 for refund of the excess amount of tax to be deducted for the month. The tax officer shall upon receipt of such application refund the remaining tax pursuant to Rule 45. While making a decision to refund the remaining tax, the tax officer shall take the following matters into

Account :

(a) Whether or not he has paid tax on purchases or imports.

(b) Whether or not he has submitted a tax return required to be submitted by him earlier, and if submitted, whether or not the claim of tax refund is substantiated by such tax return.

Explanation: For the purpose of this Chapter, "export documents " means export certificates, certificates of receipt of goods, certificates of payment, letters of credit, certificates of origin and such documents pertaining thereto as prescribed by the Department, in the case of exports other than those made on a barter basis; and certificates of payment shall be substituted by import declaration forms, in the case of goods exported on a barter basis.

b) Other Provisions Regarding Tax Deductions:

(1) In case the goods of which tax has been deducted are in stock, such goods are to be shown or allowed to be counted if the tax officer desires to see or count such goods. While seeing or counting such goods by the tax officer, if he finds such goods not to have been used in taxable transactions or been kept in stock, such goods shall be deemed to have been sold at the current market value.11

(2) The concerned tax officer may order the concerned tax-payer to pay the tax payable on the goods sold pursuant to sub-rule (1). Such tax amount shall be paid together with the tax return of the month prescribed by the tax officer. Provided that if the tax officer feels that there is a situation where the tax cannot be realized if it is not realized forthwith he may require the taxpayer to pay the tax forthwith.

(3) In case any taxpayer has carried on both the transactions of taxable goods or services and tax-exempt goods or services such taxpayer may deduct only the tax paid on purchases or imports directly related to the taxable goods or services.

(4) In case a taxpayer carrying out the transactions of both taxable and tax-exempt goods or services fails to establish the direct relationship of the purchased or imported goods with the taxable goods or services, such taxpayer may deduct the amount of tax paid on his purchases or imports by calculating the proportion of taxable transaction value out of his total sale value.

(5) While calculating tax pursuant to sub-rule (4), if the tax officer feels that it cannot be calculated proportionally, he may seek direction from the Department to calculate it through another alternative method.

c) Goods or Services In Respect of Which Tax May not be Deducted:

(1) For the purpose of Section 17 of the Act, tax may not be deducted in respect of the following goods or services:

(a) Beverages,

(b) Alcohol or alcohol mixed beverages such as liquor and beers;

(c) Light petroleum (Petrol) fuel for vehicles,

(d) Entertainment expenses.

(2) Tax on the following goods may be deducted on the following proportion:

(a) On all aircraft, 40 percent of purchase value.

(b) On automobiles, 40 percent of purchase value.

(c) On computers, 60 percent of purchase value.

Explanation: For the purpose of clause (b), the term 'automobile' means any motor vehicle with three or more wheels used on a road for carriage of passengers.

(3) In case a registered person carries on a business of those goods referred to in sub-rules (1) or (2) as the principle business, it shall not bar the deduction of tax according to the procedures as set forth in these Rules.

d) Provisions Regarding Deduction of Sales Tax:

Only the sales tax paid on the following goods left in stock before the commencement of this Act shall be allowed to be deducted:

(a) On goods bought by a taxpayer for resale,

(b) On goods and services partially produced or ancillary goods for the business,

(c) On raw materials, auxiliary raw materials, and packing materials.

e) Application To be Submitted:

(1) A Taxpayer may submit an application to the tax officer in the format set forth in Schedule -16 to have a deduction of Sales Tax paid by him on his stock of goods at the time of registering himself, the portion of the Sales Tax yet to be deducted according to the previous monthly statement and tax paid on taxable transactions.

(2) While making a claim for the deduction of Sales Tax or tax pursuant to sub rule (1), the concerned taxpayer must also submit invoices of payment of Sales Tax or tax and other documentary evidence within 15 days of registration. In absence of the documentary evidence referred to

in this Rule deduction of tax shall not be made pursuant to sub-rule (1).12

(3) In case the claim made pursuant to sub-rule (1), is amended or rejected by the tax officer, or in case it is found that such tax has already been deducted, the tax officer may take action against such Taxpayer pursuant to the Act and these Rules.

(4) In case the claim made under this Rule is accepted by the tax officer, the concerned taxpayer may deduct the amount claimed pursuant to sub-rule (1), according to sub rule (4) of Rule 39.

f) Provision Relating to Tax Deductions in Respect of Used Goods:

For the purpose of subsection (5) of Section 17 of the Act, tax paid on the purchase of used goods from a person not registered and even if from a registered person, tax paid on the goods referred to in Section 17 of the Act, and those brought for personal use, shall not be allowed to be deducted.

g) Provision Regarding Refund of Tax:

(1) When refunding the amount of tax for the purpose of sub-section (3) and (4) of Section 24 or Section 25 of the Act, the tax officer shall immediately investigate the evidence submitted by the taxpayer for the refund of tax and refund the tax within 30 days of the date of registration of the claim.

(2) If it shall be necessary to reinvestigate the evidence so received, it shall be done without delay and refund given within 15 days. If the amount to be refunded exceeds Rs. 20,000/- it shall be so refunded to his bank account.

(3) While making a claim for a tax refund by a person not registered for the purpose of clauses (a), (b) and (c) of sub-section (1) of Section 25, he shall directly apply to the Department in the format referred to in Schedules -17, -18 and -19, respectively.

h) Not to be Refunded:

Amounts to be refunded under the Act and these Rules, copies of the decisions, orders, judgments, memos or other documents where copies need to be obtained shall not be refunded or provided in cases where an application was submitted three years after the expiry of the accounting period.

i) Rate of Interest:

For the purpose of sub-section (5) of Section 24 of the Act, the rate of interest to be paid by His Majesty's Government shall be equal to the rate of interest payable on government bonds maturing in a year. Such interest amount shall be calculated only after 60 days from the date of the application for refund pursuant to sub-sections (3) and (4) of Section 24 of the Act

(Source: http://www.ird.gov.np./information).

2.11.9 Provisions on Imports and Exports

a) Tax on Imports:

(1) Goods to be imported into the Kingdom of Nepal shall be subject to tax at the rate payable on goods supplied within Nepal.

(2) When fixing the value for the purpose of the determination of tax on imported goods or services, it shall be determined by following the process referred to in sub-section (5) and (6) of Section 12 of the Act.

(3) In case the value of any imported goods cannot be determined at the time of import, such goods shall be allowed to be imported into the Kingdom of Nepal only upon obtaining a deposit sufficient to meet all types of taxes or charges payable on such goods. Until the value of the goods or services imported by a registered person is determined, no tax paid on such goods or services may be deducted.

(4) In case any goods have been imported by furnishing a deposit, a claim for a tax deduction may be made only within a year from the date of determination of the value.13

b) Provisions Regarding Temporary Imports:

(1) In case of goods (to be) imported on a duty-free basis on the condition that they shall be taken back later, permission shall be granted to import such goods upon obtaining a deposit of the tax payable on them on the basis of the estimated value determined by the customs with provision to refund it at the time when they are taken back.

(2) Tax shall be imposed on the import duty itself on the goods or articles imported on a temporary basis subject to temporary import duty.50 Supervision and Management by the Director General: His Majesty's Government may by a notification published in the Nepal Gazette so designate that the supervision and management of the tax to be collected pursuant to Section 28 of the Act is to be carried out by the Director General. The Director may if he deems it necessary order the tax officer to carry out the acts and actions as mentioned below, for the purpose of monitoring matters concerning the goods or services imported:

- (a) To take a sample of the goods or articles imported and ensure that tax has been imposed sufficiently; and return the sample to the concerned taxpayer within a reasonable time,
- (b) To enter into, inspect, search at a reasonable time in places, buildings, god owns, shops etc. connected with the transactions and make enquiries of the concerned person,
- (c) To take custody of the documents connected with the purchase, sale or imports, obtain copies of them, inspect them, remove them and return documents removed within a reasonable time if he deems it reasonable upon the request of the concerned taxpayer.

c) Special Provisions on Amounts Received In Imports:

(1) For the purpose of Sections 24 and 25 of the Act, the entire tax amount collected at the customs point shall be deposited into the Value Added Tax Fund account on a daily basis, and the Customs Office shall send

statements thereof to the nearest Value Added Tax Office within three days.

(2) The balance after refunding the amounts ordered by the Department out of the amounts to be deposited into the fund referred to in sub-rule (1) shall be deposited into the prescribed Revenue Account on a daily basis.

(3) The procedures of the operation of the fund, opening of bank account, expenditures out of fund and depositing into the Revenue Account shall be as prescribed by the office of the Comptroller General

(Source: http://www.ird.gov.np./information).

2.11.10 Provision Relating to Stoppage of Property, Auction Sale, and Searches

a) Provision on Stoppage of Property:

(1) In case the taxpayer fails to pay the tax, charges and interest to be paid under the Act and these Rules within the time-limit set forth in Rule 30, the tax officer shall pursuant to Section 21 of the Act, by obtaining permission from the Director General in the form as mentioned in Schedule-20, realize the tax arrears, charges, penalties and interest.

(2) When taking into custody of or auctioning any property of a taxpayer for the purpose of sub-rule (1), the procedure shall be as follows:

(a) Furnishing notice, in writing to the concerned office to stop movable or immovable property of the taxpayer from its sale, distribution or transferrable of its entitlement until the payment of tax.

(b) In case the tax officer finds that any property belonging to the taxpayer is being kept with or under the custody of any particular person, he shall, subject to this Rule, issue an order to the concerned person to stop such custody of the property.

b) Provision on Auction Sale:

(1) In case the tax is not realized even after taking action pursuant to Rule 52, the tax officer may realize the tax by auctioning, wholly or partially the property of the taxpayer, by fulfilling the following procedures:

  (a) To identify the property to be auctioned and publicly publish notice indicating the reason for auction sale, as well as venue and date of auction sale at least 15 days before the date of auction sale.

  (b) To conduct the auction sale, with a witness of one representative of the Village Development Committee or Metropolis/ sub-metropolis/ Municipality of the place where the goods in the auction sale are located or a representative of the nearest government office and if possible the taxpayer or his representative.

(2) All the expenses incurred on the auction sale shall first of all be borne out of the amount realized from the auction sale pursuant to sub-rule (1); tax, charges, penalties and interest payable by the taxpayer shall then be realized from the balance; and the surplus, if any, shall be refunded to the taxpayer.

(3) Notwithstanding anything contained in sub-rules (1) and (2), where the taxpayer, prior to the conduct of the auction sale of his property, comes forward to pay the entire amount including all the expenses relating to the auction sale, tax, charges, penalties and interest to be paid by him, the same shall be collected and the auction sale shall be stopped.

(4) Notwithstanding anything contained in Rule 52, when the tax officer receives information before fully realizing the tax payable by the taxpayer that the taxpayer has amounts deposited in his name with a bank or financial institution, and where such amount is realized the remaining actions of the auction sale shall be stopped.

(5) In case realization is likely to be made partially, it shall be made in the order expenses relating to auction sale, interest, charges, penalties and tax.

c) To Conduct an Auction Immediately:

In case the property stopped is likely to decay, rot or wear out because of prolonged period of stoppage resulting from the filing of a petition or appeal in any court in respect of the stoppage of the property, the tax officer shall conduct the auction sale of such goods or articles immediately and credit the proceeds thereof; and in case the amount stopped is later decided to be refundable to the taxpayer according to a court decision, only the amount obtained from the auction sale shall be refunded to him. The taxpayer shall not be entitled to claim for the return of the goods or articles.

d) Search Procedures:

(1) In case it becomes necessary to conduct searches pursuant to clause (b) of sub-section (2) of Section 23 of the Act, the following procedures shall be adopted.

(a) Where there are reasonable grounds to believe that any documents or goods related to the subject in respect of which the searches are to be conducted are likely to be found in any house or in any other place, and there is a possibility that such goods or articles cannot be found if that house or place is not 15searched immediately, or it is necessary to search immediately the tax officer may himself search or cause to be searched or deputize an employee to search such house or place.

(b) By setting out the reason for the searches the person conducting a search shall notify the owner or custodian of the house or place and those who are living in such house or place that the house or place is to be searched under clause (a); and such person shall upon receipt of such notice allow the person the search to enter in such house or place.

(c) In case the person living in or owner or custodian of the house to be searched under clause (b) does not allow the person conducting the search to enter in such house or place, the person conducting the search shall give notice and reasonable time to the women living in the house or place to go away from there, and may search therein by entering by opening or breaking any window or fastener as per necessity.

(d) In conducting the search under clause (c), it shall be witnessed by at least one member of the concerned Village Development Committee, Metropolis/Sub metropolis or Municipality, or two local people or house owner or his representative or any person.

(e) In case any person is not found as witness or refuses to become a witness under clause (d) the process referred to in clause (c) shall be deemed to have been completed after taking the signature of the person conducting the search, with indicating remarks to that effect.

(f) In conducting a search under this Rule, if the body of any person is to be searched, such search may be conducted and if the person to be searched is a woman, she shall be searched by a woman.

(g) The details of the goods or items or documents obtained while conducting the search under these Rules shall be prepared and submitted to the Department within three days

(Source: http://www.ird.gov.np./information).

2.11.11 Miscellaneous

a) Provision Regarding Goods or Services to be Supplied within the Kingdom of Nepal:

While purchasing or acquiring the goods or services on which tax of value of ten thousand rupees is payable at a time within the Kingdom of Nepal by His Majesty's Government or the association, organization or office owned by His Majesty's Government or constitutional bodies, such goods or services shall be purchased or acquired only with a registered person.

b) Regarding Diplomatic Privileges:

For the purpose of clause (a) of sub-section (1) of Section 25 of the Act, a person enjoying diplomatic privileges shall submit an application, accompanied with the note given by the Ministry of Foreign Affairs, to the Department for the refund of tax amount.

c) Free Cooperation and Information:

His Majesty's Government shall provide free of cost the following cooperation and information:

(a) Information regarding the process to be adopted for the purpose of tax,

(b) Publications on taxpayer's education.16

d) Pleadings on Matters Concerning Value Added Tax:

In case it becomes necessary to plead any case concerning tax, it shall be done by the government attorney.

e) Format of Identity Card:

The format of the tax officer identity card shall be as set forth in Schedule 21.

f) To Issue Manual:

His Majesty's Government, Ministry of Finance may make issue necessary manuals in order to implement the Act and these Rules.

g) Alterations and Changes in the Schedules:

His Majesty's Government may by publishing notification in the Nepal Gazette effect necessary alterations or changes in the Schedules.

h) Repeal and Saving:

(1) The following Rules are hereby repealed:

(a) The Entertainment Tax Rules, 2018 (1961).

(b) The Sales Tax Rules, 2024 (1967).

(c) The Contract Tax Rules, 2024 (1967).

(2) Acts done or actions taken under the Rules mentioned in sub-rule (1) shall be deemed to have been done or taken under these Rules (Source: http://www.ird.gov.np./information).

2.12 Review of Empirical Studies, Books and thesis.

Various researchers have been conducted in Nepal as well as foreign countries about VAT. But only few researchers and studies are available focusing internal issues of VAT in Nepal. Here, some relevant books, university, dissertations, journals and other reference materials were reviewed exclusively. Essence of some useful and relevant ones in presented below in brief.

2.12.1 Review of Books

Carl S. Soup (1969) in his book entitled, "public finance" explains the value added tax as the latest and probably the final stage in the historical development of general sales taxation at the national level which is levied on the value added the differences between the sales proceeds and the cost of the materials etc. That has been purchased from other firm. VAT has eliminated the convene impact of turnover tax of the manufacturers and wholesalers sales taxes. A comprehensive consumption type of VAT is equivalent to a retail sales tax in its pure form except that the later does not offer an option between the destination principle and the origin principle. Soup has explained VAT differently in closed and open economy as follow:

Value added tax in closed economy

Gross product type of value added tax:

Tax base = GNP = C+I= W+P+D

Where, c= consumption, I= gross investment, W= wage, P= net profit after depreciation, D= depreciation

Income type of value added tax:

tax base = NNI = C+I-D = W+P

Capital exemption type of value added tax

Tax base = C+W+P+D-I

Value added tax in open economy

In an open economy, considering relative impotence of the gross-product type of VAT from practical point of view, more focus is given to capital – exemption type of VAT.

Wage type of VAT: the destination principle is less satiable as it would require each import to be broken down into its wages and profit elements. Similarly, each export will need to be broken down into the same two elements so that a tax rebate can be given for the value added tax paid domestically at earlier stages on the wage element. These complication are entailed under origin principle, moreover, no tax refund on account of the exemption of profits will be required.

Consumption type of VAT: Considering a two countries world, this type of VAT under destination principle would exempt the export sales of firms of a country and would impose a tax on the import purchases of another country's firms. These types would be much simple for both taxpayer and administration under destination principle.

In conclusion, consumption type of VAT is regarded superior, however; wage type of VAT is simpler than that of consumption type under the origin principle. While analyzing the computing methods of VAT, author favors the tax-credit method; however, the origin principle and the tax-credit method are somewhat incompatible, though perhaps not so much. So a country moving to the origin principle need give up the use of the tax-credit method. Lastly, VAT a more productive and neutral tax is also complex and regressive in nature.

Due and Meyer (1988), in their research Bulletin "Dominican Republic value Added Tax" examined the VAT in Dominican Republic, Ignoring the hostile reactions of business sector, labor union and even political parties VAT was introduced in 1983 in Dominican Republic. The increased record- keeping requirement became the main issue in the medium and small sizes business dominated economy of Dominican also the belief that VAT was responsible for inflation become another obstacle, but the inflation was due to other reasons. There was general agreement that the enforcement of the tax hadn't been adequate mainly because of lack of personal, evasion was wide speared, many firms failed to register. The overall evolution of the tax in the country, therefore remained rather negative while the tax has brought additional revenue, the inadequate enforcement and failure to extend it to the commercial sector as planned, and the use to making shift, distorting system in the latter have resulted in serious failure to attain the advantage of complete value added tax. The experience of the country with the tax provides a warning to other developing countries not to attempt to use a value added tax expending beyond to import and manufacturing sectors without careful consideration of the ability of the wholesale and retail sector to operate the tax and general attitude of these sectors toward the tax.

Khadka (2002), VAT expert, has explained the concepts of VAT and application of the same in Nepalese context in his book entitled " VAT in Nepal". VAT is the most recent innovation in the field of taxation. VAT is levied on the value added to goods and services. The value added for a firm his gross receipts form sales minus all expenditure on goods and services purchased from other firms. In the production and distribution process, a firm buys materials from other firms. These materials may include principle raw materials, auxiliary raw materials, chemical, electricity and capital goods such as machinery, equipment, building, furniture's, vehicles etc. the firm adds value to those purchased materials by processing or handling them with the help of its own factors of production such as labor, land, capital etc. This increase in the value of output over inputs.

Silwal(2002), has written a book entitled "Value Added Tax: A Nepalese experiences" incorporating his practical experiences and all aspects of VAT. The book mostly concentrates on Nepalese VAT system. According to the writer" "VAT is an all stages non cascading tax system. It extends to all levels of production and distribution. Any discrimination in taxing goods or services or exempting any of them proves VAT ineffective" Mr. Silwal suggests that factors affecting VAT design should also take into consideration. A poorly designed VAT accompanied by weak administration would just drain the treasury. So, almost care is crucial while designing VAT system. According to him the following issues have been considered while designing VAT in Nepal.

a. Tax base issues,
b. Rate structure issues,
c. Exemption issues,
d. Threshold issues,

Finally Mr. Silwal has reached a conclusion that the introduction of VAT provides an opportunity to revamp a substantial part of the tax administration. In every country where VAT has been implemented efficiently. It has proved itself as a major revenue productive instrument of tax.

Kandel (2006), has published a book entitled "Tax Laws & Tax Planning in Nepal" in 2006; this is book for MBS curriculum of Tribhuvan University. In his he has mentioned about VAT in Chapter-14Laws & Tax Planning in Nepal" in 2006; this is book for MBS curriculum of Tribhuvan University. In his he has mentioned about VAT in Chapter-14 concept of VAT , origin of VAT, its Development etc. are defined clearly and some numerical problem are also solved.

Pandit (2001), Under Secretary at the MOF, writes the first article on 'VAT Accounts and Audit'. He emphasizes for a visit to a tax payers premises, if any irregularity resulting in tax evasion is found while conducting a tax audit, then the tax officers assesses the tax amount that has evaded (IRD/DANIDA Report).
Joshi (2001), Deputy Director General of IRD, writes the second article," Tax Credit and Tax Refund Process under the VAT System". The tax refund process appears to rather lengthy in his opinion. He disclosed that there has been an increase in the amount refunded each year (IRD/DANIDA Report).

Bajracharya (2001) has written an article on "VAT Assessment, Penalties and the Appeal Procedure," He opined that the requirements of VAT registration for marginal entrepreneurs are not very much conductive for entrepreneur (IRD/DANIDA Report).

Bhandari (2001) has written an article on "Value Added Tax: A Retrospection” describes the mounting enthusiasm and zeal of the staff to the support of the MOF, the VAT Department and the DANIDA VAT Project (IRD/DANIDA Reports).
Thapa (2001) has written an article on" Implementation of VAT in Nepal: In Evaluation", the article points towards the weakness inherent in the value added tax system in Nepal. He is critical to the timing of the introduction of VAT in Nepal. He strongly denounces

the existence of an unstable government at the time of introduction, which forced the government to accept many compromises in this regard. He makes critique on the lack of serious consideration to the impact of smuggling from the long open borders with India and Tibet. The lack of highly motivated tax administration and proper accounting system are also impending the functioning of VAT in Nepal (IRD/DANIDA Report).

Kandel (2001) has written an article on ”Value Added Tax in the University Curriculum", His opines that an uncoordinated working atmosphere with the government and the universities, blowing their own trumpets, is not going to benefit the nation in any way (IRD/DANIDA Report).

Mallik (2001) has written an article on " Value Added Tax and the Practice of Issuing and Receiving Invoice in the Context of Market Economy", He believes that if market runs in a fair manner, the market principle will bring welfare to much happiness to many. He clearly points out his weakness on the part of the government, the business community and the general public. This tax system deserves concerted effort of all stakeholders. The business community may use cash machines and inexpensive billing software. They can develop the habit of quoting the price inclusive of VAT and remind customers to take invoice by displaying notices. He urges for black listing and transparency on the part of the business community. Customers can inform the tax authorities about the fraudulent transactions. The tax administration should increase surveillance and consumer education level (IRD/DANIDA Report).

Jyoti (2001) has written an article on "Value Added Tax in, Nepal: Analysis and Suggestions", He suggests that the practice of under invoicing should be discouraged and the same time the custom duties must be gradually deceased (IRD/DANIDA Report).

Richard Goode (1986), in his book entitled, "government finance in developing countries", described that VAT is most important innovation in public finance. This tax is applied to the value added at successive stages of production and distribution. Value added in equivalent to the sum of wages, salaries, interest, rent and profit. A value added tax may extend through the retail stage. In that case, it is similar to a retail sales tax on goods and services covered with the important difference that the value added tax is collected at each stage rather than being concentrated at the final stage of distribution.

Goode mentioned that the advantages of value added tax are as follows:

a. It is broad-based and relatively natural.
b. It avoids both simple cascading and cumulative taxation of goods of producers that are not physically incorporated in products.
c. Spreading the tax over the several stages of production and distribution is often considered an administrative advantage compared with collecting it all of one stage because an enterprise has less incentive to evade tax.
d. It generates the possibility of using information as a cross-check on compliances with other taxes, particularly income taxes.

Although VAT appears to have been successful in a number of developing countries, its advantages and practicability is questionable fro countries where much business is carried by small enterprises accounting is unreliable and the administration is week.

Ministry of Finance (1995), conducted a study by preparing a 'Task Force' headed by Prof. Madhan K. Dahal reviewed the Nepalese tax system. It mainly analyzed the magnitude of the Nepalese tax system and recommended various measures for the tax reforms.

The study was depended on theoretical base and the study reached the conclusion that "There is no possibility of any other great measure to introduce a tax rather than introducing VAT in Nepal".

The major findings of the study are:

The necessity of VAT in Nepal

a. To increase the revenue collection by boarding the tax base.
b. To make the tax system more buoyant
c. To discourse the tendency of tax evasion
d. To make the system efficient
e. To promote the export.

The existing tax system of Nepal generates less amount of revenue, so alternatives for the system should be searched. In this context the VAT appears as the best alternatives.

Some aspects for consideration of VAT are price level, equity, the condition of tax payers and small vendor.

IV A special consumption tax on luxuries goods sold be introduce as a supplementary tax for the VAT.

There must be fully and detailed preparation before implying VAT.

Nepal Chamber of Commerce (1997) made a study to analyze the possible effects of VAT on Nepalese economy makes some observation. The observations are:

a. Adverse effect on price level.
b. Increase in the price of imported goods would hit the import business and re-export of imported goods leading to a decline in the revenue from import tax.
c. The account keeping requirement of the VAT would increase the tax compliance cost and cost of doing business, it would adversely affect the small traders.
d. Adverse effects on domestic production due to the abolition of protection policy under VAT
e. VAT would be unjustifiable on social ground; it would aggravate the income distribution.
f. Negative effects in revenue collection and
g. Changes of failure of a VAT in Nepal are great because the present administration is incapable for handling a VAT.

The study concluded that VAT in Nepal should not be implanted in haste. A partial VAT on some commodities should be implemented on experimental basis to know its pros and cons and after that a full VAT might be considered.

Nepal chamber of commerce organized a nationwide discussion programme on VAT. According to a report of the discussion programme, various views expressed about VAT in Nepal may be summarized on follows,

a. Government machine is not capable for implementing a VAT
b. The business community has no confidence in the administration because it has failed to Implement many other taxes effectively and fulfill its own commitments

even previously.

c. VAT will hamper genuine trade and as consequence illegal trade will prosper. Rise in the price of domestic products will make them less competitive. Import and re-export of imported goods will get a negative impact leading to decline in government revenue.
d. VAT will inhibit the growth of newly developing trade activities in the country.
e. The modern account or keeping system is required but difficult due to the raise in costs of doing business.
f. There will be a sharp price rise if a VAT is introduced, consumer will be badly affected due to price rise. Nepalese markets in boarder area will dry up die to VAT.

It is concluded that it is not possible to implement a VAT in Nepal and if implemented it will have adverse effect on the economy.

2.12.2 Review of Earlier Studies

Sharma (2006) submitted a thesis "Contribution of VAT on Government Revenue in Nepal" According to his thesis she had analyzed the Focus on GDP and Total Revenue.) His main objectives are as follows;

a. To review theoretical aspects of VAT and analyze its contribution to government revenue
b. To examine the VAT as an instrument for internal resource mobilization
c. To identify the major problems with VAT
d. To recommend for making VAT effective and efficient

His major conclusion was proper invoicing system has not come into existence and under-invoicing and fake bill are still prevailing. Suppressions of sales value and under-reporting of actual transaction have been the challenges that VAT has to overcome in near soon. Similarly under valuation of imported goods in customs points have been the major hurdles for the effective implementation of VAT. In customs points the goods are not properly valued. The VAT administration also could not have still wiped the stink in its face as the common consumers and people think it as the most corruptible body in the country’s financial organization. The time has come out as the VAT administration should come clean in this regard.

Ghimire (2009) has also presented a thesis entitled, “VAT as a Tools of Revenue Mobilization in Nepal ". His research mainly objectives are as under;

a. To study the contribution of VAT in revenue collection in Nepal.
b. To study the trend of revenue collection before and after the implementation of VAT.
c. To study the relationship of VAT with Total Revenue, Total Tax Revenue and Total Indirect Tax Revenue.

His main conclusion was Introducing of VAT in Nepal is both compulsion and necessity. It cannot curtail its development projects for which more revenue required. The narrow tax base of the previous sales tax failed to generate the minimum required amount because it included only the import and manufacturing unit. Income tax however has some potentiality for revenue generation; the rates of income tax are slowly increasing because the Nepalese per capital income is very low. As Nepal has entered in to the WTO, shall need to reduce the custom duties drastically so the only one alternate is the introduction of VAT.

VAT was introduced in Nepal as the part of the national tax reform. VAT is supposed to be moving toward its goal. The biggest virtue of VAT is that it is revenue buoyant and highly instrumental for revenue mobilization especially in an economy with acute shortage of resources.

Kharal (2010) conducted a study entitled “A Study on The effectiveness of VAT in Nepal. His main objectives are as under;

a. To explore the prevalent constraints of applying VAT system.
b. To identify the major issues involved in the process of its implementation.
c. To analyze the trends of registration, refund and collection of VAT.
d. To measure contribution of VAT to government revenue.

e. To identify effective measures that government should introduce for effective return from VAT.
f. To recommend a package for effective implementation of VAT.

His main conclusion was as under;

There may be weak owing to the lack of practice of issuing an receiving invoices. Similarly there may be problem of under invoicing at the customs has not been reduced.

There may be misunderstanding between tax payer and tax administrator for refund of tax. One blame the VAT system has not been put in to proper practice while other complain that there is refund owing to the fact that the tax payers don’t even comply with simple formalities.

There may be lack of publicity and effective monitoring. In the implementation of VAT the main glitch has been in terms of the lack of public awareness. Until a time when a situation is created where the consumer himself/herself, it will be an uphill road for VAT.

Khanal (2009) had written a Master’s thesis entitled "A Study of Different sector contribution to VAT" His main objectives are as under;

a. To analyze the structure of tax in Nepal.
b. To study the contribution of services, trade and production sectors to VAT and
c. To examine the major problems of VAT and recommend appropriate measures to mobilize the addition revenue from VAT.

His major conclusion was Nepalese VAT system has suffered from several problems, these problems have limited the VAT base. If such problems are controlled, the VAT base will automatically increase and the VAT system will be elastic. Thus, this study concludes that there is immense scope of VAT, which can give right direction to the tax revenue and can be a perennial source of domestic revenue in Nepalese economy.

2.13 Research Gap

About fifteen years have been passed since VAT practice came into operation but very few studies had undertaken on the topic of VAT in Nepal. Among the studies most of the studies are theoretical. Even though, the researchers try to identify existing problems of

Nepalese VAT system. All the studies market area is only Kathmandu valley by conduction field survey, in order to know some how about the practice experience of VAT. All the research have conducted in different topic and different sense but this research as tried to analysis VAT collection system and review of legal provision concerning to VAT. So, this study will be fruitful to those interested person, scholars, students, teachers, civil society, stakeholders, businessmen and government for academically as well as policy perspectives.

CHAPTER – III
RESEARCH METHODOLOGY

3.1 Introduction

It is necessary to increase the internal revenue in order to operate nation and develop the economy and to decrease the dependency on foreign loan, grant, and technical assistance. VAT is the best and reasonable source of national revenue in Nepal. The trend of VAT realization and associated problems should be studied time to time to find out the ways for proper solution and to collect maximum VAT revenue. The tax could be adjusted as to except the lowest income groups from the operation for the tax and make the richer groups bear the burden of tax according to their income.

Research methodology generalizes the way solving the research problem systematically. Therefore, research methodology is used for the achievement of the objectives of the study. It includes Research Design, source of Data, Data Gathering procedure, Data Processing Procedures, and Statistical Tools. The study is mainly concentrated on VAT Collection System and Legal Provision in Nepal.

3.2 Research Design

As per nature of study survey research design was followed with descriptive and analytical approach. Thus, research design is the overall frame work for the achievement of the goals and objectives of the research.

3.3 Sources of Data

Data, which is essential to analyze the study, are collected from primary source. The primary source of data is the opinion survey through questionnaire, field visit and information received from the respondents.

Secondary data are those data which has been used preciously, so, published newspaper, budget speech, website of Ministry of finance, Inland Revenue Department, previously conducted research work were the main source of secondary data.

3.4 Data Gathering Procedures

As the study was based on primary data, information was collected developing a scheduled questionnaire and distributing it to administrators, VAT collectors and tax payers. Nine tick mark, two ranking type and one open ended questions were included in the questionnaire (see appendix: 3). All together 50 questions were distributed to different 3 groups i.e. Administrative, VAT Collectors and Tax Payers. The no. Of individual groups was 20 from Administrative, 10 from VAT Collectors and 20 from Tax Payers. The samples from Primary data were as follows;

Respondents	Sample size
Administrative Staffs	20
VAT Collectors	10
Tax Payers	20
Total	50

3.5 Data Processing Procedures

Data obtained from different source have no meaning unless they will be arranged and presented in a systematic manner, was further needed to be verified and simplified from the purpose of analysis. Moreover, data and information so gathered will be checked, edited and tabulated in such a way that can provide convenience for at the last part of the study. Questionnaires were distributed to administrators, VAT collectors and tax payers.

In this way, the primary data were collected and thus collected data was noted down to use during analysis and interpretation of data.

3.6 Statistical Procedures

Simple percentage were used an arithmetic too to interpret data along with supporting tables and bar diagram for their diagrammatic presentation. For the interpretation of the responses three types of groups were made such as administrators, VAT collector and tax payers.

CHAPTER - IV

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

This chapter is the heart of research. This is the origin of all concepts, suggestions, analysis and interpretation. So, collated data were tabulated and analyzed in such a manner that a non-mathematical person can understand the meaning of data.

4.2 Tabulation of Data

There were numerous data but only that data were tabulated which were related to this topic. Extraction of data is repaired for the analysis of research. So, all the related data we arranged in systematic manner.

4.2.1 Government Revenue, Expenditure and Deficit

Expenditure, Revenue and Deficit are the most related in the economic perspective. There exists government expenditure in each state of activities; either collecting revenue or distribution of governmental services. When revenue exceeds the expenditure then profit arises. In Nepalese context, it is just opposite. Here, expenditure has exceeds revenue in each fiscal year.

To fulfill the gap of expenditure and revenue administrative efforts can play important role in some extent. Otherwise, there is needed huge amount of external resources like foreign aids, multinational investments etc.

The following table shows the governmental expenditure and deficit for the different fiscal year.

Table 4.1

Government Revenue, Expenditure and Deficit

(Rs. In 10 millions)

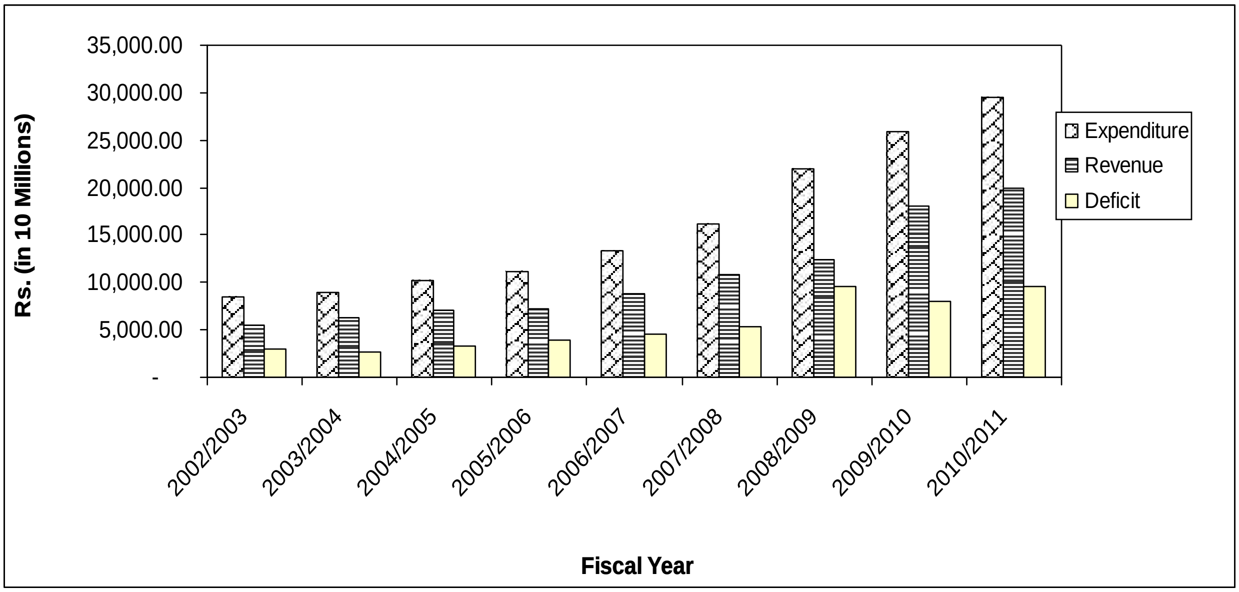
Fiscal Year	Expenditure	Revenue	Deficit
2002/2003	8,400.61	5,453.89	2,946.72
2003/2004	8,944.26	6,233.10	2,711.16
2004/2005	10,256.04	7,012.27	3,243.77
2005/2006	11,088.92	7,228.19	3,860.73
2006/2007	13,360.46	8,771.19	4,589.25
2007/2008	16,134.99	10,762.25	5,372.74
2008/2009	21,966.20	12,347.45	9,618.75
2009/2010	25,968.91	17,994.58	7,974.33
2010/2011	29,536.34	19,981.87	9,554.47
Average	**16184.08**	**10642.75**	**5541.32**

Source: MOF/NG, Economic Survey- 2010/11

From the above table it can be Cleary seen the revenue and expenditure is increasing continuously. In fiscal year 2005/2006 revenue and expenditure were Rs.7228.19 million and RS. 11088.92 Respectively and deficit was Rs. 3860.73 million. It means increasing r of rate expenditure is greater than increasing rate of revenue. There was greater deficit in Year 2008/2009 because in this year expenditure is more in compare to revenue. Some as in year 2010/2011 deficit seems to more but compare to year 2008/2009 is low in amount. It is concluded the expenditure and revenue are increasing year by year in increasing trend and deficit is also in increasing trend except year 2003/2004 and 2009/2010 and max deficit at year 2008/2009.

Figure 4.1

Government Revenue, Expenditure and Deficit



From the above diagram it is found that there was a highest gap between the expenditure and revenue in the fiscal year 2010/2011 which indicates that there is highest deficit and lowest gap between the expenditure and revenue in the fiscal year2003/2004. For the better improvement of the nation deficit should be converted into surplus.

4.2.2 Structure of Total Revenue in Nepal

Every state in the world performs numerous activities for the betterment of economical, social condition. For these activities huge amount of resources is necessary. So, every state collects revenue from internal as well as external resources. In Nepal, revenue is collected through grants, administrative incomes, businessman income and taxation. Generally the government revenue is classified into two categories such as tax revenue and non-tax revenue.

It cannot be said that there are not other resources. Nepal has other resources like repayment of loan, grants for the improvement of the existing condition. These sources are desirable to meet the fiscal deficits.

Contribution of tax revenue and non- tax revenue, trend analysis and the percentage description is presented below in the form of table, diagram and in paragraph:

Table 4.2

Structure of Total Revenue in Nepal

(Rs. In 10 millions)

Fiscal Year	Total Revenue	Tax Revenue		Non- Tax Revenue	
		Amount	Percent	Amount	Percent
2002/2003	5,453.89	4089.6	0.75	1364.29	25
2003/2004	6,233.10	4817.3	77.28	1415.8	22.71
2004/2005	7,012.27	5410.47	77.15	1601.8	22.84
2005/2006	7,228.19	5743.04	79.45	1485.15	20.05
2006/2007	8,771.19	7112.67	81.09	1658.54	23.31
2007/2008	10,762.25	8515.55	79.12	2246.7	20.87
2008/2009	12,347.45	11705.19	94.79	2642.26	21.39
2009/2010	17,994.58	15629.49	86.85	2365.09	13.14
2010/2011	19,981.87	17277.76	86.46	2704.11	13.53
Average	**10642.75**	**8922.34**	**73.66**	**1942.64**	**20.32**

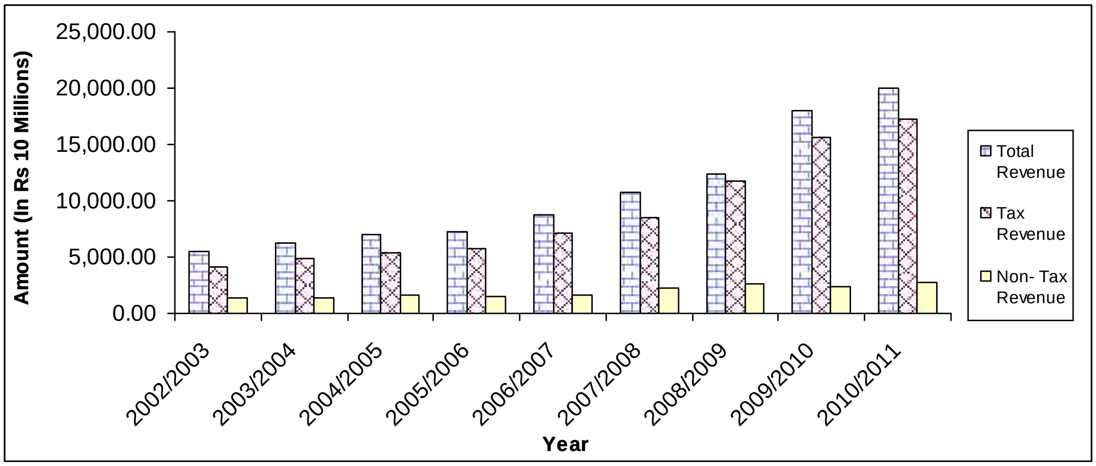
Source: MOF/NG, Economic Survey- 2010/11

From the above table show that the share of tax revenue and non tax revenue were 75% and 25% respectively to the total revenue of FY 2002/2003. It means a major amount of Government revenue is collected from tax revenue. As compare to tax revenue, the contribution ot non-tax revenue to total revenue has a very low share. Such kinds of share to tax revenue and non-tax have not been changed even in FY 2006/2007. In FY 2010/2011, the share of tax revenue is 86.46% and non tax revenue was 13.53%. So, for the betterment of economic improvement non-tax revenue should be increase.

It is concluded the total revenue and tax revenue are in increasing trend and where as non-tax revenue is at fluctuating trends, contribution of tax revenue has huge share as compare to non-tax revenue.

Figure 4.2

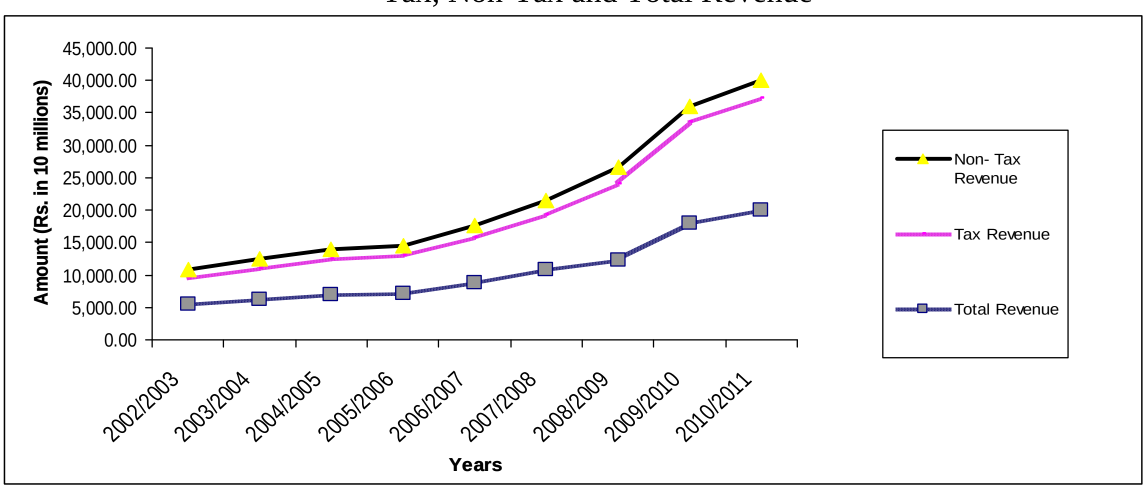
Tax, Non-Tax and Total Revenue



From the above diagram is is shown that the contribution of non- tax revenue is very low as compared to the tax revenue. In FY 2002/2003 to 2010/2011 the tax revenue has increased and non-tax revenue has at fluctuating trend. It is clearly seen in the figure contribution of tax revenue has huge share as compared to the non-tax revenue and maximum contribution is at FY 2010/2011,contribution of non-tax revenue was very poor but maximum contribution is seen in the FY 2010/2011. So, for the betterment of economic development it should be improved.

Figure 4.3

Tax, Non-Tax and Total Revenue



The gap between the tax revenue and non-tax revenue is increasing trend but in FY 2009/2010, the non-tax revenue has decreased and then in FY

2010/2011, the non-tax revenue is increase for the better improvement of the economic development trend of tax revenue should be shift upward.

4.2.3 Tax Revenue Structure of Nepal

In Nepal, Value Added Tax (VAT) was introduced on 16 Nov. 1997. This tax was levied in place of the Sales Tax, Hotel Tax, Contract Tax and Entertainment Tax. However, it could not be implemented fully until the FY 1998/99 due to political instability and strong opposition from the business community. It is compulsory contribution that the taxpayer to the government. There were a lot of resources of income generation. But taxation is the main source of income. Tax Revenue comprises compulsory, unrequited, non-payable receipts collected by the government for public revenue. It concludes interest collection on tax arrears and penalties collection on non-payment or late payment of taxes. Tax revenue is the principle source of the government revenue; however it's contribution differs significantly in different countries. In Nepal, tax revenue is major source of government to mobilize internal source effectively and properly as it has been dominating the government revenue by contributing around three quarters of total revenue. In the revenue trend of Nepal, tax revenue structure is a combination of two tax elite, one is direct tax & another is indirect tax.

Table 4.3

Structure of Total Tax Revenue

(Rs. In 10 millions)

Fiscal Year	Total Tax Revenue	Direct Tax		Indirect Tax	
		Amount	Percent	Amount	Percent
2002/2003	4089.6	1088.19	26.6	3001.41	73.4
2003/2004	4817.3	1191.26	24.73	3626.04	75.27
2004/2005	5410.47	1307.18	24.16	4103.29	75.84
2005/2006	5743.04	1396.81	24.32	4346.23	75.68
2006/2007	7112.67	1898.03	26.68	5214.64	73.31
2007/2008	8515.55	2308.77	27.11	6206.78	72.89
2008/2009	11705.19	3432.07	29.93	8273.12	70.67
2009/2010	15629.49	4175	26.71	11454.49	73.29
2010/2011	17277.76	4865.5	28.16	12412.26	71.84
Average	**8922.34**	**2406.98**	**26.49**	**6515.36**	**73.58**

Source: MOF/NG, Economic Survey- 2010/11

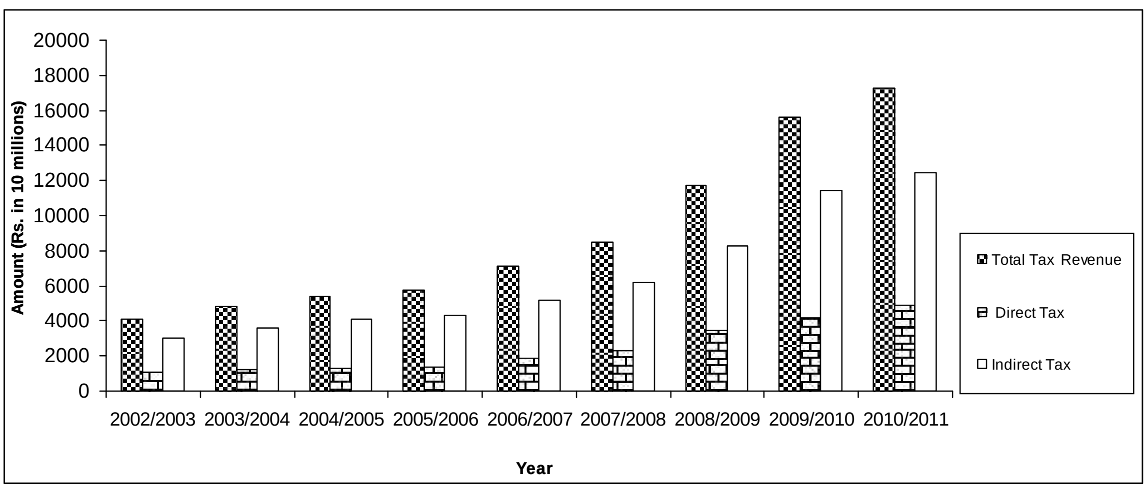
Total tax revenue is composed of direct tax and indirect tax. During the study period, there has been simultaneous increase in total indirect tax and direct tax revenue as shown in above table. In FY 2002/2003 the amount of total tax revenue, direct tax revenue, indirect tax revenue was Rs.4089.6 million, Rs.1088.19 million, Rs.301.41 million respectively. The amounts were increased to Rs. 8515.55 million, Rs2308.77 million and Rs. 6206.78 respectively in FY 2007/2008. Similarly in FY 2010/2011 it was increase i.e. Rs. 17277.76 million, Rs. 4865.5 million and Rs.12412.26 million respectively.

By the above study, share of direct tax revenue and indirect tax revenue were 26.6% and 73.4% respectively to the total tax revenue in FY 2002/2003. It means revenue from indirect tax is more than revenue from direct tax. Such kind of share of direct tax and indirect tax has not been change even in FY 2007/2008. In FY 2010/2011, the share of direct tax is 28.16% and indirect tax revenue is 71.84%.

Nevertheless, the indirect tax revenue still contributes three quarter of total tax revenue while direct tax revenue ever represent only about one quarter of total tax revenue. It would however not be very difficult to understand as to why the indirect tax has got the lion share in the total tax revenue. The industries have not developed adequately. The population is dominated by the subsistence whose per capita income is very low.

In Nepalese perspective, while the direct tax seems to be justified, the indirect tax is unavoidable. The direct tax is justified because it helps to mobilize revenue for the national exchequer and also assists to narrow the gap in the distribution of income and wealth between the richer and the poorer sections of the society, which is essential for development. However, under the existing circumstances, the direct tax can't generate sufficient revenue to the national exchequer. It is only through the indirect tax that adequate revenue can be mobilized and the consumption of harmful commodities or the investment in the unproductive sectors of the economy can effectively be discouraged. Thus, though there is the need for Nepal government to rely upon the direct tax, which would have an more dominating role in the Nepalese economy, at least for mobilizing adequate resources of development.

Figure 4.4
Structure of Total Tax Revenue

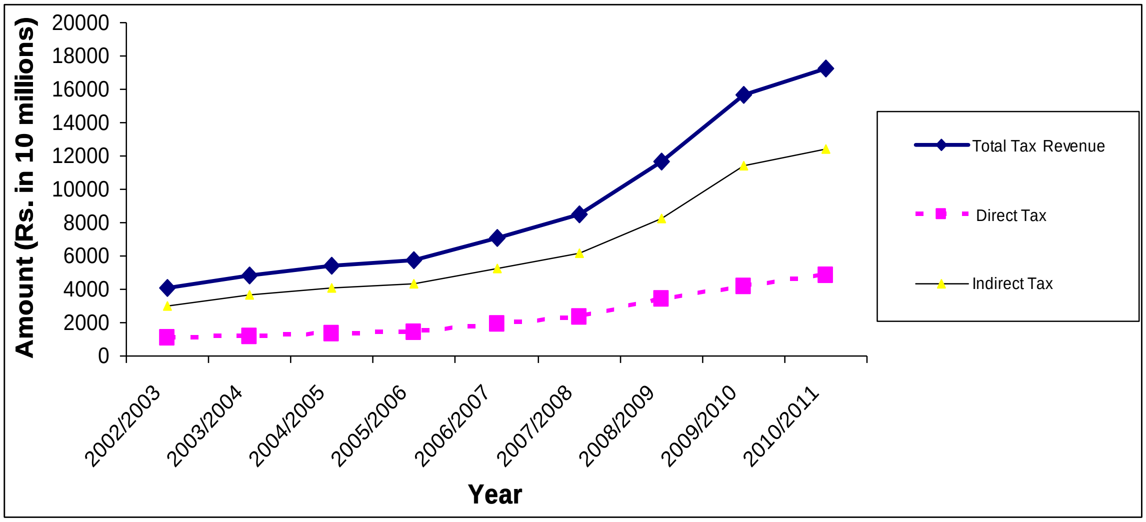


Above bar diagram clearly shows that amount of indirect tax are increasing continuously and the direct tax is also increasing but comparision to indirect tax it's increasing trend is low.

From the above table it is found that the whole Nepalese tax structure is dominited by indirect tax revenue. On the other hand the share of indirect tax as percentage of total tax revenue is firstly increasing and then in fluctuating trend. Whereas the direct tax revenue is in fluctuating trend.

Figure 4.5

Trend of Direct Tax and Indirect Tax with Respect to Total Tax Revenue



From above table and figure it is found that previously presented trend of direct tax and indirect tax clearly shows that the gap between these two revenue sources is in increasing trend, which is good indicator for economic development. For the economic growth of developing country like Nepal it is necessary to increase direct tax. Then the share of direct tax to the total tax revenue will be increased and ultimately share of indirect tax will be decreased in some extent.

4.3 Revenue Collection from VAT

From the literature of review and case study it is clear that the VAT which is practiced during past 10 years is best form of sales tax. VAT is neutral regarding method of production and helpful in generation of more revenue collection. Because of its broad coverage, neutrality transparency and fairness, VAT will generate more revenue with less distortion. The revenue collection from VAT in different fiscal year is presented below in table 4.4.

Table 4.4

Revenue Collection from VAT

(Rs. In 10 millions)

Fiscal Year	Revenue collection form VAT	Percentage change
2002/2003	1345.97	-
2003/2004	1447.89	7.57
2004/2005	1888.54	30.43
2005/2006	2161.07	14.43
2006/2007	2609.56	20.75
2007/2008	2981.57	14.25
2008/2009	3970.09	33.15
2009/2010	5492.09	38.33
2010/2011	6166.36	12.27

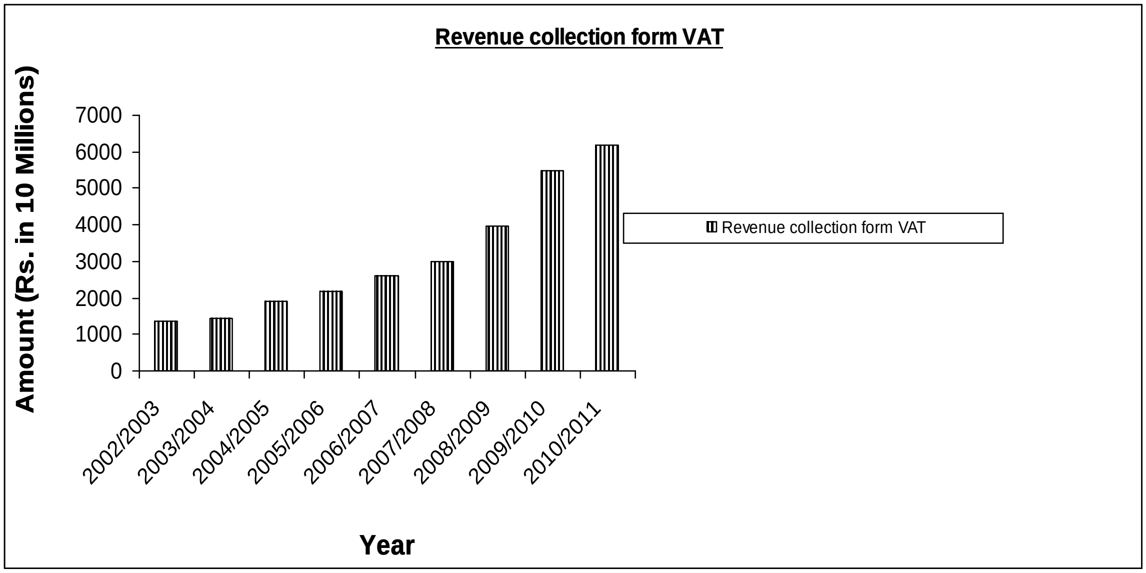
Source: MOF/NG, Economic Survey- 2010/11

From the above table it is found that the revenue collection from VAT is increasing trend. In FY 2003/2004 there is lesser amount of increase in VAT by 7.57% there was the highest revenue collection in FY 2010/2011 i.e. 12.27%. Similarly, the percentage change in revenue collection is increasing in FY 2004/2005 and in 2006/2007 and 2008/2009. But, there was very low percentage change FY 2002/2003 and in 2010/2011. At FY 2002/2003 percentage change of VAT was very low as compare to other FY.

It is concluded that revenue collection from VAT is at increasing at decreasing rate and max. At 2010/2011 and percentage change is at fluctuating.

Figure 4.6

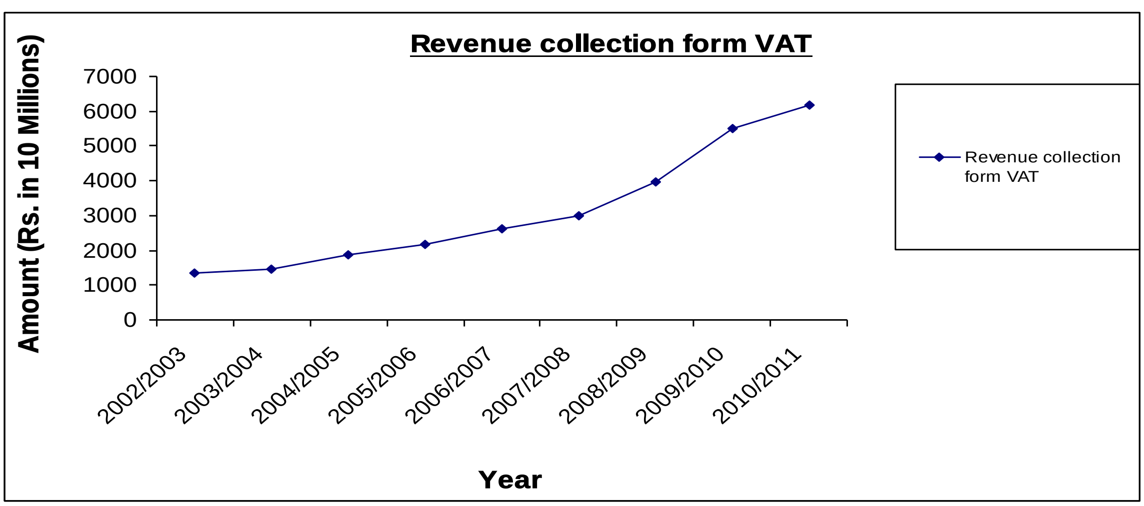
Bar Diagram of VAT collection



From the above figure it is found that the revenue collection from VAT is in increasing trend except.In FY 2003/2004 there is lesser amount of increase in VATby 7.57% there was highest revenue collection in fiscal year 2010/2011. Similarly, the percentage change in revenue collection is increasing in FY 2004/2005 & in 2006/2007 and 2008/2009. But, there was very low percentage change FY 2002/2003 & in 2010/2011. At FY 2002/2003 percentage change of VAT was very low as compare to other FY.

Figure 4.7

Trend Lines of VAT collection



Above trend of revenue collection from VAT shows that, there was the increasing trend in revenue collection. This shows revenue collection from VAT is good.

Since, VAT is a main source of government revenue it provides suitable base revenue to the government. Though there was a fluctuating trend of VAT collection it is not so bad. It is expected that VAT will generate more and more revenue in the coming days. It will be better when there exist positive percentage change in the revenue.

4.4 Contribution of VAT to Total Revenue

The percentage contribution of VAT revenue to total revenue is presented in the below table and Line diagram;

Table 4.5

Contribution of VAT to Total Revenue

(Rs. In 10 millions)

Fiscal Year	VAT Revenue	Total Revenue	Percentage of VAT
2002/2003	1345.95	5453.89	24.68
2003/2004	1447.89	6233.1	23.23
2004/2005	1888.54	7012.27	26.93
2005/2006	2161.07	7228.19	29.9
2006/2007	2609.57	8771.19	29.75
2007/2008	2981.57	10762.25	27.7
2008/2009	3970.09	12347.45	32.15
2009/2010	5492.09	17994.58	30.52
2010/2011	6166.36	19981.87	30.85
Average	**3118.2**	**10642.75**	**29.29**

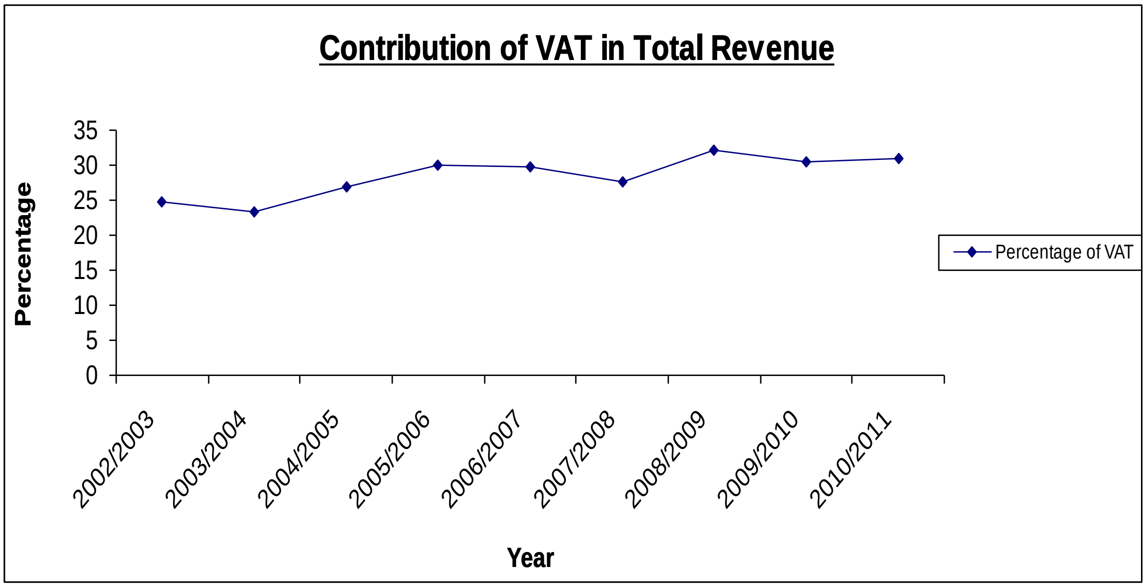
Source: MOF/NG, Economic Survey- 2010/11

From the above table and trend presented below it shows that VAT revenue is increasing from fiscal year 2002/2003 to up to FY 2010/2011 and total revenue is also increasing from FY 2002/003 to up to FY 2010/011. During the study it is found that the highest contribution of VAT revenue to total revenue was 32.15% in FY 2008/009. But lowest contribution of VAT revenue to total revenue was 23.23% in FY 2003/2004.

It is concluded that there was increasing trend of VAT revenue to total revenue throughout the study period.

Figure 4.8

Trend Lines of VAT in Total Revenue



4.5 Contribution of VAT to Total Tax Revenue

The percentage analysis of VAT to total tax revenue is presented below;

Table 4.6

Contribution of VAT to Total Tax Revenue

(Rs. In 10 millions)

Fiscal Year	VAT Revenue	Total Tax Revenue	Percentage of VAT
2002/2003	1,345.95	4089.6	31.6
2003/2004	1,447.89	4817.3	30.05
2004/2005	1,888.54	5410.47	34.9
2005/2006	2,161.07	5743.04	37.62
2006/2007	2,609.57	7112.67	36.68
2007/2008	2,981.57	8515.55	35.01
2008/2009	3,970.09	11705.19	33.91
2009/2010	5,492.09	15629.49	35.13
2010/2011	6,166.36	17277.76	35.68
Average	**3118.12**	**8922.34**	**35**

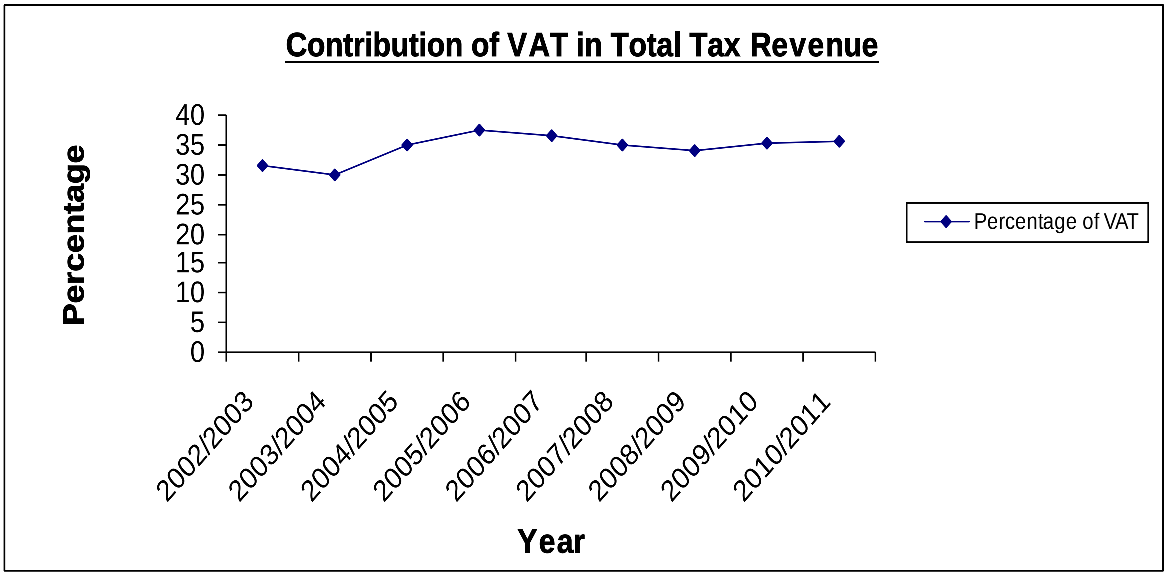
Source: MOF/NG, Economic Survey- 2010/11

From the above table and trend presented below it shows that the contribution of VAT to total tax revenue is not smooth. It is fluctuating from FY 2002/003 to 2010/011. Firstly it was decrease then increased. There was highest contribution of the VAT to total tax revenue in fiscal year 2005/006 of 37.62% and lowest in the fiscal year 2003/004 of 30.05%.

It is concluded that VAT revenue and total tax revenue are increasing trend throughout the study period.

Figure 4.9

Trend Lines of VAT in Total Tax Revenue



4.6 Contribution of VAT to Total Indirect Tax Revenue

The percentage contribution of VAT revenue in total indirect tax revenue is presented in the below table;

Table 4.7

Contribution of VAT to Total Indirect Tax Revenue

(Rs. In 10 millions)

Fiscal Year	VAT Revenue	Total Indirect Tax Revenue	Percentage of VAT
2002/2003	1,345.95	3001.41	44.84
2003/2004	1,447.89	3626.04	39.93
2004/2005	1,888.54	4103.29	46.02
2005/2006	2,161.07	4346.23	49.72
2006/2007	2,609.57	5214.64	50.04
2007/2008	2,981.57	6206.78	48.03
2008/2009	3,970.09	8273.12	47.98
2009/2010	5,492.09	11454.49	47.94
2010/2011	6,166.36	12412.26	49.67
Average	**3118.12**	**6515.37**	**47.85**

Source: MOF/NG, Economic Survey- 2010/11

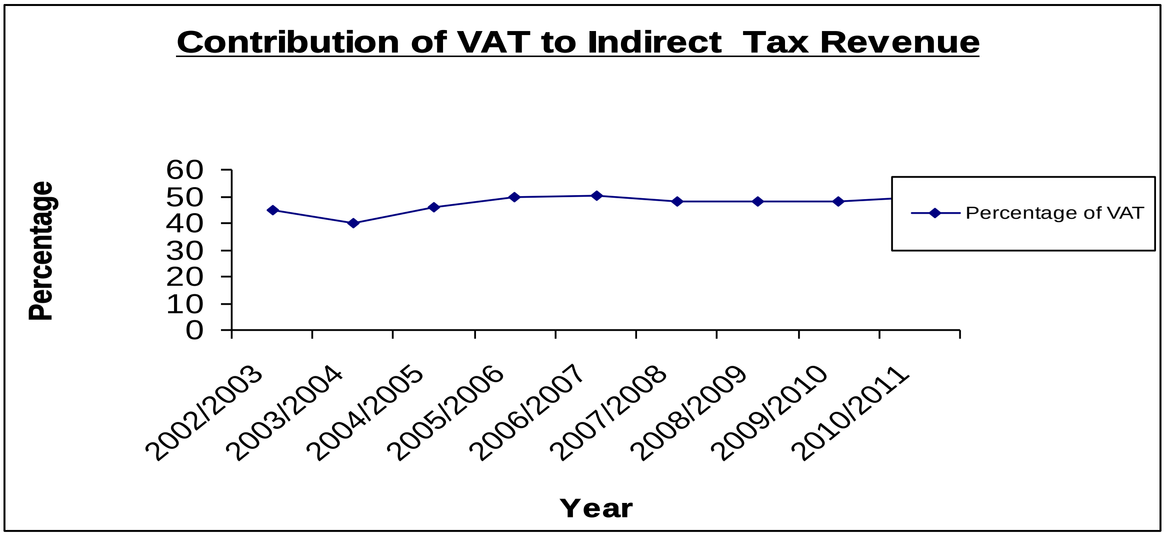
From the above table 4.7 and below trend presented shows that the share of VAT revenue in total indirect tax 44.84% in FY 2002/2003, in FY 2003/004 it has decreased to 39.93%. After the FY 2004/005 up to 2006/007 it was increased i.e. 46.02%, 49.79%& 50.04% respectively, and then after in FY 2007/008 up to 2009/010 was decrease i.e. 48.03%, 47.98%&47.94% respectively. At the end i.e. in the FY 2010/011 it reached to 49.67% which is good in comparison to FY 2002/003.

In this way highest percentage of VAT to indirect tax revenue is 50.04% in FY 2006/007 and lowest contribution of VAT to indirect tax is 39.93% in FY 2003/004. There is decreasing percentage trend of contribution of VAT to indirect tax revenue from 2002/003 to 2003/004, increasing percentage trend form 2004/005, 2005/006 &2006/007 and decreasing trend from 2007/008, 2008/2009& 2009/010 and increased at FY 2010/011.

In is concluded the VAT revenue and total indirect tax revenue is increasing year by year and contribution of VAT to total indirect tax revenue is fluctuating.

Figure 4.10

Contribution of VAT in Indirect Tax Revenue



4.7 Contribution of VAT to GDP

The contribution of VAT to Gross Domestic Product is presented in the following table and trend presented below;

Table 4.8

Contribution of VAT to GDP

(Rs. In 10 millions)

Fiscal Year	VAT Revenue	GDP	Percentage of VAT
2002/2003	1,345.95	46032.5	2.92
2003/2004	1,447.89	50069.9	2.89
2004/2005	1,888.54	54848.5	3.44
2005/2006	2,161.07	61111.8	3.53
2006/2007	2,609.57	67585.9	3.86
2007/2008	2,981.57	75525.7	3.94
2008/2009	3,970.09	90952.8	4.36
2009/2010	5,492.09	108341.5	5.06
2010/2011	6,166.36	124642.3	4.94
Average	**3118.12**	**75456.76**	**3.88**

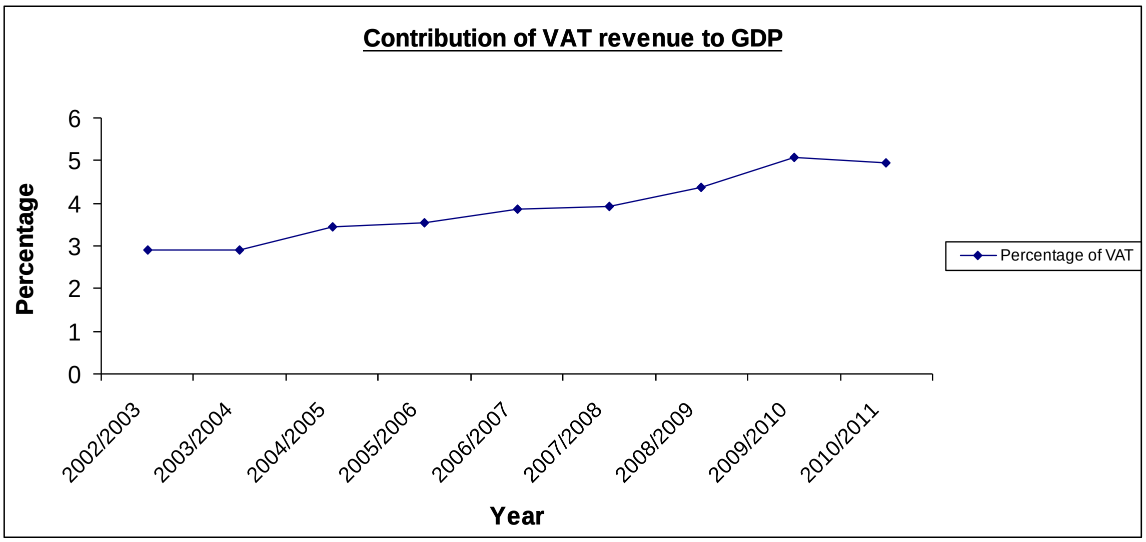
Source: MOF/NG, Economic Survey- 2010/11

The percentage contribution of VAT in GDP is presented in the above table and trend presented below. The share of VAT in GDP does not show even trend. As shown in table 4.8 the share of VAT revenue as percentage of GDP is 2.92% in FY 2002/003 decrease to 2.89% in FY 2003/004 and it is increase after FY 2004/005 up to 2009/010 i.e. 3.44%, 3.53%, 3.86%, 3.94%,4.36% and 5.06% respectively and decrease at FY 2010/011 i.e. 4.94%.

It is concluded that percentage of VAT revenue to GDP is in fluctuating trend due to fluctuation in VAT Collection.

Figure 4.11

Contribution of VAT revenue to GDP



4.8 VAT Registration

The operation of VAT in Nepal was started by addressing the sales tax registrants to register in the VAT department. The registration is compulsory for these business enterprises that have taxable transaction and taxable capacity; however the traders falling below the threshold limit can register voluntarily. Under the existing sales tax system, there were nominal registrants but VAT was in existence the number of registrants increased significantly. However, when VAT was introduced in 1997/98, there was strict opposition from the business community so VAT could not be implemented in full form. But after different provisions and aspects of VAT, business community and the government reached to an agreement in 1999/000. Then after VAT was implemented in its full form so, that the number of VAT registration has been given below in the following table:

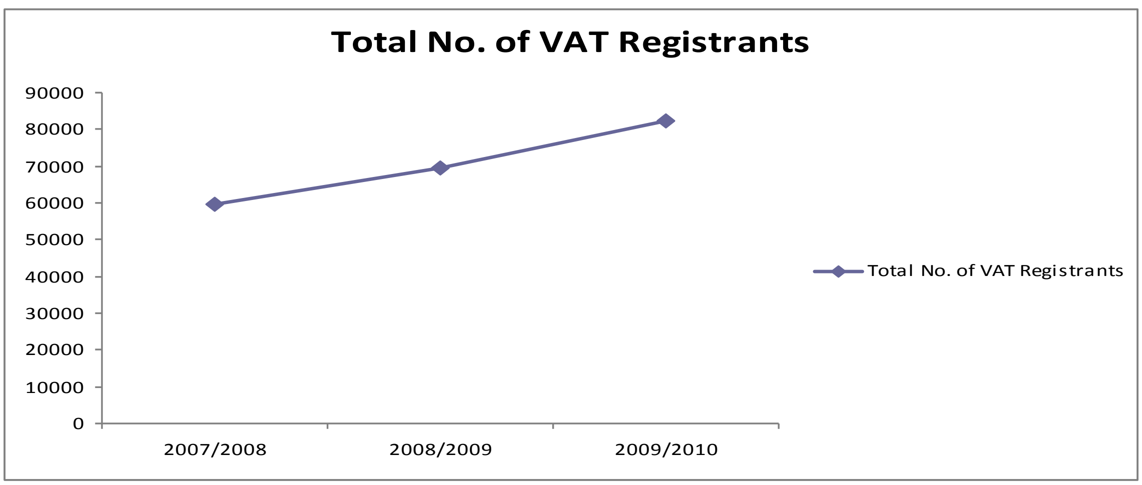
Table 4.9

Total NO. Of VAT Registrants

Fiscal Year	Total No. of VAT Registrants
2002/2003	NA
2003/2004	NA
2004/2005	NA
2005/2006	NA
2006/2007	NA
2007/2008	59775
2008/2009	69653
2009/2010	82433
2010/2011	NA

Source: MOF/NG, Economic Survey- 2010/11

Figure 4.12



From the above table it is found that the no. of VAT registrants in 2007/008 was 59,775 & increased to 69,653 in 2008/009 and also increased to 82,433 in 2009/010. This is shown that VAT registration no is increasing year by year and maximum at FY 2009/010 that shows the increase in the number of VAT registrants is impressive.

It is concluded that number of VAT registration is increasing trend throughout the study period.

4.9 Major Empirical Analysis

An empirical study was conducted in order to find out the various aspects of VAT from the experience of the real world. In this study, the analysis has been done about

VAT on the basis of information collection by Questioner from Administrator, VAT Collector and Tax payers.

In this study, the questions were asked to 50 different individuals related to this field i.e. 20 from Administrator, 10 form VAT collectors and 20 from Tax payer. The questions have covered various aspects of VAT. (See the format of questioners in appendix 1).

4.9.1 View on VAT appropriate means of raising the public Revenue.

Contribution that may be from internal or external is used for the development of nation by the government. All the sources are the mean of increasing the public revenue. There was highest contribution of VAT on public revenue of 32.15% in the fiscal year 2008/009.

The field study shows that the following results which presented in the tabular as well as descriptive form below;

Table 4.9.1

Total NO. Of Public Revenue

Respondents	Yes		No		Total
	Number	%	Number	%	
Administrators	17	85	3	15	20
VAT Collectors	9	90	1	10	10
Tax payers	9	45	11	55	20
Total	35	70	15	30	50

Source: Field Survey, 2012

85% of administrators, 90% of VAT Collectors and 45% of tax payers said that VAT is the appropriate mean of raising public revenue. Where as 15% of administrators, 10% of VAT Collectors and 55% of tax payers said that VAT, is not appropriate mean of raising public revenue. Most of tax payers are not favor of raising the public revenue.

So, it can be said that VAT is the appropriate mean of raising the public revenue. Though there are large numbers of tax payers who are not in the favor. They are not well familiar to the phenomenon of VAT.

4.9.2 View on superiority on VAT to the areas it has replaced.

VAT is advanced form of sales tax. It is indirect tax. Among the other taxes like hotel taxes, entertainment taxes and sales taxes it is superior. The same question was asked to the respondents at the time of field survey. Their attitudes towards the superiority of VAT than other taxes are presented in the following table:

Table 4.11

Total NO. Of Superiority of VAT

Views on superiority of VAT to the areas it has replaced					
Respondents	Yes		No		Total
	Number	Percent	Number	percent	
Administrator	18	90	2	10	20
VAT Collector	8	80	2	20	10
Tax Payers	13	65	7	35	20
Total	39	78	11	22	50

Source: Field Survey, 2012

From the above table it can be said that VAT is superior to the other taxes like sales tax, hotel tax and entertainment tax. Majority of the respondents proved this statement although there was a negative aspect of tax payers. Out of 20 taxpayers 13 were in the favor and rest was in negative aspect which holds 65% and 35% respectively. It is concluded that 90% of administrators and 80% of VAT collectors shows positive opinion on the superiority of VAT to the area it has replaced.

4.9.3 View on sufficiency of Legal Provision Concerning to VAT Collection System.

Before implementation of VAT, the government has prepared VAT Act 2052 and VAT Regulation 2053. But the legal provision and rules in general different to understand by all. The documents of these enactments carry all the matters such as VAT administration and its operation, the tax officers and its authorities (duty and responsibility)tax payers 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 with reference to current system of VAT. The outline/attitude of the respondent on this aspect is presented in the following table:

Table 4.12

Total NO. Of Legal Provision

Sufficiency of Legal Provision Regarding to VAT Collection										
Respondents	Yes		No		I Don't Know				Total
	No.	%	No.	%	No.	%	No.	%	
Administrator	13	65.00	7	35.00	0.00	0.00	0.00	0.00	20
VAT Collector	6	60.00	4	40.00	0.00	0.00	0.00	0.00	10
Tax Payers	7	35.00	6	30.00	7.00	35.00	7.00	35.00	20
Total	20	52.00	17	34.00	7.00	35.00	7.00	35.00	50

Source: Field Survey, 2012

The field survey shows that 65% administrators, 60% VAT collector and 35% tax payers were in the favor of existing legal provision relating VAT in Nepal. On the other hand 35% of administrators, 40% VAT collectors and 30% of the tax payers were unknown about the legal provision relating to VAT. So, finally it can be concluded that the legal provision relating to VAT collection system in Nepal are sufficient. There is only lack of proper implementation.

4.9.4 Views on Collection System

It is clear that VAT in Nepal not implementing effectively. On the assistance of the revenue Department random monitoring is conducted which indicates that there is some effort to make VAT system tighten. The activities like preparation of documents, timely payment of tax, proper valuation of goods and services are lies in the VAT collection system. Also invoices making and taking is the important one. A question that relates VAT collection system was asked to the respondent. The question was what degree of Liberace is used when VAT is collected? The views of different respondent are presented in the following table;

Table 4.13

Total NO. Of Collection of VAT

Degree of Liberalism in Collection of VAT							
Respondents	Strict		Medium		Low		Total
	No.	%	No.	%	No.	%	
Administrator	12	60	6	30	2	10	20
VAT Collector	5	50	3	20	3	30	10
Tax Payers	15	75	2	15	2	10	20
Total	32	64	11	22	7	14	50

Source: Field Survey, 2012

60% of administrator, 50% of VAT collectors and 75% of tax payers said that VAT is strictly collected where as the percentage of medium are 30% administrators, 20% of VAT collector and 15% of tax payers where as 10% of administrator, 30% of VAT collectors and 10% of tax payers said that the implementation of VAT collection system is low.

4.9.5 Views on Revenue Collection from VAT

In the early stage of the VAT implementation in Nepal, there was low contribution of VAT on total revenue, Indirect tax and domestic production. Now it has been increased in some extent. Government expenditure is also increasing trend of expenditure. When VAT is collected as it had been expected, there will be a probability of surplus.

Table 4.14

Total NO. Of Satisfactory from VAT

Satisfactory Towards collection of Revenue from VAT					
Respondent	Yes		No		Total
	No.	%	No.	%	
Administrators	2	10	18	90	20
VAT Collector	2	20	8	80	10
Tax Payers	7	35	13	65	20
Total	11	22	39	78	50

Source: Field Survey, 2012

From the field survey, 78% respondents argue that revenue collection from VAT is not satisfactory as it has been expected, 90% and 80% of administrators and VAT collectors says that VAT is not getting expected amount of revenue. But 35% of tax payers said that VAT is achieving expected amount of revenue. It is concluded that collection from VAT is not satisfactory.

4.9.5 Views on problem in the process of VAT collection in Nepal

Expected revenue from VAT is not collected due to existing various first of all problems should be avoided. The major problems may be lack of knowledge about VAT to the tax payers, tedious work, administrative problems, lack of skilled manpower and improper billing system. To find the major problems respondents were requested to rank their responses on the given choice. In case of analysis every rank has some score with it 6 marks are given to the most important problem and 1 to the least important problem. The survey result is presented here below.

Table 4.15

Total NO. Of Process of VAT Collection

Problem in the process of VAT collection in Nepal				
Problems	No. of respondent	Score	%	Rank
Lack of knowledge	50	157	17.44	3
Tedious Work	50	112	12.44	5
Administrative Problem	50	176	19.56	2
Lack of Skilled Manpower	50	140	15.56	4
Improper Billing System	50	248	27.56	1
Others	50	67	7.44	6
Total		900		

Source: Field Survey, 2012

From the above table it is concluded that improper billing system is the important problem in the process of VAT collection which holds 27.56%. Similarly tedious work holds 12.44%, ranked 5.

From above table it is concluded problems are ranked here in this way:

1. Improper Billing system
2. Administrative Problem
3. Lack of knowledge
4. Lack of Skilled Manpower
5. Tedious Work

4.9.7 Views on most important factor for the effectiveness of VAT collection.

There are so many problems existing in the VAT collection system. To make it effective, it is necessary to identify the problems and then solve successfully. These problems may be effective and efficient administration, broad coverage, tax education, proper implementation of rules and regulations and clear VAT rules and regulations.

Table 4.16

Total NO. Of Effectiveness of VAT

Views on most important Factor for the Effectiveness of VAT				
Problems	No. of Respondent	Score	%	Rank
Effective & Efficient Administration	50	90	10	5
Broad Coverage	50	120	13.33	4
Tax Education	50	176	19.56	3
Implementation of Rules & Regulations	50	250	27.78	1
Clear VAT laws and Regulation	50	214	23.78	2
Others	50	50	5.56	6
Total	50	900		

Source: Field Survey, 2012

From the above table we can conclude that proper implementation of rules and regulation is the most important factor for effectiveness of VAT collection system. On the basis of result obtained from investigation it is concluded that factors for effectiveness of VAT collection system are ranked as:

1. Proper Implementation of Rules & Regulations
2. Clear VAT laws and Regulation
3. Tax Education
4. Broad Coverage
5. Effective & Efficient Administration
6. Others

4.9.8 Views on effectiveness of VAT in the future

An international experience shows that VAT is an appropriate method to achieve better revenue generation. Due to its advantage it should be effectiveness in the future. But it depends on its implementation .If implemented properly; it will be more effectiveness in the future. The views of respondents are presented in the following table:

Table 4.17

Total NO. Of Effectiveness of VAT in The Future

Effectiveness of VAT in the future							
Respondents	Yes		No		I DON'T KNOW		Total
	No.	%	No.	%	No.	%	
Administrators	16	80	2	10	2	10	20
VAT Collector	7	70	1	10	2	20	10
Tax Payers	12	60	3	15	5	25	20
Total	35	70	6	12	9	18	50

Source: Field Survey, 2012

From the above table, 70% of respondents agree that VAT will be more effective in the future, 12% respondents were negative about the effectiveness of VAT in the future and 18% were unknown about this question. From the survey we can conclude that most of the respondents view VAT will be more effective in the future. From the study it is found that 80% administrator, 70% VAT collectors and 60% tax payers accepted that the VAT will be more effective in the future. It is concluded that VAT will be more effective in the future.

4.9.9 Views on VAT collection system and Legal Provision in Nepal

There was a question on the questionnaire "Do you have any other suggestion for the VAT collection system and legal provision in Nepal? This was an open ended question. Most of the respondent answered the question. There were different suggestions from different respondent which are listed below:

- Improvement ethics of business holder.
- Proper implementation of billing system.
- No security for employee to implement the VAT law forcefully.
- Reduce tax rate and enlarge tax base.
- Avoid under valuation and improper billing system.
- Exempt are should be thinned.
- Boarder area should be tightened.

- Valuation should be real based.
- Billing enforcement should be effective.
- VAT laws and regulation should be clear and transparent.
- VAT administrator should be efficient and effective.
- Sound tax policy is necessary.
- It should be clear and efficient in all levels.

4.10 Major Findings of the Study

On the basis of presentation and analysis of data the major finding are as followings.

- From the study, it is found that revenue is increasing continuously. In the fiscal year 2003/004 revenue and expenditure were Rs. 6233.1 million and Rs. 8944.26 million respectively and deficit was Rs. 2711.16 million, which was low deficit. There was highest deficit in fiscal year 2008/009 i.e. Rs.9618.75 million and in FY 2010/11 deficit is Rs. 9554.47 million.
- Overview the current structure of Nepal, it is found that Total Revenue is increasing from the FY 2002/003 to 2010/2011, the share of Tax Revenue has been greater then Share of Non-Tax Revenue. The average ratio of Tax Revenue to Total Revenue is 83.83% and Non Tax Revenue to Total Revenue is 16.17%.
- During the study period, there has been simultaneous increase in Total Tax Revenue, Indirect Tax Revenue and Direct Tax Revenue. In FY 2002/003 the amount of total direct and indirect tax were Rs. 4089.60 million, Rs. 1088.19 million and Rs. 3001.41 million respectively. These amounts were increased to Rs. 8515.55 million, Rs. 2308.77 million and Rs. 6206.78 million respectively, In FY 2007/008. In the FY 2010/011 these amount were increased i.e. Rs. 17277.76 million, Rs. 4865.5 million and Rs.12412.26 million respectively.
- In developing country like Nepal, Indirect tax play vital role for resource mobilization, which is now the principle source of revenue collection? From the study period it is found that the average ratio of Indirect Tax Revenue to Total Tax Revenue is 73.03% and Direct Tax Revenue to Total Tax Revenue is 26.97%.
- From study, it is found that revenue collection from VAT is in increasing trend. In FY 2002/003 there is lesser amount of increase in VAT by 7.57%. There was the

highest revenue collection in FY 2010/011 i.e. Rs. 6166.36 million and Percentage increase in VAT is 12.27% but highest percentage change was in 2009/2010 i.e. 38.33%.

- During the study, it is found that the VAT revenue is increasing from FY 2002/003 up to FY 2010/011. But VAT in fluctuating trend and lowest contribution in FY 2002/004 i.e. 23.23% and highest contribution in FY 2008/009 i.e. 32.15% and Average VAT collection was Rs.3118.12 million i.e. 29.29%. There was increasing trend of VAT revenue to Total revenue. Throughout the study period, which is beneficial for sound economic development?
- During the study, it is found that the contribution of VAT to Total Revenue is not smooth; it is fluctuating from beginning to end of study i.e. from FY 2002/003 to 2010/011. Firstly it was decreased then increased. There was highest contribution of VAT to Total Tax Revenue in FY 2005/006 i.e. 37.62% and lowest in the FY 2003/004 of 30.05% (It is concluded that VAT revenue and Total Revenue are increasing trend during the study period) and average contribution of VAT to Total Revenue is 35%.
- During the study, it is found that the contribution of VAT to Total Indirect Tax Revenue is not smooth that is first it was decreased from FY 2002/003 to 2003/004 i.e. 44.84% to 39.93 % respectively. And there it was increased to the FY 2006/007 and then again it was decrease up to FY 2009/010 and increased at FY 2010/011 i.e. 49.67% which is good in comparison to FY 2002/003.The lowest contribution of VAT to Total Indirect Tax Revenue is 39.93% in FY 2003/004 and highest contribution of VAT to Total Indirect Tax Revenue is 50.04% in FY 2006/007. The average ratio of VAT to Total Indirect Tax Revenue is 47.85%.
- During the study, it is found that the share of VAT in GDP is 2.92% in FY 2002/003 decrease to 2.89% in FY 2003/004 and from FY 2004/005 up to FY 2009/010 seems too increased and in FY 2010/011 it is 4.94%. Form this analysis the highest % of VAT Revenue to GDP in FY 2009/010 i.e. 5.06% and lowest at FY 2003/004 i.e. 2.89%.

- The average ratio of VAT to Total Revenue is 29.29%, VAT to Total Tax Revenue is 35%, VAT to Total Indirect Tax Revenue is 47.85% and VAT to GDP is 4.13% during the study period.
- During the study, it is found that number of VAT Registration is increasing year by year i.e. high registration in FY 2009/010. (Data of 2010/011 is not available) i.e. 82433. That shows the increase in the number of VAT registration is impressive.
- The study is found that VAT is the appropriate means of raising the public revenue, though there are large numbers of tax payers who are not in favor, they are not well familiar to the phenomenon of VAT.
- The study is found that 90% of administrators and 80% of VAT collectors and 65% of Tax payer shows positive opinion on the superiority of VAT to the areas it has replaced.
- The study is found that the legal provisions relating to VAT collection system in Nepal are sufficient. There is only lack of proper implementation.
- In opinion survey the question was what degree of Liberace is used when VAT is collected? The views; 60% of administrators, 50% of VAT collectors and 75% of tax payers said that VAT is strictly collected where as 30% administrators, 20% of VAT collectors and 15% of tax payer said that medium, where as 10% of administrators, 30% of VAT collectors and 10% of tax payer said that the implementation of VAT collection system is low.
- In opinion survey 78% responded argue that revenue collection from VAT is not satisfactory as it has been expected.
- In opinion survey it is concluded that improper billing system is the important problem in the process of VAT collection which hold 27.56%. Similarly, tedious work hold 12.44%, ranked 5.
- In opinion survey it is concluded that proper implementation of rules and regulation is the most important factors for effectiveness of VAT collection system.

- In opinion survey it is concluded that 70% of responded agree the VAT will be more effective in the future day, 12% of responded were negative about the effectiveness of VAT in the future and 18% were unknown about this question.
- Last at opinion survey, there was a question on the questioners “Do you have any other suggestion for VAT collection system and legal provision on Nepal? This was an open ended question; Most of the Respondents answer the questions which are list below.
    - Stable / permanent government with similar commitment about national policy.
    - VAT collection system is made more flexible and tax payer friendly.
    - Sound tax policy is necessary.
    - VAT administration should be efficient and effective.
    - VAT law and regulation should be clear and transparent.
    - Boarder area should be tightened.
    - To create as environment in which invoice are issued properly, accounts are maintain accurately.
    - Computerized system in VAT collection should be maintained.
    - VAT awareness programmed or VAT training is given.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Summary

Value Added Tax is latest innovation in the field of taxation. Actually, VAT is considered as the most important tax reform in the 21st century, which has already been implemented popularly in more than over 130 countries in the world. From the study it is found that revenue is increasing continuously. In the fiscal year 2005/2006 revenue and expenditure were Rs. 7228.19 million and 11088.92 million respectively and deficit was3860.73 million. It means increasing rate of expenditure is greater then increasing rate of revenue. There was greater deficit in FY 2008/009 i.e. Rs. 9618.75 million. In FY 2010/011 deficit is Rs. 9554.47 million, which is comparatively lower then FY 2008/009. The average deficit is Rs. 5574.64 million.

It is concluded that expenditure and revenue are increasing year by year in increasing trend and deficit is also in increasing trend except year 2003/004 & 2009/010. From study it is found that total revenue is increasing from FY 2002/003 up to 2010/011. The share of tax revenue has been greater then share of non-tax revenue.

In the fiscal year 2002/003 to 2010/011 the tax revenue has increased. But in the fiscal year 2005/006 the non-tax revenue has decreased so, it is found that there is no relationship between tax revenue and non-tax revenue.

Total tax revenue is composed by direct tax and indirect tax. During the study period, there has been simultaneous increase in total tax revenue, Indirect tax and direct tax. In FY 2002/003 the amount of total tax revenue, direct tax revenue and indirect tax revenue were RS 4089.60 million, Rs 1088.19 million and Rs 3001.41 million respectively. These amounts were increased at FY 2010/011 i.e. Rs 17277.76 million, Rs 4865.5 million and Rs 12412.26 million respectively. The average total tax revenue, direct tax revenue and indirect tax revenue is Rs 8922.34 million, Rs 2406.97 million and Rs 6515.37 million respectively.

From the study it is found that revenue collection from VAT is in increasing trend i.e. in FY 2002/003 revenue from VAT is Rs 1345.97 million and in FY 2010/011 revenue from VAT is Rs 6166.36 million. There was highest percentage change in VAT is 38.33% in FY 2009/010 and lowest percentage change in FY 2002/003.

From study it is found that highest contribution of VAT to total revenue in FY 2008/009 i.e. 32.15% and lowest contribution in FY 2003/004 i.e.23.23%. The average VAT revenue, total revenue is Rs 3118.12 million and Rs 10642.75 million and average percentage of VAT is 29.29%. So, there was increasing trends of VAT revenue to total revenue.

From study it is found that contribution of VAT to total tax revenue is not smooth. It is fluctuating from year by year i.e. in FY 2002/003 is 30.60%, in FY 2005/006 37.62% and in FY 2010/011 is 35.68 and average percentage contribution of VAT to total tax revenue is 35%.

From the study it is found that the contribution of VAT to total indirect tax revenue is fluctuating i.e. in FY 2003/004 was 39.93% which is lowest and in FY 2006/007 was 50.04% which is highest and at year 2010/011 it is 49.67% and average percentage contribution of VAT to total indirect tax is 47.85%.

From the study it is found that the share of VAT in GDP is 2.92%, in FY 2002/003 decrease to 2.89%, in FY 2003/004 and from the FY 2004/005 up to FY 2009/010, it seems to increased and in FY 2010/011 it is 4.94%.The highest Percentage of VAT revenue to GDP n year 2009/010 i.e. 5.06% and lowest at year 2003/004 i.e. 2.89%. The average percentage of VAT revenue to GDP is 4.13%. The fluctuating trend in VAT in GDP is due to fluctuation in VAT Collection.

The VAT Registrant is number increasing year by year i.e. in 2007/008 is 59775 and increase to 82433 in FY 2009/010. It shows that the number of VAT registrants is increasing. It is favorable for revenue collection and better for the development of the country.

The answer of responded was positive in the subject of VAT, 70% of responded say that VAT is appropriate means of raising public revenue,78% of responded shows positives opinion on the superiority of VAT to the area of it has replaced, 52% of responded wear in favor of existing legal provision relating to VAT in Nepal, 64% of responded said that VAT is strictly collected, 22% of respondent say that VAT is greeting expected amount of revenue, 27.56% holds that important problem in the process of VAT collection is improper billing system, 27.78% holds that important factor for the effectiveness of VAT is implementation of rules and regulation, 70% of responded agree that VAT will be more effective in future days. At last for open end question most of the responded said that sound tax policy is need for VAT collection system.

5.2 Conclusion

VAT has developed as an advance form of sales tax and puts greater significance in revenue mobilization in Nepal. Generating revenue means collecting taxes. There are various forms of tax system in Nepal. The decision to introduced VAT seems to be best for the country. VAT collection process is the origin of indirect tax revenue. For the improvement of the economic condition of Nepal it has to be increased. To achieve higher growth of revenue, every country needs to reforms some of its tax system. In the context of present world VAT is one of the best alternatives of tax reform process. There were four taxes i.e. sales tax, hotel tax, entertainment tax and contract tax which is replaced by the VAT in Nepal. VAT is the most innovative, scientific and powerful tax system which eliminates various defects of sales tax by replacing it such as pyramiding and cascading effects. VAT is broad based indirect tax. Nepal has adopted consumption type tax with tax credit mechanism. From study it is concluded that the contribution of VAT to GDP is very low. There was a highest contribution in FY 2009/010 which is 5.06 % and lowest contribution was in the fiscal year 2003/004 which is 2.89 %.

Proper invoicing system is the major problem of VAT in Nepal. Under valuation is another problem. The main reason of weakness of VAT is the lack of publicity and effective monitoring. In the implementation of VAT the main glitch has been in terms of the lack of public awareness. Until a time when a situation is created where the consumer himself/herself is self motivated to task to ask for an invoice, it will be an uphill road for VAT.

In the process of preparation for VAT, the seminars, workshops, interactions were mainly organized for specific sectors. But unless and until the general consumers are directly made conscious and alert regarding this tax, the time to time random visits and investigation alone by the government authorities will not regularize the billing process.

There are lots of elements which increases the effectiveness of VAT. Clear VAT rules, effective and efficient administration, honest tax payer, tax education and establishment of proper invoicing mechanism and extension of tax coverage are most important factor which obviously increased the revenue. Government should publish tax related information regularly through Radio, Television, Magazines, Newspaper, journals etc., it also obviously increased the revenue collection from VAT.

5.3 Recommendations

Nepal has implemented VAT since 1997. VAT act, rules and regulations have been setup in the line of international standard. Since the implementation of VAT is a great jump from the traditional tax system to a modern one, several things are still lacking to be done for the successful implementation of VAT in Nepal. On the basis of analysis of data, findings and conclusion the following recommendations have been suggested to make VAT effective and more efficient.

- In the process of VAT collection system, the focus should be on transparency, fairness and timely & quality production in administration instead of simple collection of tax.
- Non tax revenue is very low as compared to tax revenue. For the betterment of the nation it should be increased through implementation of legal procedure & consumer awareness.
- It will be better to increase to make government surplus through collection of tax revenue very effectively & bringing taxpayers to tax net through implementation of tax act and tax law.
- For the economic development of nation the gap between the direct tax and indirect tax should be decreased down with collection of direct tax through imposition progressive income tax in the country.
- Tax refund procedure should be made simple and less time consuming through establishment of different tax payers services centers and mobile services in different market areas and programmer that can aware, conscious the tax payers should be implemented such as training programme and effective computer billing system regularly.
- The manufacture should quote the price of the product as inclusive of VAT rather than exclusive of VAT.

- All the registrants should be well known to the process of registration by which they can maintain the records and accounts as per the legal provision of VAT collection system and ultimately revenue from VAT will be increased through timely payment.
- It is recommended to have separated legal provision in VAT laws to avoid the situation of taxation and tax exempted goods double tax system.
- VAT rate should be different for different type of products through multiple VAT rate. High rate should be imposed on luxurious goods and low rate for basic goods to make the VAT system broad.
- It will be better if special incentives should be provided to small business person to increase registration trend and it will be better to increased threshold amount.
- It is recommended to have open border inorder to effectively control illegal trade.
- Most of the national economic activities are dependent upon agriculture and large portion of GDP originating from agricultural sector remains out of tax net thus VAT should be levied on agriculture.
- To establish VAT invoice in the forms of a campaign, college students could be hired and mobilized. It would be appropriate to mobilize such students to find out the status and presence of VAT in the market. If group of students are placed in busy market place, it creates psychological pressure on the vendors to issue invoice. Similarly, they could e also used to collect information on various issue of VAT.
- The person who honestly takes the responsibilities should be rewarded by means of promotion and enhance the effectiveness of VAT.
- Government should publish tax related information regularly through Radio, Television, Magazines, Newspaper, journals etc.

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Appendix-1
Questionnaires

Dear Sir/Madam

I would like to introduce myself as a student of Central Department of Management, MBS Final Year, engaged in a research work. In order to fulfill the partial requirement of Master's Degree in Business Studies (MBS) of Tribhuvan University of Nepal, I am going to prepare a dissertation on VAT.

I humbly request for your valuable comments, views, suggestions and information on this issue which could prove very useful for my study, so I request you to fill up the following questionnaire. Please tick (√) the answer of your choice or wherever appropriate put in order of preference form 1 to last number on the basis of alternatives.

I assure that the information you provide me will solely be utilized in research work. I hope for kind co-operation and support with many thanks as soon as possible.

Nirmal Lamichhane

Questionnaire

Name of the Respondent :

Office/ Organization :

Designation :

Occupation :

Please tick the best answer of your choice

1. **How do you know about VAT?**

   a. Media ( ) c. Personal Communication ( )

   b. Lectures/ Seminar ( ) d. Other, please specify ( )

2. **Do you think the VAT collection system practiced now in appropriate mean of raising the public revenue?**

   a. Yes ( ) b. No ( )

3. **Is VAT more appropriate/ superior to the areas it has replaced (such as sales tax, hotel tax, entertainment tax and contract tax?**

   a. Yes ( ) b. No ( )

4. **Among the various taxation methods which one is practiced now?**

   a. Addition ( ) c. Tax Credit ( )

   b. Subtraction ( )

5. **Do you think legal provision concerning to VAT collection system are sufficient?**

   a. Yes ( ) b. No ( )

6. **What degree of liberate is used when VAT is collected?**

   a. Strict ( ) c. Low ( )

   b. Medium ( )

7. **Do you think that the revenue collection from VAT is satisfactory as it has been expected?**

a. Yes ( ) b. No ( )

8. What kind of problems has arisen in the process of VAT collection in Nepal?

a. Lack of knowledge about VAT to the tax payers
b. Tedious work
c. Lack of skilled manpower/ administer
d. Improper billing system
e. Others please specify ………

9. What is the most important factor for the effectiveness of VAT collection?

a. Effective and efficient administration
b. Broad coverage
c. Tax education
d. Proper implementation of rules and regulation
e. Clear VAT laws and regulations
f. Others please specify ………

10. What are the major problems of VAT in Nepal? (Please rank)

a. Lack of skilled manpower/ administrator
b. Smuggling and under valuation
c. Improper billing system
d. Tax unconsciousness of people.
e. Tax evasion
f. Others please specify …………

11. Do you think that VAT will be more effective in the future?

a. Yes ( ) b. No ( ) c. I don't know ( )

12. Do you have any other suggestion for the VAT collection system and legal provision in Nepal? If yes, please specify?

a. Effective and efficient administration
b. Broad coverage
c. Tax Education
d. Proper implementation of rules and regulation
e. Clear VAT laws and regulations
f. Others please specify ……