

# CHAPTER - I

## INTRODUCTION

### 1.1 Background

The power to tax is an inherent sovereign power of state to collect contribution of money or other property from its citizens and the inhabitants of its territory for defraying general expenditure (Parameswar, 1987). Its strategy position in the modern welfare state is such that without it no government can adequately discharge its manifold duties. Its constitutional significance requires legitimate popular sanction for its collection.

As Kautilya says "the launching of all programs depends first and foremost on the treasury", so every state needs resources. Whether to pay salary to the government employees or to do the development works, it needs huge amount of revenue.

The government collects revenue from different sources like grants, administration incomes, business incomes, and taxation. Grant means the amount given one to another. The administrative income denotes the amount charged by government for providing administration service. Business incomes mean the return received by the government for the government for providing various goods and services to the people. All these revenue are called as non tax revenues. In Nepal around 20 percent revenue collects from these sources (Kandel, 2011).

Another source of government revenues is the taxation. Customs, excise, value added tax, corporate and personal income tax are the examples of the sources of tax revenues. Nepal collects around 80 percent of the revenue from different taxes.

Tax is a compulsory levy on those who have to pay it without getting corresponding benefit and services or goods from the government. Tax is a liability to pay an amount to the state. The basis for the payment is that the assesses have income of minimum amount from certain specified sources. The tax system should be helpful in income redistribution of economic stability.

There are two kinds of tax one is direct tax and other is indirect tax. Value added tax is the one kind of indirect tax. VAT is developed from sales tax. It is an improved and modified form of sales tax. It is levied on value added of goods and services at each stage in the process of production and distribution chain. This stage can be import, manufacturing, wholesales and retail. Value added for a firm is sales value minus all expenditures on goods and services purchased from other firms. The value added can be obtained by adding payments to factors of production (wages, salaries, rent, interest and profit). This value added is the base of VAT. Although VAT is eventually borne by the final consumer, it is collected at each stage of production and distribution chain.

### **Direct and Indirect Tax**

#### **Direct Tax**

A direct tax is a form of tax paid by a person on whom it is legally imposed. It is collected directly by the government from the person who bears the tax burden. Tax payers need to file tax returns directly to the government. Therefore, direct tax cannot be shifted. The impact or the money burden and the incidence are on the one and the same person. In other words, the same property. Examples include income tax, property tax, vehicle tax, interest tax, expenditure tax, death tax, gift tax etc.

In the word of Dalton "A direct tax is really paid by the same person on whom it is legally imposed" (Kandel, 2011). The characteristics of direct tax are equitable as per the property or income certainty as per the process of payment, amount to be paid, time of payment, elastic in nature.

#### **Indirect Tax**

An indirect tax is a form of tax imposed on one person but partly or wholly paid by another. It is collected by mediators who transfer the taxes to the government and also perform functions associated with filing tax returns. Hence, indirect tax can be shifted. Indirect tax, the impact and incidence of tax are on different person. In other words, the person paying and bearing the tax is different. It is the tax on consumption or expenditures, Examples include Vat, excise duty, import and export duty etc.

In the word of Dalton" An indirect tax is imposed on one person but paid partly or wholly by another" (Kandel, 2011). The main features of indirect tax are convenience to pay mass participation, limited evasion, shifting of incidence; the consumer pays the tax to the businessman not to the government. The examples of indirect taxes are customs, excise, VAT, contract tax and so on.

The Value Added Tax (VAT) is the most choice and ingredient of tax reform. The tax reform and adoption of VAT is therefore, essentially connected with the efforts of many under developing countries (UDCs) to achieve the goal of the country's economic development. Since the VAT is one of the components of indirect tax, developed in the past, is probably the best tax, which had gained prominence on such a short period of time. A VAT may be adopted by developing countries with some additional efforts and sincerity. A VAT is an important instrument for the mobilization of internal resources. The pressure of VAT on economic activities is minimal or not at all since VAT is an indirect tax and no one can deny the importance of its in developing country like Nepal. Indirect tax is the major sources of tax revenue in Nepal. It covers about 80% of tax revenue. Major of indirect taxes are custom duty, sales tax and excise duty. Custom duty is followed by sales tax (now it is called VAT) in case of continuing in direct tax revenue. The tax reform and adoption of a tax is therefore, essentially connected with the efforts of many UDCs to achieve the goal of country's economic development.

### **Characteristics of a Full-fledged VAT System**

1. It is an indirect tax.
2. It is based on added value.
3. It is a broad based tax.
4. It is based on self-assessment system.
5. It avoids cascading and pyramiding.
6. It has the self policing and catching up benefit.

VAT is most important tax innovation on the second half of the twentieth century. VAT is a scientific tax system, which was first introduced in 1954 in France. VAT has been spreading all over the world since late 1960s and now this tax has become

one of the mainstays of the tax system in over the world covering 120 countries (Bhattarai, 2005).

Nepal introduced VAT in November 1997. However, the concept of this tax in Nepal was introduced in early years of 1990s. Nepal included the concept of introductory VAT in its 8<sup>th</sup> plan, Finance Act, 1992 and 1999, introduced two-tier sales tax, to make the base of implementing VAT. VAT task force was formulated in 1993, in technical assistance of USAID, which suggested the steps to be followed while implementing the VAT in Nepal. In Nepal, VAT was brought to replace sales tax, contract tax, Hotel tax, and entertainment tax.

Value Added Tax is a tax imposed on the Value Added in each economic activity from production to consumption. It means VAT is charged to value addition each stage. Ultimate resting place of this tax is final consumption so that consumers are the sole taxpayers of the VAT. Business people only collected the VAT as a mediator so that they don't bear its burden.

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 difference between the sales proceeds and the cost of the materials etc. that has purchased from other firms. VAT has eliminated the uneven impact of the turnover tax and manufactures and wholesalers sales taxes. A comprehensive consumption type of VAT is equivalent to a retail sales tax in its pure form expect that the later does not offer an option between the destination principle and the origin principle. VAT differently studies in closed and open economy as follows (Shoup 1969).

In conclusion, VAT should be the most essential for most developing countries as an ingredient of their tax reforms because it is the most improved form of sales tax and revenue enhancement and economic efficiency. It is an important instrument for the mobilization of internal resources. There is tremendous scope for increasing the revenue from VAT. The implementation of VAT will

Nepal's position in term of GNP per capita is the lowest in the SAARC region. Still remains 12th position from the bottom in the world hardly reaching US \$ 300 per year according to WDR 2005. This shows Nepal remains one of the poorest countries in

the world. Despite more than four decades of planned obviously increase its contribution in coming days. Thus, the tax reform and adoption of a VAT is therefore, essentially connected with the efforts of many UDCs as one of the major elements of tax revenue to achieve the goal of country's economic development.

## **1.2 Statement of the Problem**

Development the Nepalese economy is persistently suffering from general poverty and stagnation. The low income leads Nepalese people under the vicious circle of poverty. The percentage of population having per day income or purchasing power parity below one dollar is 37.7, the worst position in Asia. The average growth of GDP during (2001-2010) is 4.9 percent. The low income people in Nepal are suffering from economic humiliation. They are suffering today from several economic and social disturbances in the country. Unfortunately, problem being solved are rather deepening and worsening.

However, all of these sources are economically undesirable in the long run as they create the macro economic problems. Foreign loan leads the economy into the debt trap while printing of money is inflationary by nature. Domestic borrowing raises the domestic rate structure, which eventually may crowd out private sector investment. The excessive use of foreign exchange reserve may create a balance of payment as well as exchange rate crisis. However, developing countries need to launch several developmental activities. So increasing trend of government expenditure may be taken as general phenomena. While adjusting the fiscal policy, it is necessary to increase government revenue rather than reducing the investment to the resource gap. So the ultimate and the best measure to fill up the resource gap is increase the public revenue through the effective tax system. Tax effort ratio is still extremely low in Nepal. Further Nepalese tax system is massively dominated by the custom duties. In such circumstances Nepal has already been adopted VAT since 1997 as a major step of reforming tax system for the purpose of strengthening internal resource mobilization.

Value Added Tax is an important source of the revenue. In Nepal, VAT has been facing many controversies especially in the practical implementation and how it

contributes in taxation. GNP ratio is the lowest among the rest of the world. Therefore, this topic has been selected, due to the following conditions.

- a. The role of VAT in Tax.
- b. Still there is controversy in its operation.
- c. Sufficient academic researches have not been conducted and have not been established rationalities.
- d. Administrative difficulties from the concern office.
- e. Amount of VAT collection has not been achieved as its projection.

### **1.2.1 Research Questions**

In the view of discussion of the Problem, the research question is as follow:

- a. What are the problems regarding VAT implementation in Nepal?
- b. Is the VAT management system of Nepal effective?
- c. What is the future prospect of VAT in Nepal?
- d. In what extent does VAT contribution revenue to government in Nepal?

### **1.3 Objectives of the Study**

This study has focused on the analysis of VAT in tax revenue in Nepal. The basic objectives of this study are as follows:-

1. To examine the role of VAT in the tax structure of Nepal.
2. To analyze the reasons for under collection of VAT irrespective of the emphasis given by government.
3. To give suggestions for the improvement of VAT implementation in Nepal.

### **1.4 Significance of the Study**

VAT is the most popular indirect tax to collect the revenue for the countries. Evidence shows that VAT was used in most of the countries in short time. It's history was not long but in short period of time VAT gained popularity. In the world more than 130 countries have adopted the system, which include developed countries, developing countries, and least developing countries. VAT collection procedure is most favorable so all countries were successful in the process. The result is favorable to increase the

revenue of the countries. In Nepal, VAT is most popular in short time. It is contributing a lot in raising the National Revenue. An attempt has been made to generate information. In this study, what is the role of the VAT in tax structure and how it contributes to the national economy? That is why the study is most significant in the present context. The policy makers, businessman, researchers, and other people to private sector as well as public sectors will be benefited from this study.

### **1.5 Limitation of the Study**

- a. The study is based on the secondary data of nine years from FY 2001/02 to 2009/10.
- b. The data needs for the study have also collected from primary sources.
- c. The sample size has been selected only from Kathmandu valley due to time limitation and resource constraint.
- d. Simple statistical tools are used for data analysis.

### **1.6 Organization of the Study**

This study has been organized in to five chapters. They are as follows:

#### **Chapter One: Introduction**

This is the introduction Chapter. It includes general background, statement of problem, objective of the study, scope, Significance and limitation of the study.

#### **Chapter Two: Review of literature**

This chapter is about the Review of literature through available and published books, reports, articles and dissertation. Legal provision regarding Introduction to VAT. It includes conceptual framework and review of previous studies.

#### **Chapter Three: Research Methodology**

This chapter is on Research Methodology, which includes types of Research, Research Design, population and sample, nature and sources of Data, Data collection Procedure, Data processing and Analysis.

#### **Chapter Four: Presentation and Analysis of Data**

This fourth chapter deals with analysis and Presentation of data, Operation of the VAT, VAT structure & Implementation, Tax GDP Ratio, VAT Implementation Analysis, Nepalese tax structure, contribution of income tax to GDP, Empirical Findings and Major Findings of the Study.

#### **Chapter Five: Summary, Conclusion and Recommendation**

The last chapter states the finding summary, conclusion of the whole study and recommendations have been made respectively. It also offers several avenues for future research.

Bibliography and appendix also are incorporated at the end of the study.



## **CAPTER-II**

### **REVIEW OF LITERATURE**

Several studies in the field of VAT have been already carried out by the researchers, learners, students and other for different purposes, in the books, booklets, magazines as well as dissertations. Thus, before entering to the actual analysis tools and data presentation, related literatures were reviewed thoroughly. Therefore, this chapter includes the review of underlying literature from textbooks, related books, journals and previous researches.

#### **2.1 Theoretical Review**

##### **2.1.1 Introduction to VAT**

###### **Origin and Development**

Historically, the VAT has emerged as an alternative to defective multi-stage turnover tax or cascading types of sales tax. VAT was introduced as an attempt to improve the existing shortcomings of the sales tax.

First of all, a German economist Dr. Wilhelm von Siemens introduced VAT as improved turnover tax for Germany, in 1919. It was advance over existing turnover tax by employing the concept of subtraction of previous outlays from taxable sales. Similarly, Prof Thomas A. Adams recommended VAT for the United States of America in 1921.He recommended the sales tax with a credit or refund system to replace the existing corporate income tax.

Further, the same tax system was developed in 1949 by a tax mission to Japan led by Prof Carl.S. Shoup for the purpose of reconstructing the Japanese economy by avoiding the existing defects of the turnover taxes. Although the proposals suggestions and recommendations were not came into practice but gradually raising the interest so for the implementations of VAT. Thus the concept of VAT was remained a subject for academic discussion till 1953.

France becomes the pioneer country in the history of taxation by adopting VAT in 1954, replaced the France production taxes. This move of France becomes the first

step in the field of VAT implementation. Maurice Laure, an officer in the Ministry of Finance in France designed the VAT for France. Up to 1968, it has covered the industrial sector and wholesale level only. Ivory Coast, French colonial country, followed the France by adopting VAT in 1960. Senegal also implemented VAT since 1961. VAT was limited to import and manufacturing stage only in both the countries.

Since the 1960's VAT became a popular subject matter of taxation in many countries. This fiscal and financial committee of European union (then EEC) recommended all European common market to shift VAT to replacing their existing turnover taxes in 1962 and it was recognized by EU council of ministers. In 1968, France extended VAT from wholesale level to retail level. In the same front, Federal Republic of Germany introduced VAT in its tax system in 1969, Netherlands and Sweden in 1970, Belgium in 1971, Ireland in 1972, Italy and United Kingdom in 1973, Portugal and Spain in 1986 also introduced this tax. In the same way, Greece adopted VAT in 1987 and Finland in 1994. Besides EU countries, many other countries of north and South America, Africa and oceanic as well as Asia gradually adopted a newly improved tax in their respective countries. This trend of adopting VAT shows that this system became a very popular in the world at a short period.

Vietnam became the first country in Asian region to adopt VAT in 1973. Soon after the implementation it was abolished and again reintroduced in 1999, other Asian countries adopting VAT are South Korea in 1977, China 1984, Japan in 1989, Thailand in 1992, Singapore in 1994 and Mongolia in 1998.

In SAARC region, Pakistan is the first country adopting VAT. It introduced VAT in 1990. India implemented MOD-VAT (modified value added tax) in place of VAT 1986. Bangladesh adopted in 1992 and Sri Lanka in 1995 respectively, and India has shown its in-depth willingness to expand the MOD- VAT into VAT in different stages and sectors. A lot of preparation has been also been made. A deadline for the adoption of VAT in different states has been announced frequently but due to federal system and lack of cross state arrangements it couldn't be materialized. But besides these difficulties now full VAT has been implemented in India with effect from 1<sup>st</sup> April 2003.

Nepal has adopted VAT since 16 November 1997(1 Mangsir, 2054 B.S.). However the first intention of Nepal towards VAT could be found since the Eight Five year plan (1992-1997) but the government finally expressed its commitment to introduce VAT in April 1997. Finance Act, 1992 and 1994 introduced two tier sales tax to make the base of implementing VAT. VAT task force was formulated in 1993, in technical assistance the VAT in Nepal. It drafted the VAT law as well. High level tax system Review task force headed by Prof. Madan Dahal suggested implementing VAT in 1995. VAT related act and rules were enacted in 1995 and 1996 respectively. In Nepal, VAT was brought to replace sales tax, contract tax, hotel tax and entertainment tax.

Because of broad base and more revenue productive, more than 120 countries have been adopted VAT system. Many rich and poor countries, developed and developing countries, small and big countries, socialist and capitalist countries have been adopted VAT in the world.

VAT is a new tax system for Nepal. VAT has been justified in the light of government fiscal imbalances and need for extra revenue mobilization through an efficient tax system. The Government of Nepal has increased VAT to 13 percent with effect from Magh 1, 2061.

### **2.1.2 Concept of VAT**

VAT is a sales tax in advanced form. It is imposed on different stages. It is imposed on added value of good and services. Value added tax is one of the forms of indirect taxes too. Encyclopedia of taxation and tax policy says:

“Value added tax is a broad based tax on business designed to measure net value generated in a country”. Being a broad based tax, it is imposed on producer, wholesaler, retailer and consumers also. It is related to both the goods and services. It is levied on industry as well as commerce. Accordingly, it measures net value generated in a country, i.e. GDP. India Tax Institute defines 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 a tax system that aims to minimize tax evasion and increase resource mobilization. It is imposed on value added amount in each stage and therefore, is equivalent to multistage sales tax. In contrast to sales tax, VAT is imposed on added value of

production and distribution. The value is added in the form of profit, rent, wages, salary etc. (Kandel, 2011).

### **2.1.3 Methods of Calculation of VAT**

VAT can be computed with the following methods:

#### **(I) Additional Method**

This method is that where tax liability is calculated by adding the incomes. These incomes may include interest, profit, rent, wages etc. This method is appropriate for the income type of VAT that includes in its base.

#### **(II) Subtraction Method**

In this method calculated VAT liability by subtracting the cost of materials from sales proceeds. Thus, the VAT is levied on the amount which is divided by subtracting purchases from sales. This method is appropriate for the consumption variant of VAT.

#### **(III) Tax Credit Method**

This method is known as invoice method. In this method, value added is never calculated to get VAT payable. Under tax credit or invoice method, the liability is derived by deducting tax paid by the seller in purchasing from the amount of the collected from sales.

Calculation of VAT payable in three methods may be expressed as follows:

Additional method:  $T = F$  (wages+rent+interest+profit)

Subtraction method:  $T = F$  (outputs-inputs)

Tax credit method:  $T = F$  (outputs) - F (inputs)

**Table: 2.1**

**Different Methods of Calculating the VAT Liability**

**A. Addition Method**

(Assumed VAT rate 13%)

S. No		Stages of manufacture	Production & wholesaler	Distribution	Total (Rs)
1	Wages(a)	900	200	350	1450
2	Rent (b)	200	200	200	600
3	Interest(c)	100	50	-	150
4	Profit(d)	100	150	50	300
5	Value added(a+b+c+d)=e	1300	600	600	2500
6	VAT liability(13% of e)	169	78	78	325

Source: - Arbitrarily Estimated Figures

**B. Subtraction Method.**

(Assumed VAT rate 13%)

S. No		Stage of manufacture	Production & wholesaler	Distribution	Total (Rs)
1	Sales(a)	3500	3600	3800	10900
2	Purchases(b)	2200	3000	3200	8400
3	Value added (a-b)= c	1300	600	600	2500
4	VAT liability (13% of c)	169	78	78	325

Source: - Arbitrarily Estimated Figures

**C. Tax Credit Method.**

(Assumed VAT rate 13%)

S. No		Stage of manufacture	Production & wholesaler	Distribution	Total (Rs)
1	Sales(a)	3500	3600	3800	10900
2	Tax on sales(gross tax) (b)	455	468	494	1417
3	Purchase (c)	2200	3000	3200	8400
4	Tax purchases (d)	286	390	416	1092
5	Net VAT liability (b-d)	169	78	78	325

Source: - Arbitrarily Estimated Figures

Among of those three methods, the credit method is of universal use. It is an original EC model, which is adopted as a method of tax. All the countries in the world, the following table can give more idea about the calculation of VAT liability using tax credit method.

**Table: 2.2****Calculation of VAT liability using Tax credit Method**

Activities:	Cost price exclusive of VAT	Added value profit	Selling price exclusive VAT	VAT @ 13%	Selling price including VAT	VAT payable to Govt level
Imported goods	32180.21	-	-	4183.43	-	4183.43
Importer to manufacture	32180.21	3218.02	35398.23	4601.77	40000	418.34
Manufacture to wholesaler	35398.23	3539.82	38938.05	5061.95	44000	460.18

Let each of these sellers made on profit of 10% on Cost.

Source: - (Bhattarai, 2005).

#### **2.1.4 The Basis for VAT**

The basis for VAT is the value addition that takes place at each level in the production and distribution process of goods and services. For example, if a wholesaler purchases something from a producer at Rs 100 and sells to retailer at Rs 130 then value addition at the wholesaler level is Rs 30 and it is on this amount that VAT is levied since VAT is levied at rate of 13 percent the VAT amount will be Rs 3.9 on Rs 30 (Khadka, 2002).

#### **2.1.5 Freeing from VAT**

Some goods and services are left from the scope of VAT or they aren't taxed. Freeing from VAT may be justified for three reasons:

1. Administrative reason: Taxing some goods and services is administratively very difficult.
2. Economic reason: Taxing some goods and services may reduce the production and consumption.
3. Equity reason: Taxing some goods and services make the tax system much inequitable.

For the tax system stated above certain goods and services necessary must be free from VAT. There are two general methods for freeing from VAT exemption and zero rating.

#### **2.1.6 An Outline of Nepalese VAT System**

##### **A. Tax Exemption**

The supply where the VAT isn't imposed is exempt is exempt supply. This is not taken into account in determining whether a trader is a taxable person or not. According to act, input tax attributable to it is not normally available for credit. The example of goods and services which are tax exempt are Basic Agricultural product, Goods of basic needs like water, fuel salt etc. (Kandel 2011).

The exemption may be granted only for a single stage to small firms is that stage as means of reducing administrative cost relative to revenue. Exemption of the final product may be intended not as a completed exemption but only as an exemption of value added to that particular product at that final stage. The tax credit can be restricted accordingly. Such a product.

### **B. Zero Rating**

The zero rate is a tax rate of nil. Zero rate is equivalent to complete exemption. The zero rate is applied to supplied for export. Although no tax is charged on a supply taxed at the zero rate. It is taken as taxable supply. The input tax paid on it is available for credit it is opposite of exempt supply because the tax paid on input in case of exemption is not credited. Zero rating is granted for particularly goods.

### **C. Basic Features**

Nepal has adopted a modern and popular types of VAT already spread all over the world. It has some special features .They are:

- ⇒ The adoptions of consumption type VAT.
- ⇒ The computation of VAT through tax credit method.
- ⇒ The principle of destination.
- ⇒ The provision of exemption and zero rated goods and services.
- ⇒ The application of VAT to all business turnover through the rental stages.
- ⇒ The allowance of tax credit for taxable suppliers including the zero rated supply.
- ⇒ The facility of tax refund.
- ⇒ The use of single positive rate of 13 percent.
- ⇒ The threshold amount has been fixed on monthly basis also. The shops doing the transaction of more than Rs 200,000 per month through its annual transaction is less than Rs 2000,000 should register its business.



⇒ Extensive and excellent information about the new tax provided to the public and business firms.

#### **D. Tax Rates**

The standard rate of VAT is determined by Finance Act of each year. Right now, this rate is 13 percent based on the tax exclusive value of the goods or services supplied.

#### **E. Threshold**

Small suppliers having transactions of up to certain limit aren't required to register. The amount determined for that purpose is known as threshold. The main objective of threshold is to make easy to tax administrator to administer and to make easy to small supplier in doing his business. The threshold amount varies from country to country and time to time. It depends on number of factors like revenue requirement, administrative capacity, status of the recording system in the economy etc. In our country Nepal, the present threshold level is Rs 20 lacks for one year or Rs 2 lacks per month.

Similarly, importers who have commercial import of less than Rs 2 lacks annually or less than 10000 at one time aren't required to register.

#### **F. Tax credit**

This method is also known as the invoice method. Under this method tax is levied on the total value of sales and taxpayers are permitted to deduct from their gross tax liability the taxes already paid by their supplier and passed on to them. Thus in contrast to the subtraction method, which deducts purchases from sales and levies taxes on the difference, tax on purchases is subtracted from the tax on sales under the tax credit method (Value Added Tax Act 1995)

The credit method is almost universally preferred at least for the comprehensive VAT. In fact, it is clearly a necessity if multiple rates are used. A firm pays based upon its sale value and claims a deduction for the VAT paid upon its supplies of goods and services. In this case the tax paid on inputs, serves as an important record and not the specific value of purchases. This tax is then credited against taxes due to the sales made by the enterprises.

## **G. Tax Refund**

Under the Nepalese VAT system, there is a provision for the refund of VAT. Such situations generally arise in the case of zero rated supplies such as export business. A VAT registrant can deduct the tax paid (input tax) in relation to his /her taxable transaction from the tax collected (out put tax) from his / her sales and if the tax paid on purchases exceeds the tax collected from sales, he /she can adjust the difference amount in the tax to be paid in the following month. If the credit cannot be adjusted for 6 consecutive months, there is provision to get refund of exceeded amount. But an exporter can get an immediate refund of the tax paid on purchases. The tax administration has adopted a policy to provide refund within 30days of the receipt of the refund claim although the time limit fixed under the law is 60days. There is also provision to refund the tax paid on goods purchased by diplomats and international organizational. Organizations and on goods brought by projects run under bilateral or multilateral agreements (Khadka, 2002).

### **2.1.7 Principle of VAT**

The principles for levying VAT are:

#### **a. Original principle**

Under this principle, goods and services produced in a country are taxed at the place where they are produced or rendered. It implies that all exports are taxable and all imports are non-taxable. Where there is boarder and cross-country trade this principle gives preference to imported goods and services over domestic production. Countries with international boundaries prefer not to have this principle while taxing however, in European community where there is common boarder, this principle of taxation is gaining advantages. One major consideration is not following this principle is of revenue loss. Thus this principle affects balance of payment of the country negatively specially for those who have a poor performance in the world economy.

#### **b. Destination principle**

Under this principle, goods and services are not taxed at the place where they are produced or rendered but taxed at the place where they are consumed. Alternatively,

all imports are not taxed. The main benefit arising out of this is non discrimination between imported goods and internal production. This is the most popular form of principle adopted by a large number of countries. Thus this principle gives support for export. By following this principle of VAT many countries of the world are encouraging export. The equal treatment provided for both imports and domestic production fulfills the criterion of tax being neutral.

In conclusion, destination principle is more appropriate, for a country having consumption type VAT with the tax credit method. Special benefit by destination principle can be attained by those countries who have open boarder and cross- country trade and less competent in the open market.

#### **2.1.8. Reason for VAT's growing attraction in the world:-**

- ⇒ VAT is based on the most modern theories.
- ⇒ It is more informative.
- ⇒ It raises considerable revenue and sustains it.
- ⇒ Increment of tax payers are also advanced in it.
- ⇒ It is less tedious.
- ⇒ It is free from cascading effect due to the input tax credit.
- ⇒ It is effective to control price raise and reduce tax evasion due to its catch up effect.

#### **2.2 Review of Related Studies**

**Shoup (1969)**, in an article made an attempt to analyze the structure of the VAT and different policy issues relating to developing countries. A VAT covering all economic activities from the earlier stage of farming or mining right through the retail level is considered comprehensive consumption is superior. VAT is more revenue productive and serves self enforcing feature, and its regressively can reduced by providing zero rated for food and basic essentials. VAT will have favorable effect and it is relatively easy to administrative. But it is inflationary because firms through increase in price

must recoup it. In comparison with turnover tax and retail sales tax, VAT stand in first position but it requires caution in implementation. Although, the choice between turnover tax and VAT becomes a matter of weighing the pros and cons. Basic accounting and efficient tax administration are lacking in developing countries, which create difficulty for the successful implementation of VAT in such countries.

**Hsiung (1991)** had conducted a study to evaluate the VAT in Taiwan which was in effect since 1986. The study showed the goods result of VAT after some years of experiences. The impact of VAT showed the business tax revenue increased considerably due to cross checking procedures of VAT. Adoption of VAT did not cause price fluctuation.

**Choi (1993)** analysis and evaluates the VAT experience in Korea through his paper “Value added tax in introduction to effect on the economy” VAT in the republic of Korea was introduced in 1977 as a major step of tax reform with the objectives of simplifying tax structure and its administration, promoting exports and exports and capital formation. Besides these, introduction of VAT was also supported by the expectation of higher revenue productivity and maintaining neutrality in the indirect tax system. A single rate of VAT 10 % was used since the introduction of VAT and general characteristics remained same as the VAT adopted by the European countries, Korean VAT was the consumption type covering all the stages of production and distribution and the tax credit method was used for computation. Experience showed good symptoms for the prospects of VAT, as the effects of than the expectation made by either VAT supporter or opponents. VAT showed a good impact on investment and encouraged exporters as compared to the previous tax system, and there were no major impacts on the increase as well.

This study concludes that Korean VAT has worked relatively well and in some cases must better than its designers and taxpayers had anticipate. As compared to the previous taxes VAT has broadened the tax base, reduced evasion, increased revenue and eliminated many problems that were in existence. Further, Korean experience provide proper lessons for other country to tackle with the problems and issues relating to VAT implementation including coverage, rate structure, administration, special taxpayers coordination with direct taxation etc.

**Due and Friedlander (1981)** in their famous book, Government Finance evaluates the VAT that in avoiding the adverse consequences of turnover tax and greater revenue raiser a proper cross audit is possible of the VAT. Researcher accepted that “the administrative complexity” is the main visualized problem of VAT in developing countries. However they conclude that, it is undoubtedly the ideal form of sale tax in many countries.

A report prepared by a high level task force headed by Dahal (1995) reviewed Nepalese tax system and made some recommendations for a VAT in Nepal. It has mainly analyzed the magnitude of Nepal’s tax system and emphasized due to the following reasons:

- ⇒ It broadens the tax base and hence increases the tax revenue
- ⇒ It is more transparent, elastic and prevents tax evasion
- ⇒ It promotes exports
- ⇒ It makes tax system more efficient.

Some basic factors to be considered seriously before implementing VAT are:

- ⇒ Price level
- ⇒ Equity
- ⇒ Small traders

More focus is given for necessary preparation to be undertaken before implementing VAT and a functional organizational pattern is recommended in the report.

In Nepalese context, the following things include the process of VAT implementation.

- ⇒ Choice of the type of VAT and computation method
- ⇒ Determination of structure , exemption and threshold
- ⇒ Providing basic information to the public
- ⇒ Developing more efficient and proper tax administration
- ⇒ Analysis about the possible effects on different sectors

In conclusion report recommended VAT as the best alternate to eliminate the existing weakness of the tax system

**Khadka (1998)** in his books entitled “VAT in Nepal” has described the theoretical background and the development of VAT in Nepal. Being a researcher and a VAT advisor, he has spent a lot of time in preparatory work in VAT and has played a significant role in formulation of tax policy.

**Bista (1999)** in his research has concluded “VAT is applicable and feasible in Nepal” he has focused the need of VAT for Nepal for several reasons: transparency and avoiding all tax loopholes, VAT helps to the resource gap by broadening tax base and mobilizing additional resource by controlling tax leakage, smuggling, unofficial trade and corruption through trade and corruption through transparency and account based cross checking. Positive and favorable effects of VAT on all sectors can be alliance. Only if government can operates the VAT administration with effectively and efficiently. The public awareness level relating VAT and effective administration are essential perquisite in the additional resources and the rest of the internal resources by boarding the tax base by checking the existing tax loopholes and it ultimately affects the major macro variables positively which accelerates the economic growth. Income inequality, which is one of the major problems of Nepal, can be reduced through VAT by applying the provisions like threshold, exemption and zero rating. VAT being account based, invoice based and record based checks the loopholes such as under valuation no recording unauthorized trade. Further, VAT serves the vertical equity. Existing sales tax is neglected on several reasons such as narrow tax based less elastic, incapable and weak administration, incentive for tax evasion, corruption and political intervention. In the context, the best alternative for existing sales tax is VAT with more efficient and capable administrative efforts.

**Khadka (2000)** in his other book entitled “The Nepalese tax system” he describes tax compliance is very poor in Nepal and different taxes aren’t being fully paid as per the law. There is lack of transparency .Both the taxpayers and tax collectors take undue advantage of the situation. There is lack of co-ordinate approach and long term strategy.

**Ghimire (2003)** in his dissertation explains that administrative capacity, organizational structure, audit and inspection system, reward and punishments, political intervention, selection of skilled and experienced manpower are needed to improve for effective implementation of VAT.

Ghimire has given suggestions to implement VAT effectively are as follows:

- ⇒ Administrative power and creditability
- ⇒ Taxpayers identification system
- ⇒ Registration and educational program
- ⇒ Some incentive for small trader.

The existing major problem of VAT implementation in Nepal are existence of small traders in large proportion, lack of accounting records, open boarder with India market etc. which create question for the successful implementation of VAT. The essential perquisite for the successful implementation of VAT in Nepal are strong administration , educational program, technical data base system, combination of various revenue offices high level VAT implementation team. Co-ordination of VAT department closed co-ordination between government and the private sector.

**Kandel (2005)** on his article “Implementation of VAT in Nepal: Success or Failure?” Kandel describes nine years have already gone after the implementation of VAT in Nepal. The time has come to see whether we have been successful in VAT implementation or not during these years. Certainty, the major basis to evaluate is its contribution to national treasury in terms of revenue.

While gauging the success or failure of VAT in Nepal, one cannot clearly say whether it has failed or succeeds. From the point of view transparency in tax administration, increase in number of taxpayers it is satisfactory. But, from the point of view of revenue raised by value added tax itself, it isn't a success in comparison to the aim envisaged while introducing it. It was assumed at time of its initiation that it would become the major revenue source in Nepal providing folds of revenues, in comparison to than sales tax. The revenue raised today, in comparison to expectation is negligible. The trend of credit return, deregistration etc is also discouraging. Thus the VAT story in Nepal is neither total success nor total failure. However, if certain problems related to monitoring, enforcement threshold, and rate and above all invoicing are solved; there is possibility of emerging the VAT a real success as well.

The performance of VAT implementation for the past 8 years is a debatable issue. The supporters of vat at the time of its supporters of vat at the time of its introduction

used to say that it is performing well. The increase in revenue collection and the rise in taxpayers seem quite satisfactory in a country like Nepal. Had there were peace in the country, it would have better what the country is experiencing in revenue mobilization front currently. Instead, the business community and those opposing VAT at the time of its introduction used to express the views that it has failed to perform as per the expectations. Some thought that the VAT as gift box, those who can kindly contribute and those who are miser don't. VAT revenue collected by the government is completely gift amount.

**Khadka (2004)** an article as “Overview of VAT in Nepal” concludes that VAT in Nepal was introduced as a major part of the overall tax reform program initiated in the yearly 1990's. A detailed preparation was made for the implementation encountered various obstacles due mainly to the political instability and opposition from the business community. Despite this, the number of VAT registrants and the VAT revenue collection has been increasing gradually. The implementation of VAT will broaden the tax base and develop a stable and reliable source for future revenue generation.

**Laudan (2006)** in his dissertation “Analysis the problem and prospects of VAT in Nepal” concludes that VAT will have effect on economic growth major problems associated with the VAT system to business houses are account keeping and billing. Weakness of VAT administration are lack of motivation service minded attitude and dishonesty in VAT officers. VAT system the best and advanced fiscal tool in theoretical sense couldn't yielding the expected returns in Nepal because of the lack of strong and honest tax administration, lack of co-ordination between tax collectors and taxpayers, lack of strong political commitment.

**Thapa (2007)** on his dissertation “Resource mobilization through VAT in Nepal” stated that the main objectives of introducing VAT are:

- ⇒ Collecting the revenue at low rate
- ⇒ Export promotion
- ⇒ Evolving clear and transparent accounting system.
- ⇒ Reduce the economic inefficiency
- ⇒ Removing of unfairness of sales tax expanding the tax net.



The average percentage of import before the introduction of VAT was 75% whereas; the average percentage of exports was 25% only. Similarly, the average percentage of import was 70.2% and the average percentage of export was 29.8%. It shows the introduction of VAT in Nepal improves the inclination of export to some extent of 4.8%.

**Paudyal (2008)** on his dissertation “Effectiveness of VAT” concludes that VAT would definitely help to increase revenue collection of Nepal. If implemented properly. The present situation of VAT shows that the system need for understanding and commitment at the political level and administration level.

Computer networking system should be established in all the customs point with department so that related information can be accessed to all the concerned officials. Internet facilities must be providing to concern offices for the access of international price.

To improve billing system in the market needs regular supervision, audits and investigation. Consumer education is required to promote the use of invoice.

There are certain elements which increase the effectiveness of VAT. Availability of clear VAT laws and rules, effective and efficient administration, honest taxpayer, a good education program, establishment of proper invoicing mechanism and extension of tax coverage are the most important factor which obviously increase the revenue mobilization through VAT and effectiveness of VAT can be achieved.

**Bhattarai (2009)** “Practicing scenario of VAT system in Nepal” This study follows analytical and descriptive research design. In his dissertation he concludes: The business community has bitter experiences of the years of harassment from the tax administration in the past. The authority to ascertain the amount tax payable in cases of violation of rules was at the discretion of the tax officers to some extent. There has been no change in the attitude of the staff. The tax administration hasn’t able to carry out timely verification of necessary documents in case of export and undertake audit in case of other taxpayers. There are widespread complaints regarding the system of tax refund. The long open border between Nepal and India is also a great problem for us. VAT registrants find it difficult to compete with the smuggled products in the market.

### **2.3 Research Gap**

There is only few research works conducted in this topic. But such VAT related research work hasn't provided appropriate solution about effective implementation of VAT system in Nepal. Ruined practicing scenario was the main problem of VAT system. Researchers have provided general recommendation only. In this research, researcher has tried to fulfill such research gap. For better implementation of VAT needs to specific recommendation. Researcher wants to eliminate research gap exist in the past and explore for in-depth information, which can be helpful better implementation of VAT phenomenon.

## CHAPTER-III

### RESEARCH METHODOLOGY

This chapter contains a brief description of research design, population and sample, sources of data, data collection techniques, data analysis tools and limitation of the methodology

#### 3.1 Research Design

Research design is the plan, structure and strategy of investigation conceived so as to obtain answers to research questions to control variance.

This study is based on descriptive method for the historical study. Regarding the analysis of revenue collection through VAT this study is done under qualitative analysis design on the available data.

#### 3.2 Population and Sample

All the tax experts and tax payers in Nepal are considered as total population out of them, the tax experts and taxpayers in Kathmandu valley were considered as target population. 45 samples from Kathmandu valley have been taken to fulfill the objective of the study. The respondents have been divided into three groups.

The following table shows the groups of various respondents and size of sample

**Table-3.1**

**Groups of Respondents and Size of Samples**

<b>S.N</b>	<b>Group of respondents</b>	<b>Sample size</b>
1.	Tax experts/ officers	15
2.	Businessmen/ traders	15
3.	Consumers	15
	<b>Total</b>	<b>45</b>

### **3.3 Sources of Data**

The data analyzed in this study were collected from primary as well as secondary sources.

#### **3.3.1 Primary Data**

The major tools used for the collection of primary data was a set of questionnaire. A set of questionnaire was prepared and distributed to the selected respondents i.e. tax experts/officers, businessman/traders and consumers.

#### **3.3.2 Secondary Data**

The secondary data have been collected from various sources as follows:-

- ⇒ Books, journals, newspapers reports related to VAT.
- ⇒ Economic survey and budget speeches of various years.
- ⇒ Ministry of finance.
- ⇒ Various reports of VAT.
- ⇒ Dissertation related to VAT, central library.
- ⇒ Publication of VAT department and VAT project.
- ⇒ Publications of Nepal Rasta bank.
- ⇒ Publication of central bureau of statistics.
- ⇒ Publications of national planning commission.
- ⇒ National journal, magazines.

### **3.4 Data Collection Techniques**

The secondary data were collected from published reports, publications of different organizations. The primary data were collected through scheduled questionnaire. In order to get actual and accurate information the distribution works of the questionnaire was done through personal field visit.

### **3.5 Data Analysis Tools**

The data received from primary as well as secondary sources were firstly tabulated into separate format. After that the tabulated data were analyzed according to the objectives of this study. For analysis purpose the following tools have been used:

**Correlation analysis:** Karl Pearson's correlation coefficient is used to analyze the degree of correlation between different variables.

**Pie-chart/bar diagram:** Both pie-chart and bar-diagram are used for the presentation of data.

**Percentage:** To analyze the data briefly value of the data have been presented in percentage which makes the data easier to understand.

**Tabulation and trend presentation:** All the gathered data have been tabulated and present systematically.

## **CHAPTER- IV**

### **DATA PRESENTATION AND ANALYSIS**

Revenue collection has been one of the challenging jobs for the developing nations. Negligence in maintaining the book of A/c by the vendor , lack of government commitment to enforce them to maintain A/c of their business, late introduction of arise technology in the country, narrow tax base and low level of tax consciousness among the Nepalese citizen are the prominent challenge in revenue collection .

Taxation is one of the key internal sources of total government revenues. It is also the pillar of the fiscal policy. It contributes more than 70% to total internal resources of revenue. In this situation the tax structure stands as a mirror of the fiscal policy. For the purpose of this study tax structure from FY 2001/02 to 2009/10 and VAT FY 2001/02 to 2009/10 data has been used. Nepalese fiscal year starts from Shrawan 1<sup>st</sup> to Ashadh end. (June 15 to July 15)

#### **4.1 Operation of VAT**

##### **4.1.1 Registration**

Suppliers of taxable goods and services are required to register under VAT and collecting this tax. In other words, all vendors carrying on taxable business must be required to register for VAT. It is, however, not necessary for them to register if they deal only with tax exempt goods and services. Similarly, small vendors having annual turnover below the registration threshold can register voluntarily. Like other registered vendors, Small vendors who are registered voluntarily, will be able claim back input tax paid on their purchases to collect VAT on their sale and to hold the collected tax until its payment concerned tax offices.

VAT registered vendor is given a registration certificate and a taxpayer identification number (TPIN), which must be prominently displayed in the public area of his business. In the case of all other places of business, Copies of this certificate must be displayed.

#### **4.1.2 Invoicing/Accounting**

At registrant is required to issue a tax invoice wherever a transaction takes place. It is necessary to mention a tax seller's TPIN, buyer's TPIN when buyer is registered, address of buyers and sellers, description and price of goods and VAT amount of the invoices. A minimum of three copies of each invoice must be prepared. First copy must be issued in sequential numerical order. However, they can prepare invoices with different serial number for branches or different sectors of a business with prior approval of VAT administration.

Similarly, VAT registrants are also required to maintain VAT amount. It is a monthly summary of taxable purchase and sales and tax paid on purchases and charged on sales.

#### **4.1.3 Return and Payment**

VAT registrant is required to complete VAT return and submit it to the concerned VAT office with in 25 days of the month following the end of the accounting period. Accounting period is one month for the compulsory registrants and four months for the voluntary registrants.

On receipt of VAT return the tax officer is required to examine the return and check for arithmetical accuracy. If this confirms that the amount shown as payable and four particulars on the returns are collecting, the return is to be accepted.

Payment of VAT is to be made to the concerned VAT office if the amount is less than Rs.5000, payment vouchers may be collected at the designated bank and submitted to the concerned tax office.

#### **4.1.4 Tax Assessment**

VAT is self assessed tax under this system, a tax payer determines his tax liability, file his return to VAT office and pays tax within stipulated time. However, not all tax payers may file the correct returns. In such cases, VAT officials have to make tax assessment. Such assessment may be either computer assessment or management assessment.

Taxpayer's receive a notice of the processed assessment before finalizing the assessment and many actions can be taken to recover the tax. VAT assessment will normally extend back four year from the time of submission of the return by a tax payer or the due date for the submission of a tax return.

## 4.2 VAT structure and Implementation

### 4.2.1 Revenue Structure in Nepal

Every state is responsible to perform numerous activities for the betterment of the people in the country. Government needs huge volume of income to fulfill various types of expenditure. For this purpose the government collects revenue from different source like grants, administrative income, business incomes and taxation. Generally the government revenue is classified into two categories tax revenue and non tax revenue and their sum constituted the government revenue. Beside these sources, government has other sources which are subject to repayment such as loans and however grants are not compulsorily repaid. These sources are desirable only to meet the fiscal deficits.

The trends and composition of tax revenue and non tax revenue in different fiscal years are presented below:-

**Table 4.1**

### **Magnitude of Revenue Collection in Nepal**

(Rs in million)

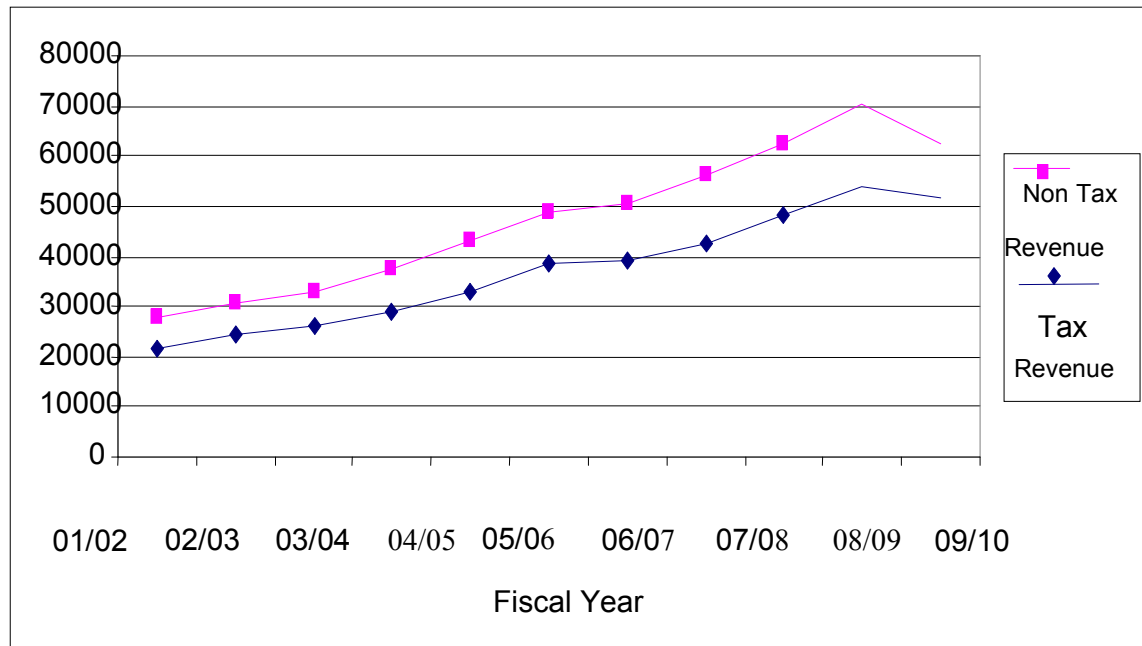
Fiscal year	Total Revenue	Tax Revenue		Non Tax Revenue	
		Amount	% as Total Revenue	Amount	% as Total Revenue
2001/02	30373.5	24424.3	80.41	5949.2	19.24
2002/03	32937.9	25939.8	78.75	6998.1	22.24
2003/04	37251	28752.9	77.18	8498.1	22.81
2004/05	42893.8	33152.2	77.28	9741.6	22.71
2005/06	48893.6	38865.0	79.48	10028.6	20.51
2006/07	50445.5	39330.6	77.96	11114.9	22.03
2007/08	56229.8	42586.9	75.73	13642.9	24.26
2008/09	62331	48173	77.28	14158.0	22.71
2009/10	70122.7	54104.7	77.15	16018.0	22.84

Source: Economic Survey, 2009/10, Ministry of Finance (MOF), Nepal

**Figure 4.1**



## Magnitude of Revenue Collection in Nepal



In fiscal year 2001/2002, the total revenue was Rs.30373.5 million in which the share of tax and non tax revenue was 80.41% and % respectively. In fiscal year 2009/10 the total revenue was Rs.70122.7 million, which share of tax and non-tax revenue was 77.15% and 22.84% respectively. Although the contribution of both tax and non tax revenue to total revenue seem to be growing simultaneously, the dominant role is tax revenue. During the study period, contribution of tax revenue has been increased in percentage term while the contribution of non tax is almost steady. But in F/Y 2009/10 it has decreased by 4 % due to instability of government and political conflict in the country.

### 4.2.2 Tax Revenue Structure of Nepal

Total tax revenue is composed of direct and indirect tax revenue. The tax on consumption is known as indirect tax whereas tax on income and capital is known as direct tax. Furthermore, land tax, registration fees, income taxes, house rent, vehicle etc. are the sources of direct tax and whereas VAT, custom, sales tax, hotel, entertainment, excise duty, contract road taxes etc are sources of indirect tax. The contribution of total tax revenue as the sum of direct and indirect is presented in table.

**Table 4.2****Structure of Tax Revenue**

(Rs in million)

Fiscal year	Total Tax Revenue	Direct Tax		Indirect Tax	
		Amount	% as Total Tax Revenue	Amount	% as Total Tax Revenue
2001/2002	21668.0	4655.9	21.48	17012.1	78.51
2002/03	24424.3	5340.0	21.86	19084.3	78.13
2003/04	25939.8	6187.9	23.85	19751.9	76.14
2004/05	28752.9	7516.0	26.13	21236.8	73.86
2005/06	33152.1	8951.5	27.00	24200.6	72.99
2006/07	38865.1	10159.4	26.14	28705.7	73.859
2007/08	39330.6	10597.5	26.94	28733.1	73.05
2008/09	42587.0	10102.8	23.72	32481.2	76.27
2009/10	48173.0	11912.6	24.72	36260.9	75.27

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

During this study period, the share of direct tax in total tax is increasing simultaneously from 2001/2002 to 2009/10 but it has decreased by 2 % in F/Y 2009/10 because of Political crisis of Nepal. The share of indirect taxes of total revenue remains high through out the study. Through the relative share of direct taxes is increasing, tax revenue is still dominated by indirect taxes.

**4.2.3 Magnitude of Direct Tax Revenue**

The compositions of direct tax are land revenue, registration, tax on property and income is shown below:-

**Table 4.3****Magnitude of Direct Tax Revenue**

(Rs in million)

Fiscal Year	Direct Tax	Land Revenue and Registration		Tax on property, income	
		Amount	Percentage	Amount	Percentage
2001/02	4655.9	1066.6	22.90	3589.3	77.09
2002/03	5340.0	1015.4	19.0	4324.6	80.09
2003/04	6187.9	1004.2	16.22	5183.7	83.77
2004/05	7516.0	1003.2	13.34	6512.9	86.65
2005/06	8951.5	1015.9	11.34	7935.6	88.65
2006/07	10159.4	612.9	6.03	9546.5	93.96
2007/08	10597.5	1131.8	10.67	9465.7	89.32
2008/09	10102.8	1414.3	13.99	8691.5	86.00
2009/10	11912.6	1697.5	14.24	10215.1	85.77

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

In fiscal year 2001/2002 the contribution of both components to direct tax was Rs.1066.6 (22.90%) million and 3589.3 (77.09%) million respectively. Similarly in 2008/09, their contribution were 1414.3 (13.99%) million and 8691.5 (86%) million and in F/Y 2009/10 their contribution were 1697.5 (14.24%) million and 10215.1 (85.77%) million. During the study period it is found that the proportion of land revenue went on declining and reached to the lowest percent i.e. 6% in 2005/06 best after two years, the collection of land revenue gradually increased but tax on property income is almost steady.

**4.2.4 Magnitude of Indirect Tax Revenue**

The composition of indirect tax is custom tax on consumption & product of goods and services.

**Table 4.4****Magnitude of Indirect Tax Revenue**

(Rs in million)

Fiscal Year	Indirect Tax	Land Customs		Tax on consumption & product of goods and services	
		Amount	Percentage	Amount	Percentage
2001/02	17012.1	7327.4	43.07	9684.7	56.92
2002/03	19084.3	8309.1	43.53	10775.2	56.46
2003/04	19751.9	8502.2	43.04	11247.0	56.94
2004/05	21236.8	9517.7	44.81	11719.1	55.18
2005/06	24200.6	10813.3	44.68	13387.3	55.18
2006/07	28705.7	12552.1	43.72	16153.6	56.27
2007/08	28733.1	12658.8	44.05	16074.3	55.94
2008/09	32481.2	14236.4	43.82	18244.8	56.17
2009/10	36260.9	15554.8	42.89	20705.6	57.10

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

The components of indirect tax revenue are : Custom duties (imports, exports, Indian duties and other), tax on consumption and production of goods and services (industrial products, liquor contract, sales tax / value added tax, entertainment tax, hotel tax, air flight, contract tax, road and bridges maintenance tax and others). Indirect tax provides around seventy percentage revenue of the total tax revenue in Nepal. In second part the value added tax plays the vital role to increase an indirect tax.

**4.2.5 Tax/GDP Ratio**

The Tax / GDP ratio is shown in table 4.5. The table shows rather disappointing scenario of Tax / GDP for the study period.

**Table 4.5****Tax / GDP Ratio****(Rs in million)**

<b>Fiscal Year</b>	<b>GDP</b>	<b>Tax Revenue</b>	<b>Tax / GDP ratio</b>
2001/2002	239388	21668.0	9.05
2002/03	269570	24424.3	9.06
2003/04	289798	25939.8	8.4
2004/05	330018	28752.9	8.7
2005/06	366251	33152.1	9.05
2006/07	394052	38865.1	9.8
2007/08	406138	39330.6	9.68
2008/09	437546	42587.0	9.73
2009/10	474919	48173.0	10.14

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

However, it has been rising from 9.05% in fiscal year 2001/2002 to 10.14% in 2009/10 but growth is not continuous. Once the growth reached to 9.73% in F/Y 2008/09 and again started declines & reached to 8.4% in fiscal year 2003/2004, from fiscal year 2004/05 again started to rise and reached to 9.73% in fiscal year 2008/09 and again it increase in current year 2009/10. This implies that Tax / GDP ratio seems to be very low and it is marginally increasing.

### 4.3 VAT Implementation Analysis

#### 4.3.1 Registration

**Table 4.6**  
**Trend of VAT Registration**

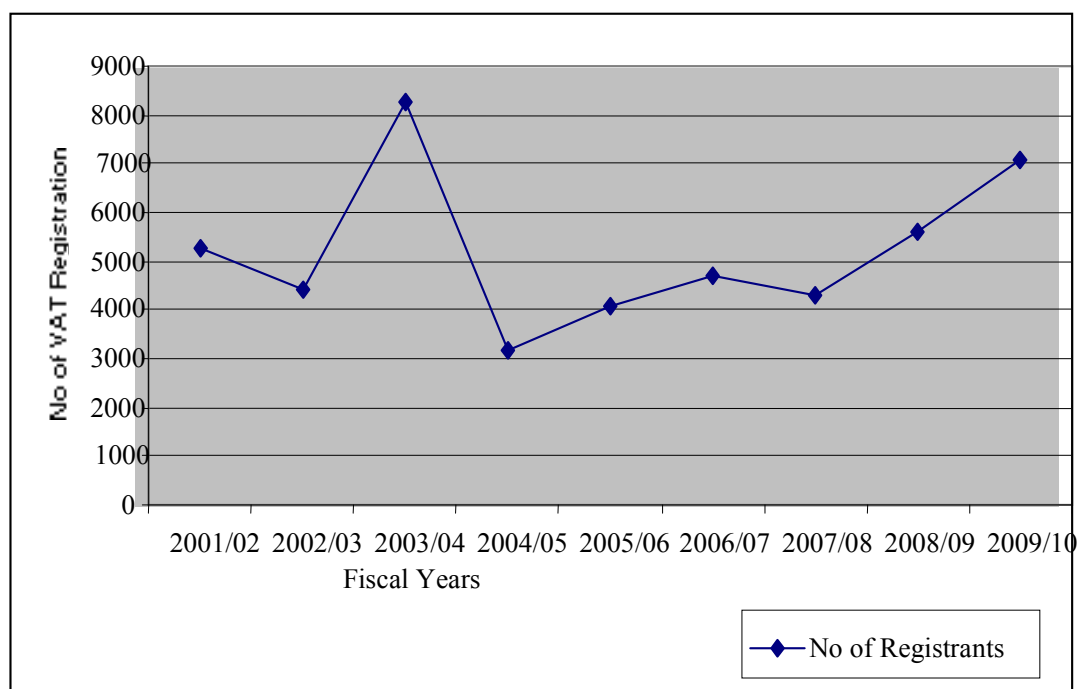
(Rs in million)

Fiscal Year	No of VAT Registrants	Registrants each year	Percentage Increase
2001/02	5247	5247	-
2002/03	9687	4440	84.61
2003/04	17947	8260	85.26
2004/05	21093	3146	17.53
2005/06	25149	4056	19.22
2006/07	29872	4723	18.78
2007/08	34174	4302	14.40
2008/09	39776	5602	16.39
2009/10	46831	7055	17.73

Sources: Annual Report (2009/10) Inland Revenue Department, Nepal

**Figure 4.2**

**Trends of VAT**



The number of VAT registrants has increased consistently in the last 9 years from 5247 in FY 2001/02, to 9687 in 2002/03, to 17947 in FY 2003/04, to 21093 in FY2004/05, to 25149 in FY 2005/06, to 29872 in 2006/07, to 34174 in 2007/08, to 39776 in2008/09 and to 46831 in 2009/10. The growth rate of registrants is satisfactory. Compromise made by government with registrants has also helped to increase VAT registrant's number gradually. There may be potential tax payer still outside from the tax net. According to questionnaire, the registration process and service provide by tax office is not satisfactory.

#### 4.3.2 VAT Revenue Collections

Value Added Tax is the best form of Sales tax, which 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 distortion. The revenue collection from VAT in different fiscal year is presented in table.

**Table 4.7**

#### **Trends of VAT Collection**

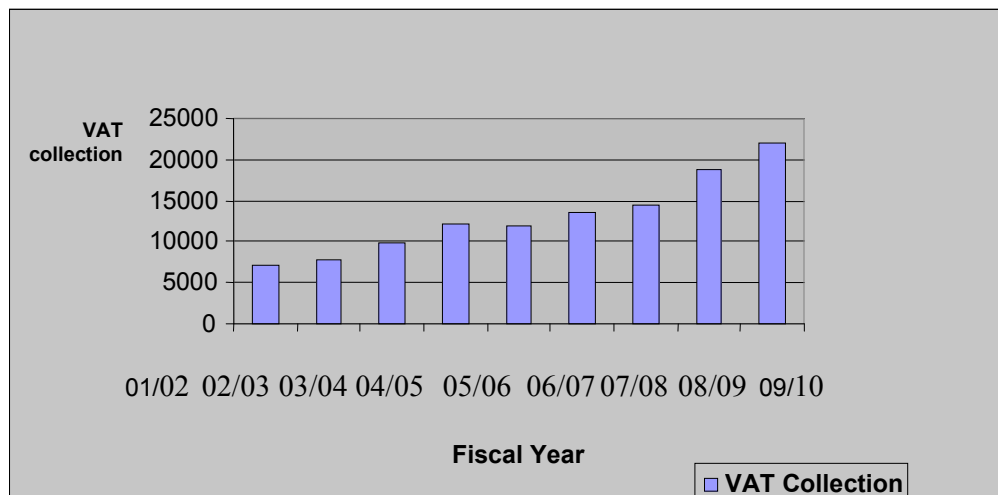
(Rs in million)

<b>Fiscal Year</b>	<b>VAT Collection</b>	<b>Percentage Change</b>
2001/02	7123	-
2002/03	7882	10.65
2003/04	9850	24.96
2004/05	12048	22.31
2005/06	11948	-0.83
2006/07	13450	12.57
2007/08	14479	7.65
2008/09	18895	30.50
2009/10	21946	16.15

Sources: - Annual report (2009/10), Inland Revenue Department, Nepal.

**Figure 4.3**

## Trends of VAT Collection



In the above table (4.7) VAT revenue was 7123 million in F/Y 2001/02. The next year VAT was increase by 10.65 percent, which were 7882. Similarly, revenue collection from VAT in fiscal year 2003/04 to 2009/10 are 9850, 12048, 11948, 13450, 14479, 18895 and 21946 respectively. In fiscal 2005/06 VAT collection was decrease by 100 million or -0.83%. Fiscal year 2008/09 was increased by 4416 million or 30.50%. The VAT revenue is in increasing trend. It may be due to increasing trend of registration into VAT. The interview revealed that the causes of not collecting VAT as expected are economic slowdown, lengthy accounting system and lack of social recognition to taxpayer.

### 4.3.3 Composition of VAT Revenue

VAT Revenue is divided in two domestic and import components which is indicated in Table 4.8.

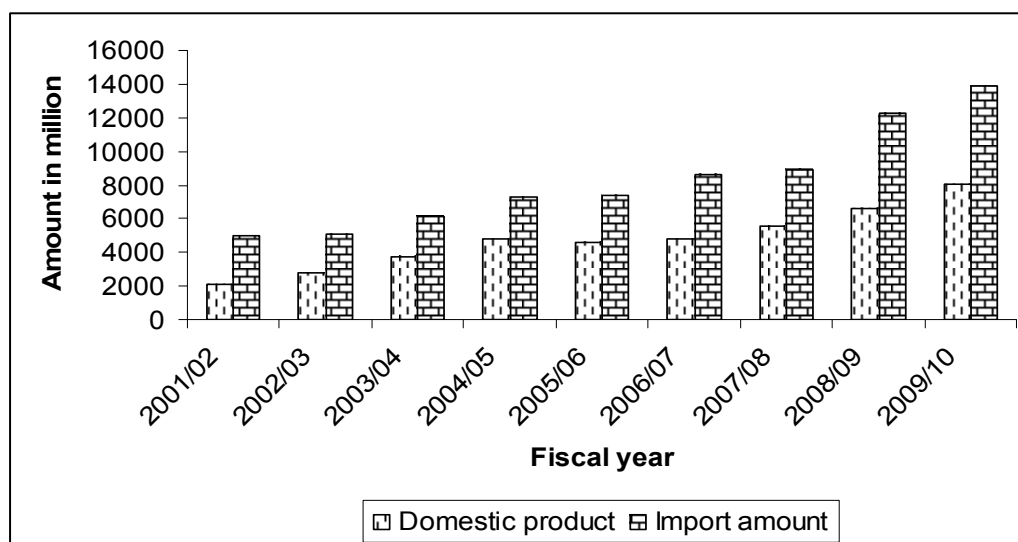


**Table: 4.8****Division of Total VAT Revenue**

(Rs in million)

Fiscal Year	VAT Revenue	Domestic products		Imports	
		Amount	percentage	Amount	Percentage
2001/02	7123	2101	29.50	5022	70.50
2002/03	7882	2813	35.70	5069	64.31
2003/04	9850	3720	37.80	6130	62.23
2004/05	12048	4745	39.38	7303	60.61
2005/06	11948	4608	38.56	7340	61.43
2006/07	13450	4802	35.83	8630	64.16
2007/08	14479	5604	38.70	8875	61.29
2008/09	18895	6624	35.00	12270	65.00
2009/10	21946	8057	36.71	13889	63.29

Sources: - Annual report (2009/10), Inland Revenue Department, Nepal

**Figure 4.4****Division of Total VAT Revenue**

Almost two-third of VAT revenue is generated from imports and rest from domestic products. In the Fiscal Year 2001/02, the share of domestic product products and import product in total VAT revenue was 29.5% and 70.5% respectively, whereas in fiscal year 2002/03 their share was 35.7% and 64.31% like wise , in fiscal year 2009/10, the share of domestic products and imports was exactly 36.71% and 63.29%. In the above trend, total revenue from domestic products of VAT was increasing condition but import product was increasing condition. Imports product of VAT was

declining condition due to membership of WTO.

From this Table 4.8 correlation between the domestic product and imports, can be determined and the relation between them have been assessed. The table shows these variables, VAT revenue as the dependent variable and domestic products and imports as independent variables. In this period the Multiple Correlation is suitable.

Let,

$x_1$  = VAT Revenue

$x_2$  = Domestic product

$x_3$  = Imports

By formula

$$R_{1.23} = \sqrt{\frac{r_{12}^2 + r_{13}^2 - 2r_{12} \cdot r_{23} \cdot r_{13}}{1 - r_{23}^2}}$$

Where,

$r_{12}$  = Simple (zero order) correlation coefficient between  $x_1$  and  $x_2$

$r_{23}$  = Simple (zero order) correlation coefficient between  $x_2$  and  $x_3$

$r_{13}$  = Simple (zero order) correlation coefficient between  $x_1$  and  $x_3$

$$r_{12} = \frac{\sum x_1 x_2}{\sqrt{\sum x_1^2 \cdot \sum x_2^2}}$$

$$r_{13} = \frac{\sum x_1 x_3}{\sqrt{\sum x_1^2 \cdot \sum x_3^2}}$$

$$r_{23} = \frac{\sum x_2 x_3}{\sqrt{\sum x_2^2 \cdot \sum x_3^2}}$$

**Table: 4.9**

**Calculation of Correlation coefficient between VAT, Domestic Products and Imports**

$x_1$	$x_2$	$x_3$	$x_1x_2$	$x_1x_3$	$x_2x_3$	$x_1^2$	$x_2^2$	$x_3^2$
7123	2101	5022	14965423	35771706	10551222	50737129	4414201	25220484
7882	2813	5069	22172066	39953858	4259097	62125924	7912969	25694761
9850	3720	6130	36642000	60380500	22803600	97022500	13838400	37576900
12048	4745	7303	57167760	879865440	346527350	145154304	22515025	5333380900
11948	4608	7340	55056384	87698320	33822720	142754704	21233664	538756200
13450	4802	8630	64829000	116073500	41596600	180902500	23232400	74476900
14479	5604	8875	81140316	128501125	49735500	209641441	31404816	787656625
18895	6624	12270	125160480	331841650	81276480	357021025	43877376	150552900
21946	8057	13889	176818922	304807994	111903673	481626916	64915249	192904321
			$\sum x_1x_2$ 633852351	$\sum x_1x_3$ 1884894093	$\sum x_2x_3$ 712476242	$\sum x_1^2$ 1726586443	$\sum x_2^2$ 233344100	$\sum x_3^2$ 2972448391

$$r_{12} = \frac{\sum x_1x_2}{\sqrt{\sum x_1^2 \cdot \sum x_2^2}} = \frac{633952351}{\sqrt{1726986443 \times 233344100}} = 0.9986$$

$$r_{13} = \frac{\sum x_1x_3}{\sqrt{\sum x_1^2 \cdot \sum x_3^2}} = \frac{1884894093}{\sqrt{1726986443 \times 5972498391}} = 0.5869$$

$$r_{23} = \frac{\sum x_2x_3}{\sqrt{\sum x_2^2 \cdot \sum x_3^2}} = \frac{712476242}{\sqrt{233344100 \times 5972448391}} = 0.6035$$

$$\begin{aligned}
R1.23 &= \sqrt{\frac{r_{12}^2 + r_{13}^2 - 2r_{12} \cdot r_{23} \cdot r_{13}}{1 - r_{23}^2}} \\
&= \sqrt{\frac{(10.9986)^2 + (0.5869)^2 - 2 \times 0.9986 \times 0.5869 \times 0.6035}{1 - (0.6035)^2}} \\
&= \sqrt{\frac{0.9972 + 0.3444 - 0.7073}{0.3657}} \\
&= 0.9988
\end{aligned}$$

**Decision:** There is significant positive correlation between domestic products and imports for the VAT. Hence, it proves that domestic products and imports are significant positive correlated for each other.

#### 4.3.4 Share of VAT Revenue in GDP (Gross Domestic Product)

The share of VAT Revenue in GDP is shown in Table: 4.10

**Table: 4.10**

#### Share of VAT Revenue in GDP

(Rs in million)

Fiscal Year	GDP	VAT Revenue	% of GDP
2001/02	289798	7123	2.46
2002/03	330018	7882	2.39
2003/04	366251	9850	2.69
2004/05	394052	12048	3.06
2005/06	406138	11948	2.94
2006/07	437546	13450	3.07
2007/08	474919	14479	3.04
2008/09	508651	18895	3.71
2009/10	557869	21946	3.93
<b>Average</b>	<b>418360</b>	<b>13069</b>	<b>3.03</b>

Sources: - Annual report (2009/10), Inland Revenue Department, Nepal

**Figure: 4.5**

**Share of VAT Revenue in GDP**

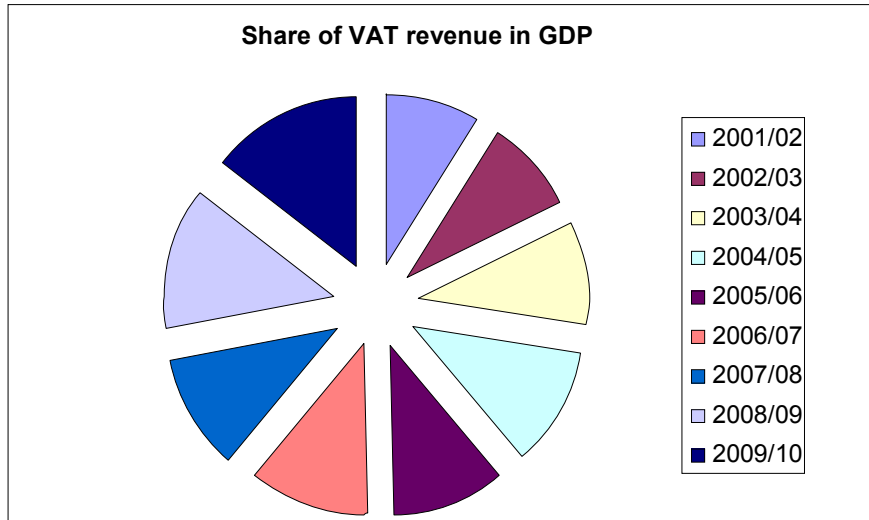


Table 4.10 and figure 4.5 shows that on an average the share of VAT revenue as percentage of GDP was 3.03%

The share of VAT revenue in total GDP is very low from F/Y 2001/02 to 2009/10. The ratio of the VAT in GDP was not comparatively increase but it was slightly increasing in ratio of the VAT in GDP. VAT revenue of Nepal as percentage of GDP is between 2.46 to 3.93 with no higher fluctuation. Lacks of co-operation from business community and awareness level of consumer are the main cause of VAT.

**4.3.5 Share of VAT in Total Revenue**

The share of VAT revenue in total revenue is indicated in Table 4.11

**Table 4.11**

**Share of VAT in Total Revenue**

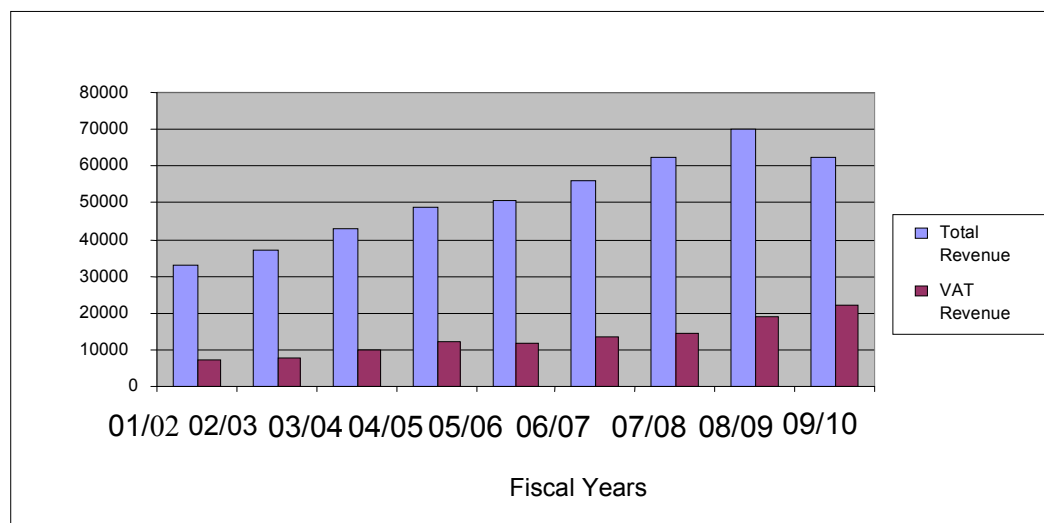
(Rs in million)

<b>Fiscal Year</b>	<b>Total Revenue</b>	<b>VAT Revenue</b>	<b>% of VAT in Total Revenue</b>
2001/02	32937.9	7123	21.62
2002/03	37251	7882	21.20
2003/04	42893.8	9850	23.00
2004/05	48893.6	12048	24.64
2005/06	50445.5	11948	23.68
2006/07	56229.8	13450	23.92
2007/08	62331	14479	23.23
2008/09	70122.7	18895	26.94
2009/10	62178.1	21946	35.29
<b>Average</b>	<b>51475.9</b>	<b>13069</b>	<b>24.83</b>

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

**Figure 4.6**

**VAT and Total Revenue**



Above table 4.11 and figure 4.6 shows that on average VAT revenue to total revenue is 24.83%.

The share of VAT revenue is total revenue is almost around 24% during the study period and the fiscal year 2008/09 is highest percentage for the eight year implementation year. Hence, the percentage of VAT played greater role in total revenue of the government justification for the implementation of VAT is difficult to explain. The total revenue is increasing but in F/Y 2009/10, it has decreased it's causes may be lack of co-ordination between business community and government and other it may be instability of government.

#### 4.3.6 Share of VAT in Total Tax Revenue

The share of VAT revenue in total tax revenue is shown in Table.4.12

**Table 4.12**

#### **Share of VAT Revenue in Total Tax Revenue**

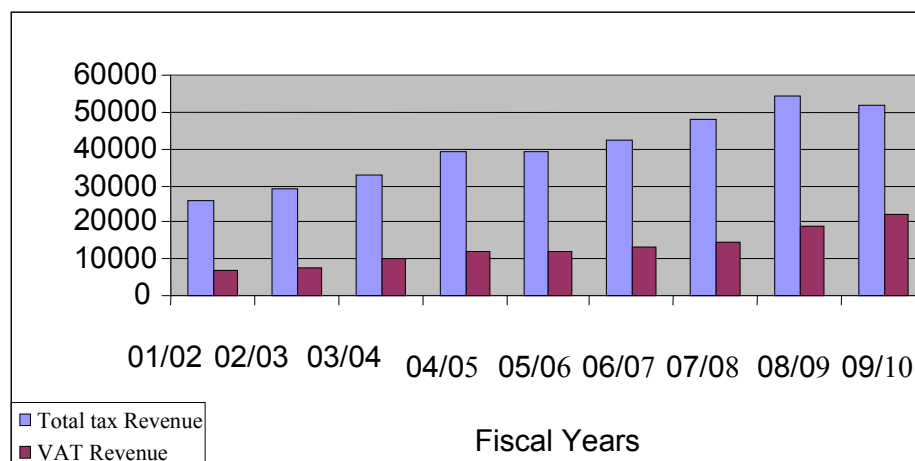
(Rs. in million)

<b>Fiscal Year</b>	<b>Total tax Revenue</b>	<b>VAT Revenue</b>	<b>% of VAT in Total Tax</b>
2001/02	25939.8	7123	27.5
2002/03	28752.9	7882	27.41
2003/04	33152.1	9850	29.71
2004/05	38865.1	12048	31.00
2005/06	39330.6	11948	30.37
2006/07	42587.0	13450	31.60
2007/08	48173.0	14479	30.00
2008/09	54104.7	18895	35.00
2009/10	51907.5	21946	34.37
<b>Average</b>	<b>34959.9</b>	<b>13069</b>	<b>31.65</b>

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal

**Figure 4.7**

**Trend of VAT Revenue in Total Tax Revenue**



In above table, VAT revenue contributes 27.5% to 34.7% to the total tax revenue. VAT revenue to total tax revenue is in increasing trend from F/Y 2001/02 to 2009/10.

**4.3.7 Share of VAT in Total Indirect Tax Revenue**

The share of VAT in total indirect tax revenue is shown in Table 4.13

**Table 4.13**

**VAT Revenue percentage of Total Indirect Tax**

(Rs in million)

Fiscal Year	Total Indirect Tax Revenue	VAT Revenue	% of VAT Indirect Tax
2001/02	19751.9	7123	36
2002/03	21236.8	7882	37.11
2003/04	24200.6	9850	40.70
2004/05	28705.7	12048	41.97
2005/06	28733.1	11948	41.58
2006/07	32481.2	13450	41.40
2007/08	36260.9	14479	40.00
2008/09	41032.9	18895	46.00
2009/10	40294.35	21946	54.46
<b>Average</b>	<b>30299.7</b>	<b>13069</b>	<b>42.135</b>

Source: Economic Survey 2009/10, Ministry of Finance (MOF), Nepal



**Figure 4.8**

**Percentage of VAT Revenue in Total Indirect Tax**

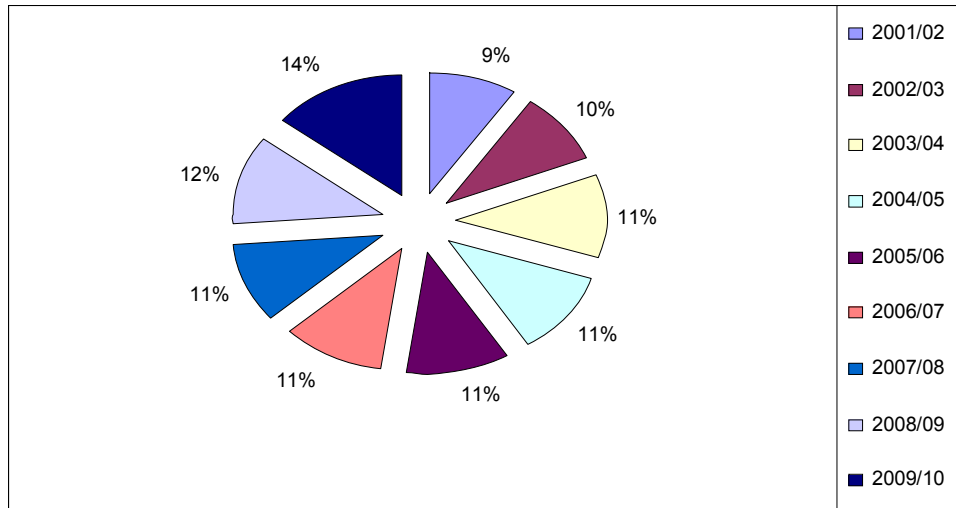


Table 4.13 and pie chart 4.8 shows the share of VAT in total indirect tax. On an average share of VAT in total indirect tax is 42.135%.

The share of VAT revenue is almost 40% of the total indirect tax revenue and it is increasing over time for the study period. VAT share contributes from 36% to 54.46% of the total indirect tax. It may be caused on private sector rising in Nepal after accession to WTO.

**4.4 Empirical Findings**

There have been various empirical studies conducted before and after the implementation of VAT system in Nepal. It is viewed that this system hasn't been implemented effectively as expected. Despite the strong opposition from the business community during the earlier period, VAT was implemented in its full fledged with the co-operation between private sector and government. In the earlier period of VAT implementation, there was lack of skilled and trained man powers, administrative structure wasn't setup properly. But currently different informative programs, seminars and meeting were held to make businessmen, consumers and people known to the VAT. Currently business community is also in favor of VAT and further demanding to identify all the traders having taxable capacity and include into the net.

In such situation an empirical study is done to know the views of persons of different field on different aspects of VAT.

For the purpose of survey, different questionnaire were prepared to know the opinion of the various persons of different field including tax expert/tax officers, businessmen and consumers about various aspects of VAT.

The sample for this survey is taken only from different fields as given in the table

**Table: 4.14**

**Sample Size of the Field Survey**

<b>S.N</b>	<b>Respondents</b>	<b>Sample Size</b>	<b>Percentage</b>
1	Tax Experts/Officers	15	33.33
2	Businessmen	15	33.33
3	Consumers	15	33.33
<b>Total</b>		<b>45</b>	<b>100</b>

Source: - Opinion Survey, 2011

The results and the interpretation of the survey results have been presented below:-

**4.4.1 Views on VAT as an appropriate Means of Raising the Government Revenue**

In the context of Nepal where, government expenditure is always increasing but the revenue collection is not increasing proportionately as required to finance the government expenditure. It is just 8 years of VAT implementation in Nepal, the impact of VAT has not seen properly. Theoretically VAT is the best form of taxable but practically it depends on the environment provided by the country for its implementation. It is necessary to know whether VAT is an appropriate means of raising fund or not in the views of its appropriateness regarding its revenue collection can be shown in the following table:

**Table 4.15****Views on VAT as an appropriate Means of Raising the Government Revenue**

Respondents	Yes		No		Total
	Number	Percent	Number	Percent	
Tax Experts/Officers	15	100	-	-	15
Businessmen	13	86.67	2	13.33	15
Consumers	14	93.33	1	6.67	15
<b>Total</b>	<b>42</b>	<b>93.33</b>	<b>3</b>	<b>6.67</b>	<b>45</b>

Source: - Opinion Survey, 2011

In the above table it is observed that almost all the respondents i.e. 93.33 % of respondents are agreed that the VAT is an appropriate means of raising government revenue which include 100 % of Tax experts/Tax officers, 86.67% businessmen and 93.33 % consumers, whether 6.67% gave their negative opinion which comprise 13.33% from businessmen, 6.67%from consumers and non from Tax officer and Tax experts. It shows that VAT is the appropriate means of government revenue.

**4.4.2 Causes on VAT as an appropriate Means of Raising Government Revenue**

To see the answer why the VAT is appropriate mean of raising government revenue, a question asked. The answer given by the respondents has been presented in table 4.16

**Table 4.16****Causes on VAT as an appropriate Means of Raising Government Revenue**

Respondents	Broad coverage		Control tax evasion		Proper implementation		Stop illegal trade		All		Total
	No.	%	No.	%	No.	%	No.	%	No.	%	
Tax Experts/officers	6	40	4	26.67	1	6.67	3	20	1	16.67	15
Businessmen	3	23	7	53.84	-	-	2	15.38	1	7.6	13
Consumers	4	28.57	5	35.71	-	-	3	21.42	2	14.28	14
<b>Total</b>	<b>13</b>	<b>30.95</b>	<b>16</b>	<b>38.09</b>	<b>1</b>	<b>6.67</b>	<b>8</b>	<b>19.04</b>	<b>4</b>	<b>9.5</b>	<b>42</b>

Source: - Opinion Survey, 2011

It is observed that 38.09% respondents viewed that it is appropriate means to control evasion followed 30.95% due to broad base, 19.04% to stop illegal trade, 9.5% due to all the reasons and 6.67% for proper implementation tax system in Nepal.

**4.4.3 Views on appropriate means of Raising Government Revenue**

To know the opinion of respondents why VAT is not an appropriate means of raising

government, a question was asked, if not, what the appropriate mean to raise government revenue. The opinion suggested by the respondents are presented in table 4.17

**Table 4.17**

**Views on appropriate means of Raising Government Revenue**

Respondents	Sales tax		Contract tax		Entertainment tax		Excise duty		Others		Total
	No.	%	No	%	No.	%	No.	%	No.	%	
Tax Experts/officers	-	-	-	-	-	-	-	-	-	-	-
Businessmen	1	50	-	-	1	50	-	-	-	-	2
Consumers	-	-	-	-	1	100	-	-	-	-	1
<b>Total</b>	<b>1</b>	<b>33.33</b>	-	-	<b>2</b>	<b>66.67</b>	-	-	-	-	<b>3</b>

Source: - Opinion Survey, 2011

It is observed that those who were disagreed that Vat is the appropriate means of raising of government revenue 33.33% respondents viewed sales tax is main source of raising government revenue, 66.67% of respondents viewed the entertainment tax is the main source of raising government revenue. But no one accepted that contract Tax and Excise Duty were the main source of government revenue. Thus it is concluded that neither Sales Tax nor Contract Tax nor Entertainment nor Excise Duty are the main source of government revenue.

**4.4.4 Views on Superiority of VAT to the Areas it has replaced**

VAT has replaced four taxes such as sales tax, entertainment tax, hotel tax and contract tax. VAT, a latest development of sales tax system, is a new innovation in the field of taxation. VAT being preferred by many countries of the world, has proved itself to Sales Tax as well as other taxes. Because of effective of revenue mobilization as ability to tackle with all the Tax evasion, wide tax base, transparent, VAT is considered superior to other areas of tax it has replaced. The survey result in this aspect has been summarized in the table below:

**Table 4.18****Views on Superiority of VAT**

Respondents	Yes		No		Total
	Number	Percent	Number	Percent	
Tax Experts/Officers	15	100	-	-	15
Businessmen	12	80	3	20	15
Consumers	11	73.33	4	26.67	15
<b>Total</b>	<b>38</b>	<b>84.44</b>	<b>7</b>	<b>15.56</b>	<b>45</b>

Source: - Opinion Survey, 2011

It is observed that out of 45 respondents 84.44% respondents said that VAT is superior to other forms of Tax. Those who put this view were 100% Tax experts/officers; 80% Businessmen and 73.33% consumers. However 15.56% respondents have opposed it. Those respondents who have opposed this view were 20 % Businessmen and 26.67 % Consumers. From this analysis it is clear that VAT is superior to other form of indirect tax like Sales, Contract, Entertainment, Excise and others.

**4.4.5 Causes on VAT is Superior than Other Types of Sales tax**

A question asking the reasons why VAT is superior to other form of Tax, the responses provided by them have been presented in table 4.19

**Table 4.19****Causes on VAT is Superior than Other Types of Sales tax**

Respondents	Increase revenue collection		Facility of refund		Facility of tax credit		All		Total
	No.	Percent	No.	Percent	No.	Percent	No.	Percent	
Tax Experts/Officers	11	73	1	6.67	2	13.33	1	6.67	15
Businessmen	6	50	3	25	2	16.67	1	8.3	12
Consumers	8	72	1	9.9	1	9.09	1	9.09	11
<b>Total</b>	<b>25</b>	<b>65.78</b>	<b>5</b>	<b>13.15</b>	<b>5</b>	<b>13.15</b>	<b>3</b>	<b>7.8</b>	<b>38</b>

Source: - Opinion Survey, 2011

From above table shows that among 38 respondents 65.78% said that VAT is superior to other types of sales tax because it helps to increase revenue collection, 13.15% said it has provided the facility of refunding Tax, other 13.15% noted it has tax credit facility and rest 7.8% maintained all causes mentioned above. Thus it shows that VAT is superior to all other form of sale Tax.

#### 4.4.6 Views on Superior types of Sales Tax

**Table 4.20**

#### **Views on Superior types of Sales Tax**

Respondents	Sales Tax		Contract Tax		Entertainment Tax		Excise duty		Import/Export duty		Others		Total
	No	%	No	%	No	%	No	%	No	%	No	%	
Tax Experts/officers			-	-	-	-	-	-	-	-	-	-	--
Businessmen	1	33.33	-	-	1	33.33	-	-	1	33.33	-	-	3
Consumers	2	50.00	-	--	1	25	1	25	--	--	-	-	4
<b>Total</b>	<b>3</b>	<b>42.87</b>	-	-	<b>2</b>	<b>28.57</b>		<b>14.28</b>	<b>1</b>	<b>14.28</b>	-	-	<b>7</b>

Source: - Opinion Survey, 2011

Above table shows 7 respondents showed their disagreement that VAT is superior to other form of Tax out of 45 respondents. They said that other individual taxes are superior then the VAT. 42.87% of respondents prefer sales tax over than VAT, 28.57% of respondents said entertainment tax is superior to VAT. 14.28% respondents said Excise duty and 14.28% respondents said Import/Export duty are superior to VAT and other types of Sales tax.

#### 4.4.7 Views on Billing System

Billing System is the backbone of the VAT system. All the business has to receive the bills of actual transaction price while importing and buying of goods and services. The price of the goods and services with and without VAT has to be mentioned explicitly in the bill. The business has to pay the amount of difference between tax collected on sale and tax paid on purchase to the VAT office. He has to pay the

income tax as well as the profit of the transaction. Thus the billing system plays important role in the field of VAT system. But in Nepal the billing system has been one of the major problems. So, the question is designed to show the comments on billing system of VAT. The outcome of the field survey is given below:

**Table 4.21**

**Views on Billing System**

Respondents	Possible		Impossible		Costly		Total
	Number	Percent	Number	Percent	Number	Percent	
Tax Experts/Officers	15	100	-	-			15
Businessmen	10	66.67	-	-	5	33.33	15
Consumers	10	66.67	2	13	3	20	15
<b>Total</b>	<b>35</b>	<b>77.78</b>	<b>2</b>	<b>4.4</b>	<b>8</b>	<b>17.78</b>	<b>45</b>

Source: - Opinion Survey, 2011

From the empirical survey, it is found that all the tax expert or officers advocate for the possibility of billing system. Out of 45 respondent 35 respondents who represent 77.78% replied that issuing bill is very much possible but 4.4% said issuing bill is impossible and 17.78% replied/viewed it is costly

**4.4.8 Views on Rising Price due to VAT System**

In the earlier stage of VAT implementation, there was a strong opposition from the business community regarding the possibility of rise in the price of commodities due to VAT system. There was also a voice from different people on price rising on commodities; consumers also complain that businessmen would charge more prices and validate role of the VAT. Here, attempt has been made to obtain the information from the respondents to find out whether VAT would raise the price of the commodity or not? The views of the respondents have been presented in table 4.22

**Table 4.22**

**Views on Rising Price due to VAT System**

<b>Respondents</b>	<b>Yes</b>		<b>No</b>		<b>Total</b>
	<b>Number</b>	<b>Percent</b>	<b>Number</b>	<b>Percent</b>	
Tax Experts/Officers	1	6.67	14	93.33	15
Businessmen	6	40	9	60.00	15
Consumers	5	33.33	10	66.67	15
<b>Total</b>	<b>12</b>	<b>26.67</b>	<b>33</b>	<b>73.33</b>	<b>45</b>

Source: - Opinion Survey, 2011

It is observed that out of 45 respondents 12 respondents which represents 26.67% gave their opinion that VAT would increase the price of commodity whereas 33 respondents which comes to 73.33% showed their view negatively. It shows that price of the commodity would not increase due to implementation of VAT. Among them who opinioned that VAT would increase the price of commodity were 6.67% Tax experts, 40% Businessmen, and 33.33% consumers however those respondents who claimed that VAT would not increase the price were 93.33% Tax experts/officers, 60% businessmen and 66.67% consumers argue that there is no raise in price due to VAT system. From the above analysis it is clear that price of the commodity would not increase because of implementation of VAT.

**4.4.9 Causes on Price Rise due to VAT System**

Some respondents argue that price would be raised price due to VAT system. The causes behind the rise in the price have been presented below:



**Tables 4.23**

**Causes on Price Rise due to VAT System**

Respondents	Compliance		High Profit		Non awareness of consumer		All		Total
	No	Percent	No	Percent	No	Percent	No	Percent	
Tax Experts/Officers	-	-	-	-	1	100	-	-	11
Businessmen	1	16.67	1	16.67	2	33.33	2	33.33	6
Consumers	2	40	1	20	1	20	1	20	5
<b>Total</b>	<b>3</b>	<b>25</b>	<b>2</b>	<b>16.67</b>	<b>4</b>	<b>33.33</b>	<b>3</b>	<b>25</b>	<b>12</b>

Source: - Opinion Survey, 2011

It is observed that those, respondents who argued that there is rise in price due to VAT system, said that non awareness of consumers 33.33%, compliance cost, high profit 25%,16.67% and all the above 25% are the main reason for increasing price of the commodity.

**4.4.10 Opinions on Problems in the Process of VAT Implementation**

The taxpayers and the tax collectors both have to be well known and conscious about the record keeping and process of VAT system. The field survey was conducted to know the opinions of different respondents to explore the problems in the process of VAT collection. The study showed registration, collection and tax refund were the main problems for the implementation of VAT.

It is common opinion of the people that there is problem to implement VAT in Nepal. So to see the answer a question was asked what kind of problem was observed in the person of VAT implementation in Nepal. The responses given by the respondents have been presented in the table 4.26

**Table: 4.24**

**Opinions on Problems in the Process of VAT Implementation**

Respondents	Registration		Collection		Refund		Other		Total
	No.	%	No.	%	No.	%	No.	%	
Tax Experts/Officers	4	26.67	9	60	1	6.67	1	6.67	15
Businessmen	6	40	5	33.33	3	20	1	6.67	15
Consumers	3	20	8	53.33	2	13.33	2	13.33	15
<b>Total</b>	<b>13</b>	<b>28.88</b>	<b>22</b>	<b>48.88</b>	<b>6</b>	<b>13.33</b>	<b>4</b>	<b>26.67</b>	<b>45</b>

Source: - Opinion Survey, 2011

It is observed that out of 45 respondents 22 (48.88%) respondents showed the collection problem followed by registration 28.88%, refund 13.33% and 26.67% others. Respondents who showed the problem in collection were 60% Tax experts/Tax officers, 33.33% businessmen and 53.33% consumers. Similarly the respondents who showed registration problem were 26.67% Tax Experts/officers 40% businessmen and 20% consumers. Those who showed the refunding problem were 6.67% Tax experts/officers, 20% businessmen and 13.33% consumers.

**4.4.11 Important Factor for the Effectiveness of VAT in Revenue Collection**

Although it has been nine year from the implementation of VAT, however it has not yet secured the expected results. There are many problems existing in the Implementation of VAT. It is necessary to identify the existing problems and efforts to solve them successively to make the VAT more successful. There are many factors that effect of VAT. They are proper implementation, broad coverage, tax education, effective and efficient administration and clear VAT laws and regulation. In order to know the most important factor for effectiveness of VAT in Nepal, respondents were requested to rank their responses on the given choice. The opinion made on this context has been summarized in the table.

In the course of analysis each rank has given some score with it.1 marks has been given to the most important factor and 6 mark to the least one. The rank given to each factors has been presented as under.

**Table 4.25**

**Views on the most important factor for the effectiveness of VAT in revenue collection**

S.N.	Factor	No. of respondents	Score	Percent	Rank
1	Proper implementation	45	190	20.08	5
2	Broad coverage	45	142	15.01	2
3	Tax education	45	76	8.03	1
4	Effective and efficient administration	45	181	19.13	4
5	Clear VAT laws and Regulation	45	157	16.59	3
6	Others	45	200	21.14	6
7		<b>270</b>	<b>946</b>		

Source: - Opinion Survey, 2011

To know the important factor to make the VAT effective a question was asked," what is the most effective factor for the effectiveness of VAT in revenue collection?" The responses provided by the respondents has been tabulated as under

From the above table it is observed that Tax Education is the most important factor for the effectiveness of VAT in revenue collection. The other important factors for the effectiveness of VAT were: Tax education, Broad Coverage, Clear VAT laws and regulation, Effective and efficient administration, Proper implementation and Others, which were ranked 1, 2, 3, 4,5& 6 respectively

Among the others proper billing system and accounting system, effective tax audit and effective monitoring and regulating mechanism are important factors.

#### 4.4.12 Views on Major Problems of VAT in Nepal

To achieve the expected result from the VAT, the problem related to VAT should be settled. First of all, identifications of these problems is necessary and then required effective steps should be taken to settle the problems relating to vat. The major problems may be lack of skilled administrators/manpower, smuggling trade and under valuation of stock, improper billing system, tax unconsciousness on the part of Taxpayer and tax evasion. In order to know the major problems, respondents were requested to rank their responses on the given choice. The result of opinion survey on this context has been summarized in the table.

In case of analysis every rank has some score with it .1marks are given to the most important problem and 6 marks to the least important problem.

**Table: 4.26**

#### **Views on the major problems of VAT**

<b>S.N</b>	<b>Problems</b>	<b>No of respondents</b>	<b>Score</b>	<b>%</b>	<b>Rank</b>
1	Lack of skilled administration	45	165	17.04	3
2	Smuggling and Under Valuation	45	179	18.49	4
3	Improper billing system	45	137	14.15	2
4	Tax unconsciousness of people	45	67	6.92	1
5	Tax evasion	45	203	20.97	5
6	Others	45	217	22.41	6
<b>Total</b>		<b>270</b>	<b>968</b>	<b>100</b>	

Source: - Opinion Survey, 2011

From the above table it is observed that tax unconsciousness people on the part of people are the most important factor. Other major problems observed were improper billing system followed by ranked Lack of skilled administrators/manpower, Smuggling and under valuation Tax evasion and others

Among other geographical barriers is the main problem, weak economic condition and stagnant situation of the country are the notable creating problem for the implementation of VAT in Nepal.

#### **4.5 Major Findings of the Study**

Value added tax played the most significant role to mobilize the revenue in Nepal. In Nepal VAT was introduced in fiscal year 2001/02. Like in any other country, the government of Nepal needs revenue to fulfill the functions of an independent state. Generating revenue means collecting taxes. There are various forms of tax within the systems. Among others VAT is most scientific, innovative and powerful tax which built in quality of universal application for both developed and developing economies.

On the basis of above analysis, some important findings have been drawn and presented as follows:

1. The registrant of tax payers are gradually increasing from 5247 to 46831 in fiscal year 2001/02 to 2009/10. The highest registrants were 8260 in fiscal year 2003/04.
2. The indexes of the revenue (VAT) collection for the implementation year. 2001/02 is Rs 7123 and this trend was slowly increasing. The highest VAT revenue collection was Rs. 21946 million in fiscal year 2009/10.
3. The share of VAT in total GDP is not significant because the ratio of VAT to GDP is 2.46% in 2001/02 and the ratio of VAT to GDP is 3.93% fiscal year 2009/10. It is low percentage; hence it hasn't contributed the major share for the GDP enhancement, through the percentage to VAT in GDP showed an increasing trend over study period.
4. The relation between imports and domestic product are significant positive correlation.
5. The collection of VAT, the comparative study showed that the revenue collection of goods from the imports is higher than domestic products. The share of imports and domestic products are 70.5% and 29.5% respectively in fiscal year 2001/02 but the ratio is gradually changing slowly changed and the

share of import and domestic product reached to 63.28% and 36.71% respectively in fiscal year 2009/10.

6. The collection of VAT revenue in total tax revenue is in increasing trend and share of VAT in total indirect tax revenue is also increasing condition.
7. From the empirical survey it is found that VAT is an appropriate mean of raising government revenue. 93.33% respondents viewed in support of the aspect that VAT is an appropriate mean of raising government revenue and 6.67% respondents went against the view.
8. Most of the respondents are in favor about the view a superiority of VAT to the areas it has replaced as it is 84.44%, 15.56% respondents are against the issue.
9. From the study it has found that VAT billing system is possible, 75.56% respondents see the possibility of billing system. 4.4% take billing system as impossible and 20% take it costly.
10. 73.33% of the total respondents reached to the conclusion that VAT will raise price of the commodities but 26.67% claimed for price increment from VAT.
11. Opinion survey shows that the main problem in the process of VAT implementation is tax collection process. 48.88% respondents take it as a main problem in the process of VAT implementation.
12. Empirical study shows the most effective factors for the effectiveness of VAT is the availability of educational programs relating to VAT. Other factors mainly its proper implementation, broad coverage; effective and efficient administration and clear VAT laws and regulations can play the great role for the effective implementation of VAT.
13. There are so many problems in the environment which are creating the obstacle in the effective implementation on VAT. Lack tax consciousness of people is the main problem. The other problem are improper billing system,

smuggling and undervaluation lack of skilled administrators/manpower, tax evasion etc.

To achieve the potential benefit from the VAT is should be effectively implemented. There are many factors which will increase the effectiveness of VAT. The most important factor for the effectiveness of VAT in revenue contribution is its proper implementation. The other factors such as tax education, clear VAT laws and regulation and broad coverage will also increase the effectiveness of VAT in revenue collection.

According to researcher and interviewed person, many compromises were made in the principles of VAT due to political instability and frequent change in economic slowdown. VAT could not be fully implemented. In our environment where the tax awareness is minimal, the practice of maintaining tax accounts is negligible or improper, smuggling and under valuation is rampant and tax leakages takes place with negotiations between taxpayer and tax administration it was not easy implement Vat and the political instability only aggraded the situation and made it more complex. Until these trends are resolved, there will not be significant VAT collection. The key issues of VAT collection have been eliminate

## CHAPTER-IV

### SUMMARY, CONCLUSION & RECOMMENDATION

#### 5.1 Summary

Taxation and economic development are interrelated. Taxation has an important role in country's economic development. In recent decades, many developments around the world have begun to focus their attention on reforming their poorly designed defective tax structures as an integral part of their development efforts.

The Value added tax (VAT) is a broad based indirect tax. VAT is the most recent innovation in the field of taxation. VAT is the most important tax reform in the 21<sup>st</sup> century as it has already been implemented popularly in more than 125 countries. It is a modern tax system intended when fully implemented to improve the collection of tax, to increase efficiency and to lesser the tax evasion. VAT is multistage commodity and service based tax which is imposed on goods and service at each stage of production and distribution. It is imposed only on good and services at each stage of production and distribution. It is imposed only on value added amount. VAT is not perfectly new form of taxation. It is a commodity based refined form of sales tax.

VAT is the youngest member of sales tax family. Although the concept of VAT was innovated in the year 1919 by Dr. Wilhelm V. Siemoms of Germany but after three and half decades of the evolution of the concept of VAT, France became the first country to put VAT on practice. France introduced Vat in 1954 AD. Then after almost all countries started to take VAT as a best alternative of tax reform process. Because of its special features such as input tax credit system, based on accounting system, less chance of tax evasion, avoidance of cascading and pyramiding effects, it becomes very popular tax system throughout the world. In the context of Nepal, VAT system is completely new system of taxation. Nepalese governments introduce VAT since Nov 16, 1997. Before the implementation of VAT, task force was created in September 1993, with the technical assistance from USAID. But, due to the mid term election 1994, VAT was not implemented as it was suggested by the task force. Then after another task force was formed and it recommended the VAT should be introduced. In earlier stage of VAT implementation there was strong oppositions from the business



community about the implementation of the VAT. But with the follow of time VAT was slowly accepted by the business community. Nepal has adopted destination based consumption type VAT with tax credit mechanism extending right through the retail level. The tax rate is 13% combined with zero on exports with exemption on specified transaction or goods and services. The registration threshold is Rs 2 million (Rs 2 Lacks for imports).

VAT is levied on each level of sales from production and import to distribution of all goods and services except exempt one. But business persons engaged in the sale of goods and services below specified threshold level, it is not mandatory for them to register under VAT. The transaction of tax-exempt goods and services remains outside the purview of VAT. Those dealing in such transaction do not have to fulfill any formalities, including registering under VAT. In case of zero rated suppliers such as export, there is a provision of tax refund of VAT. Such registrants have to collect VAT at the rate of zero percentage on their sales and can deduct the tax incurred on their purchase of imports. In this system, every persons or business firms, which are above threshold limit, should compulsory be registered in VAT office registered persons/business firms get credit facility on tax paid, on their purchases. Purchases pay VAT to the sellers and sellers transfer it to government, deducting g VAT paid on their business purchases.

The first step towards VAT operation is registration of vendor who is legal taxpayers. Each and every registered vendor should received and given the bill while purchasing and selling the goods respectively. Each VAT registrant should keep records of all tax invoices they issue and receive, including the serial number and the data of the invoice, the amount changed and the VAT charged. If a registrant's output tax liability is greater than his input tax credit, he required to limit of out put tax and input tax to the authority with in specified time period. VAT is self assessed tax. Tax payer determines their tax liability themselves and pays tax. If a tax payer doesn't assess is income himself and doesn't file his returns within specified time, he is terms to be a non filer. In such cases, VAT officials may have to make a tax assessment. Penalties are designed to punish tax payer for their VAT officials and to recoup the revenue losses due to the mal-function of tax payers.

The main reasons behind the introduction of VAT in Nepal are to increase revenue mobilization by broadening the tax base to make tax system natural and efficient to establish a fair and transparent tax system and to promote economic growth.

Since the implementation of VAT, it has been generating reasonable amount of revenue despite having too many challenges regarding the implementation of VAT. The tax revenue structure shows that the share of indirect tax in total tax has continuously declined but the share of VAT to indirect tax has been increasing with some fluctuation. VAT contributes more than 40 Percent to indirect tax revenue. Among the major components of indirect tax, the share of custom duty and excise duty are in decline tendency except VAT. Although the amount from VAT revenues has been increasing but it is unable to achieve its potential. The reasons behind this are various problems relating its implementation. But another positive factor is that there is increment in the tax registrants' year by year. Although it is the eight year of VAT implementation the problems relating to VAT are yet to be eliminated. Billing system being the back bone of VAT system, the main problem lies on the proper invoicing system. Lack of required number of qualified and trained tax administrations is another problem. Other problems relating to the effectiveness of VAT are lack of awareness about VAT on different groups of people, existence of rampant corruption, smuggling and under valuation, narrow tax payer and tax collector and between different department of government, lack of courage to take accountability by different groups etc.

To avoid above challenges major steps are required to get positive effective from VAT system. To enhance its revenue collection there is a need to establish proper accounting and invoicing system. Tax administrators, tax payers and consumers need to be educated about VAT system. If we can tackle the challenges relating VAT then there must be great improvement in revenue collection from VAT.

## **5.2 Conclusions**

Every country of this world wants to get better economic development. To get the pace of economic development it is essential to have sufficient revenue generation, particularly tax revenue plays the great role for development of nation's economy. To achieve higher growth of revenue, every country needs to reform some of its tax

system. In the context of present world VAT is one of the best alternatives of tax reform process. In the process of tax reform, Nepalese government adopted VAT by replacing four other tax system i.e. sales tax, hotel tax, contract tax and adoption of v is that is broadens the tax base which increase revenue mobilization, system is transparent and discourage tax evasion. VAT is the most innovative, scientific and powerful tax with built in quality of universal application for both developed and developing economics. Being a developing country facing great shortage of revenue, Nepal adopted VAT because VAT is revenue buoyant and highly instrumental for resource mobilization.

VAT eliminates various defects of sales tax by replacing it such as pyramiding and cascading effects. Other sources of taxation are not able to get required level of revenue generation. So, implementation of VAT for Nepal is both a compulsion and necessity. VAT is a broad-based indirect tax. Nepal has adopted a destination based consumption type VAT with tax credit mechanism extending right through the retail level. Being consumption based indirect tax it does not maintain equity norms but VAT is the best alternative to get more amount of revenue.

In the Nepalese context the trend of revenue contribution is fluctuating but the amount has been increasing reasonably. It is only the seventh year of VAT implementation but the revenue collection from Vat is not that bad. Theoretically VAT is the best alternative to gain high revenue collection. But practically it depends on its environment where it exists to get the potential target from VAT the environment relating to VAT must be as required. It is only the preliminary stage of VAT implementation in Nepal so the revenue collection from VAT is not as high. If the government can make the people educated and conscious then we can remove the minimizing factor regarding the better implementation of VAT. First of all the system must be effective. There are certain elements which increase the effectiveness of VAT. Availability of clear VAT laws and rules, effective and efficient administration, honest tax payer, a good education programme, establishment of proper invoicing mechanism and extension of tax coverage are the most important factor which obviously increase the revenue mobilization through VAT and effectiveness of VAT can be achieved. The government needs to have that particular mechanism to control and monitor the different practical aspects relating to VAT. The government needs to

be creative to take actions against those who are acting against the proper effectiveness of VAT.

In conclusion if properly implemented VAT can able to contribute towards the economic development of any country.

### **5.3 Recommendations**

The implementation of VAT has not devoid the challenge yet. To establish this tax on a completely successful scale and to make it a part of the daily of the people requires much bigger efforts than what we have now.

Nepal has been undergoing through server fiscal crises due to limited sources of revenue and increasing government expenditures. The trend of 9 years (2001/02 to 2009/10) shows revenue expenditure gap. The country is heading toward debt trap situation. In the wake of such a crisis Nepal has adopted VAT.

According to interviewed person and researcher, to overcome the major challenges faced in the implementation of VAT. The following measure could be adopted.

1. A collection strategy needs to be developed and implemented effectively in order to collect the increasing amounts of arrear. To improve billing condition in the market needs regular supervision, audits and investigation. Consumer education is required to promote the use of invoice.
2. While the design of the returned system is good, it has not been implemented properly. It is necessary that the refund procedure be implemented in a timely and proper manner and that both taxpayer and tax official be educated on the procedure to prevent any misuse of the refund procedure.
3. Awareness program on VAT about value added tax should be carried out so that consumer may become aware of the tax. Recently the government has introduced a lottery program to encourage demanding invoice during purchase. All conscious citizens should be alert and aware regarding these facts.
4. The fragile political situation should be ended for economic development , peace and mandatory
5. For effective implementation, big responsibilities remain with the shoulders of tax administration. Therefore the administration has to implement this tax in

the right spirit of VAT. In depth training must be provided to tax officials to expertise them in the field of taxation

6. To establish VAT invoices in the form of a campaign, college students could be hired and mobilized. This could provide the student part-time employment and also enhance publicity. It would be appropriate to mobilize such students to find out the status and presences of VAT in the market. If group of students are placed in busy market places, it creates psychological pressure on the vendors to issue invoices. Similarly, they could be also used to collect information on various issues of VAT.
7. To make VAT effective and transparent, unnoticed inspection on the road of goods being transported from time to time would discourage incorrect business transaction. Unreal business transaction should be banned to promote real business.
8. It is essential to widen the base of the domestic commodity tax system and increase revenue mobilization. The VAT administration should expand audit and investigation activities in order to identify and remove artificial credit.
9. To make VAT effective, it is essential to create an environment in which invoices are issued properly, accounts are maintain accurately, tax is based on transaction, there is acceptance of the taxpayer correct accounts and a fair competition among industrialists and businessmen should be established.
10. The proper co-ordinations among various Government departments involved in revenue collection must be maintained.
11. Computer networking system should be established in all the customs point with department so that related information can be accessed to all the concerned officers for the access of international price.

VAT would definitely help to increase revenue collection of Nepal, if implemented properly. The present situation of VAT shows that the system need for understanding and commitment at the political level and administration level.

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**ANNEX - I**

**Interview schedule**

**“A study on contribution of Value added tax in tax revenue in Nepal”**

***Questionnaire***

**Dear sir/madam,**

I, Mr. Dipesh Subedi, student of Central Department of Management, is going to conduct a research entitled “Contribution of Value Added Tax to Total Tax Revenue in Nepal.” This is purely a academic research for the partial fulfillment of the requirement for MBS. So, I request you to fill up the questionnaire.

**Respondent’s Details:-**

Name	Profession
Sex	Address

Please provide your opinion on VAT. Number one is for the most important rank and the last number for the least important rank.

1. Are you familiar with VAT?  
a. Yes                      b. No
2. Do you take the VAT as on appropriate mean of raising the government revenue?  
a. Yes                      b. No
3. If yes, why?  
a. Broad coverage    b. Control Tax evasion    c. Proper implementation    d. Stop illegal trade    e. All the above
4. If not, what are the appropriate mean?  
a. Sales tax            b. Contract tax            c. Entertainment tax            d. Excise duty            e. if any others (please specify).....
5. Is VAT superior than other types of sales tax?  
a. Yes                      b. No

6. If yes why?

- a. Increase revenue collection
- b. Facility of refund
- c. Facility of tax credit
- d. all the above

7. If not, which is the superior than vat?

- a. Sales tax
- b. Contract tax
- c. Entertainment tax
- d. Excise duty
- e. Export/Import duty
- f. If any others (please specify).....

8. What is your view about billing system?

- a. possible
- b. Impossible
- c. Costly

9. Will price rise due to VAT system?

- a. Yes
- b. No

10. If yes, how it raise the price?

- a. Compliance cost
- b. High profit
- c. Non awareness of consumers
- d. All the above

11. If not, why?

- a. Billing system
- b. Tax education
- c. Control the tax evasion
- d. Clear vat law and regulation
- e. All the above

12. What kind of problem has risen in the process of VAT implementation in Nepal?

- a. Registration
- b. Collection
- c. Tax refund
- d. If any others (please specify).....

13. What is the most important factor for the effectiveness of VAT in revenue collection? (Answer on 1 to 6 measurement scale)

- a. Proper implementation
- b. Broad coverage
- c. Tax education
- d. Effective and efficient administration
- e. Clear VAT laws and regulations
- f. If any others (please specify) .....

14. What are the major problems of VAT in Nepal? (Answer on 1 to 6 measurement scale)

- a. Lack of skill manpower
- b. Smuggling on under valuation
- c. Improper billing system
- d. Tax unconsciousness of people
- e. Tax evasion
- f. If any others (please specify).....

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

- a. Yes
- b. No

Thank you very much for providing your valuable time and suggestion.

## ANNEX - II

### List of VAT exempt goods and services

1. Basic agricultural products
  - a) Paddy, rice, wheat, maize, barley, millet, pulses, flour, and similar unprocessed food materials.
  - b) Green and fresh vegetables, fresh fruits, fresh eggs and similar products (except used in hotels, restaurants, bars, guest houses, cafeteria and other similar organizations).
  - c) Unprocessed cereals, (such as sugarcane, tealeaf, tobacco, cotton, cardamom, jute, oilseeds, and soybean).
  - d) Herbs.
2. Goods of basic needs.
  - a) Unprocessed edible oil.
  - b) Piped water, including water supplied by tankers.
  - c) Fuel wood and coal.
  - d) Kerosene.
  - e) Salt.
3. Live animals and animal products.
  - a) He goat, sheep, yak, he buffalo, bore, pigs, rabbit, and similar other animals; their fresh mil, and uncooked/unprocessed varieties.
  - b) Cows, she buffalo and she goat.
  - c) Ducks, hens, cocks, turkey and similar other/birds and other fresh meat, eggs and similar uncooked varieties.

d) Fresh or dried fish (other than packed).

4. Agricultural inputs.

a) Seeds of any plants listed in group I.

b) Manure, fertilizer and soil conditioners agriculture hand Implements.

c) Pesticides made mainly for use of crops.

d) Agriculture equipment, including tractors.

e) Birds and animal feed.

5. Medicine, medical and similar health services.

a) Medical or surgical services provided by government institutions.

b) Human blood and products derived from human blood.

c) Human or animal organs or tissue for medical research.

d) The supply of services by persons on the register of veterinary surgeons and veterinary doctors.

e) The supply of goods made for and suitable only for the use of disabled persons.

f) X-ray film and oxygen gas to be used for treatment.

g) Raw materials purchased or imported by the drug industries to the extent approved by the department of drug management.

6. Education

a) The provision of research in a school or university.

b) The provision, otherwise than for profit, of professional or vocational training or refresher training.

c) The provision of education in a school or university and supply of goods made in connection with such services.

7. Books, Newspaper etc.

a) Books, newspaper, newsletter and periodicals.

b) Newsprint.

8. Artistic and cultural goods and services, carrying services.

a) Painting, handicrafts, carving and related services.

b) Cultural program.

c) Admission to libraries, archeology, museums, zoos and botanical gardens.

9. Personal or professional services.

Air transport, on-tourist passenger transportation: except cable car and goods carrier except transportation related to supply.

10. Personnel or professional service.

(Personnel services rendered by artists, sportsmen, authors, writers, designers, translators and interpreters institutionally or individually).

11. Other goods or services.

i. Postal services (provided by HMG only).

a) The service of conveyance of letters, money and postal packets by the post office.

b) The supply by the post office of any service in connection with the conveyance of letters money and postal packets.

c) Postage stamps.

ii. Financial and insurance services.

iii. Bank notes, and cheque books.

a) The printing and issue of bank notes.

- b) The supply of bank notes from outside the kingdom of Nepal to the kingdom of Nepal.
- c) Cheque book.
- iv. Gold and silver.
  - a) Gold, gold coins and gold ornaments.
  - b) Silver and silver coins (other than ornaments and goods made of silver).
- v. Electricity.
- vi. Raw tool.
- vii. Battery operated tempo, their chassis and battery.
- viii. Biogas, solar power and wind power operated power generation plant and their main parts on the recommendation of the alternative energy center.
- ix. Aero plane, helicopter, fire brigade and ambulance.
- x. Jute goods.
- xi. Industrial machinery included in section 84 of customers' tariff and subject to 5% tariff.
- xii. Woolen carpet & woolen carpet weaving, dying, washing, knitting.
- xiii. Aluminum, cooper, scrape, circle, plate and utensils.
- xiv. Cotton sadi, lungi, dhoti, gamcha.
- xv. Cotton yarn.
- xvi. Woolen yarn to be used in hand knitting sweater (except artificial & acrylic) domestically.
- xvii. Donated goods received for calamities or philanthropic purpose approved by Ministry of finance.



12. Land and building.

Purchase and rent of land and building (except the rental service provided by hotels, guesthouses or similar organization).

13. Betting, Casino, Lotteries.

a) The provision of any facilities for the placing of bets or the playing of games of chance.

b) Lottery.