

CHAPTER- I

INTRODUCTION

1.1 Background of the Study

An isolated, agrarian society until the mid-20th century, Nepal entered the modern era in 1951. The country has, however, made progress toward sustainable economic growth since the 1950s and is committed to a program of economic liberalization.

Nepal has used a series of five-year plans in an attempt to make progress in economic development. Planned economic development began in 1953. It completed its tenth economic development plan in 2007, July.

Under the tenth plan, to run until 2007/08, priorities have shifted to security and poverty reduction, but with a renewed emphasis on privatization and the effort to encourage private investment.

Currently Nepal has formulated periodic three years Interim Plan from fiscal year 2007/08.

The following policies will be taken in this interim plan to create favorable impact on domestic revenue mobilization:

-) The system of collecting and mobilizing taxes will be made transparent and simple by reviewing existing tax system and acts.
-) Revenue leakage will be controlled by strengthening revenue administration capacity.
-) Value Added Tax system will be made more effective.
-) The tax base will be gradually broadened.

-) Customs rate and other tax systems will be adopted in line accordance with Nepal's commitment to international and regional organizations like World Trade Organization, and SAFTA.
-) Domestic revenue mobilization will be strengthened by broadening existing tax base.

In 2009/10, revenue mobilization of the government increased significantly by 25.4 percent to 101.9 percent of annual budget estimate which was Rs. 179.95 billion. The revenue had risen by 33.31% and in amount by Rs. 35852 million in 2008/09. A positive impact of "Tax Compliance year", increase in PAN number holders, mobilization of tax volunteers, growth in imports, control in revenue leakages and tax administration reforms mainly contributed to such an increase in the revenue mobilization.

Of the total revenue mobilization, VAT revenue grew by 33.15 percent and in amount Rs. 9885.2 million in 2008/9. Such revenue had increased by 14.26 percent in the previous year. The increase in VAT revenue was on account of growing imports and consumption induced by an increase in the inflow of remittances and reforms in VAT administration.

In 2009/10, customs revenue rose by 31.6 percent and in amount Rs. 35.3 billion compared to an increase of 34.4 percent in the previous year. Reforms in custom administration increase in imports of high tax yielding vehicles and spare parts and increase in the amount of Indian excise refund contributed to such a high growth of customs revenue.

Income tax revenue increased by 22.4 percent and in amount Rs. 33.65 billion in 2009/10 compared to an increase of 43.9 percent in the previous year. A positive impact of tax compliance year and increase in PAN number holders accounted for such an increase in the income tax revenue mobilization.

In the review year, excise revenue increased by 49.6 percent and in amount Rs. 24.31 billion compared to an increase of 44.9 percent in the previous year. Reforms in excise administration and increase in the imports of high excise tax yielding light vehicles accounted for such a growth of excise revenue in the review year.

Among the components of revenue in 2009/10, VAT constituted a share of 29.7 percent followed by income tax (18.7 percent), customs duties (19.5 percent), and excise duties (13.5 percent). In the previous year, such compositions were 27.6 percent, 19.2 percent, 18.6 percent and 11.3 percent respectively.

A nation requires sufficient funds to carry out development plans, handled day to day administration, maintain peace and security and lunch other public welfare activities. A fund required by the government is normally collected from two source internal sources or external sources. The internal revenue of the government comes basically from two sources tax and non-tax.

Among internal resources taxation is a prime factor it is the pillar of the fiscal policy. It is the backbone of the welfare state and government most imposes taxation to finance various welfare and social services like education, health, electricity, transportation, communication etc (Kadel, 2003).

Among various taxes, income tax plays an important role in tax revenue. Income tax is imposed on those activities contributes to wards the creation of wealth is created with the help of labor, capital& labor activities that generate income from employment, investment and business. Being a developing nation, Nepal still has been unable to maximize the collection of income tax the important of income tax has been increasing day by day and it has not only remained a sources of revenue for emergency but has become a regular sources of income for government (Bhattarai & Koirala , 2003).

Income tax is collected from various sources of profit and income. It is collected from public enterprises, semi-public enterprises, private corporate bodies, individuals etc. in other words income tax is collected either direct or indirect.

1.2 Statement of the Problem

For the overall development of the country Economic development is the prime concern. The challenges to Nepal's economic development are formidable. These include limited natural resources, difficult topography, poor infrastructure, landlocked location, weak human capital (with both low levels of education and health), poor public management, and a long history of political interference in the economy. The majority of people have not been able to get even basic facilities. Nepal's economy is characterized by a high vulnerability to shocks, natural and man-made. Its growth has been arrested since 2001, and with a per capita income \$562, it remains one of the world's poorest countries. It remains to be seen whether its economic reform programs will be swept away, or prove to be built solidly enough to weather the passing storms.

The government wants to fulfill the basic needs of the people and accelerate development activities one at a time thus; every nation of the world is

accomplishing various activities to fulfill these objectives. It needs huge amount of capital. Despite the various measures adopted by the government to boost revenue collection there is still a subset entail resource gap between expenditure and revenue. The rate of government expenditure is exceeding the rate of growth revenue almost every year. In other words Nepal has been facing persistent budget deficit from the beginning of her development phase. External deficit, Currency depreciation, in factionary pressure, rising interest rates which may cause crowding out effect and reduction in economic growth are the consequences of the budget deficits. The mobilization of revenue has not increase to level in which level in which level and speed at our expenditure is rising. Raising the government revenue helps to overcome from the serious bottleneck of resource gap in the process of economic development programs by mobilization additional resources from domestic sources.

Government finance sector was also negatively affected by the past conflict and political instability. Government revenue was affected because tourism, industry and business as well as other income generating sectors could not expand activities due to conflict.

Similarly, the task of collecting revenues has become challenging due to lack of development of tax-paying culture among individuals and institutions that can pay taxes.

Income tax is one of the component of taxation and major sources of government revenue. Income tax in developing nations has been regarded as an instrument of growth and social justice. But Nepal Government is being unable to mobilize the expected income tax from personal as well as corporation. Most of the personal tax payers do not reveal the income sources

even they earn significant amount. Similarly, many research reports have addressed that tax evasion has become a serious problem as a result the actual collection of income tax is being very low. So, the role of corporate income tax revenue is justifiable. But the performance of corporate sector, specially the industry is very poor. Their number, profitability investment in fixed assets share in market transaction is all in weak position. There is no agreement as regards to various issues in corporate tax area. The debate is going on as regards to base of tax, method of taxing corporation, method and rate of depreciation, use of appropriate type of tax incentive, treatment of tax inflation. Such problem is developing countries generate more direct tax and less indirect but in developing countries generates more indirect tax and less direct tax etc.

Besides the above problem, the study addresses the following research questions.

1. How direct & indirect taxes are contributing to national revenue?
2. What are the structures of direct and indirect taxes?
3. How corporate tax is contributing to national revenue?
4. Which are the important factors that influence on effectiveness of income tax in Nepal?

1.3 Objectives of the Study

Each country has its own tax system; different taxes collected by government are used for providing public services. Main objective of the study is to analyze the contribution of direct tax and indirect tax to national revenue of Nepal. Other specific objectives of the study are listed below.

1. To analyze the contribution of direct tax and indirect tax to national revenue in Nepal.

2. To analyze the structure of direct and indirect taxes.
3. To analyze the contribution of corporate tax to national revenue of Nepal.
4. To identify the most important factors influential on the effectiveness of income tax in Nepal.
5. To provide suggestions for effective collection of direct and indirect taxes in Nepal.

1.4 Significance of the Study

Nepal is an agro-based developing country with low speed in industrialization process. There are only a limited number of corporate bodies and their economic performance is very dismal so, there is need to growth and development of corporate sector in our nation the government needs huge amount of funds to spend on daily expense as well as development activities. Every year, Nepalese has been presenting deficit budget, there is increment in resource gap. Most of the development activities depend on bilateral and multilateral grants and loans the nation is hardly bearing the loan and the internal sources of revenue is not sufficient event to meet the ordinary expenses. In this context the easy and long lasting way to increase revenue to strengthen the internal source is through income tax in which corporate income tax is one of the major components. Thus, a comparative study contributes direct tax and indirect tax to national revenues of Nepal has been chosen as a relevant topic for the study.

The study is useful to economist planners, tax officers, tax administrators, government and other in arrested person about the contribution of corporate sector in internal resources and the problem and prospects of corporate

sector. It also provides the information about trends projection of corporate income tax.

1.5 Limitations of the Study

The study has the following limitations:-

1. The study is based on secondary data the reliability depends on it.
2. Some primary data also has been taken into consideration.
3. Main focus is given to direct and indirect taxes of Nepal.
4. This study has been conducted to fulfill the requirement of the MBS programs.
5. Due to the constraint and other difficulties, field survey was done in Kathmandu.
6. Major data have been used this study, secondary data, primary information gathered from tax office, various web sites.
7. Monetary policy has published only 11 months data up to Jestha 2067 therefore we taken data up to 2065/66
8. All the data, percentage are calculated in Microsoft Excel, there be remain some rounding errors due to computerized system.

1.6 Organization of the Study

The entire study has been designed into five main chapters. They are:

1. Introduction
2. Review of literature
3. Research Methodology
4. Presentation and analysis of data

5. Summary, conclusion and recommendation.

The first introduction chapter includes statement of problem objectives of the study, need and significance of the study, limitation of the study and organization of the study.

The second chapter Review of literature is done to know what researches had been done in the related topic in previous days and what is to be done at present or in future. This chapter has been divided into two main aspects (1) Conceptual framework and (2) Review of related materials i.e. review of books, review of thesis of newspapers, magazines, journals etc.

Research methodology is mentioned in the third chapter it includes research design population and sampling, sources of data, procedure of data collection and tools used for analysis.

Presentation and analysis of data have been made in the fourth chapter the data collected from various sources have been tabulated in thesis sequential order and data have described, analyzed and projected with statistic too as well as general accounting and taxation principle.

The fifth chapter consists of brief summary conclusion and recommendation of the study. Lastly essential appendices and bibliography have been presented at the end of the study.

CHAPTER-II

CONCEPTUAL FRAMEWORK AND REVIEW OF LITERATURE

2.1 Conceptual Framework

2.1.1 Introduction

Income is the consumption and savings opportunity gained by an entity within a specified time frame, which is generally expressed in monetary terms. However, for households and individuals, "income is the sum of all the wages, salaries, profits, interest payments, rents and other forms of earnings received in a given period of time." For firms, income generally refers to net-profit: what remains of revenue after expenses have been subtracted. In the field of public economics, it may refer to the accumulation of both monetary and non-monetary consumption ability, the former being used as a proxy for total income.

Economists define the term income in a broad sense. It is an economic gain or receipt to a person during a particular by way of wages, interest, profit and rent. The money income of the people is generally used for two purpose part of income is spent on consumption and part is saved this definition can be pressed in the formula as follows.

$$Y=C+S$$

Where,

Y=income

S=saving

C=consumption

But for the purpose of taxation the definition of income is somehow different from the aforesaid definition. A fee charged ("levied") by a government on a product, income, or activity.

According to income tax act, 1974(2031)" income means the income earned or received in cash or kind from the sources mentioned. They were as follows:

[ITA, 1974]

1. Agriculture
2. Industry, Business, Profession or Vocation
3. Remuneration
4. House and land rent
5. Other sources.

The exiting income tax Act, 2002 (2058), which has been enacted since 2058 chaitra (First, April, 2002) has defined income in section 2/a as person's income from any employment business as calculated in accordance with this act (ITA, 2002). It includes all sorts of income received for the provision of labor or capital or both of whatever form or mature in the taxable income.

Tax is in simple terminology, a liability to pay an amount to the government. It is a compulsory contribution to the national revenue from the tax payer according to law. In the word of Seligman, taxation is the compulsory contribution from a person to the government to destroy expenses in curried in the common interest of all without reference to specific benefit conferred"

Income tax refers to the levied on the income of a person and profit of corporation for the specific time period particularly one year. Income tax is levied on the taxable income of a person or a company after, deducting allowable expenses. According profits may differ from taxable profits for the computation of taxable income, generally incomes are added and expenses

are subtracted and losses, which are allowed to deduct under the provision of income tax act are also subtracted then.

2.2 Tax

To tax (from the Latin taxo; "I estimate", which in turn is from tangō; "I touch") is to impose a financial charge or other levy upon a taxpayer (an individual or legal entity) by a state or the functional equivalent of a state such that failure to pay is punishable by law.

The purpose of taxation is to finance government expenditure. One of the most important uses of taxes is to finance public goods and services, such as street lighting and street cleaning. Since public goods and services do not allow a non-payer to be excluded, or allow exclusion by a consumer, there cannot be a market in the good or service, and so they need to be provided by the government or a quasi-government agency, which tend to finance themselves largely through taxes.

2.2.1 Meaning of tax

Tax is compulsory contribution from people to government to undertake work of public good. Many tax experts have given the definition of tax in their own words. They have focused the different aspect of tax according to their own view.

A tax may be defined as a "pecuniary burden laid upon individuals or property owners to support the government a payment exacted by legislative authority." A tax "is not a voluntary payment or donation, but an enforced contribution, exacted pursuant to legislative authority" and is "any contribution imposed by government whether under the name of toll, tribute, tillage, gable, impost, duty, custom, excise, subsidy, aid, supply, or other name."

According to Prof. Seligman “tax is compulsory contribution from a person to the government to defray the expenses incurred in the common interest of all without reference to special benefit conferred (Dhakal, 2000: 1-2).

According to Plehn, “taxes are general contribution of wealth levied upon persons, natural or corporate to defray expenses incurred in conferring common benefit upon the resident of the states” (Dhakal, 2000: 20).

According to Layer. “A tax is a compulsory payment to the government without expectation of direct benefit in return to the payer” (Amatya, 2003).

From the above definitions it is clear that tax is imposed on the person by the government according to the law of the country the person on whom tax is imposed must pay taxes. Otherwise the law punishes him. The government doesn't provide any corresponding benefit to the tax payer for the amount of tax he pays. It is used for the common goods of the country. This means the government of the amount of tax paid by tax payer provides no special benefit.

2.2.2 Classification of Taxes

Economists have classified taxes into several categories. The major categories of may be

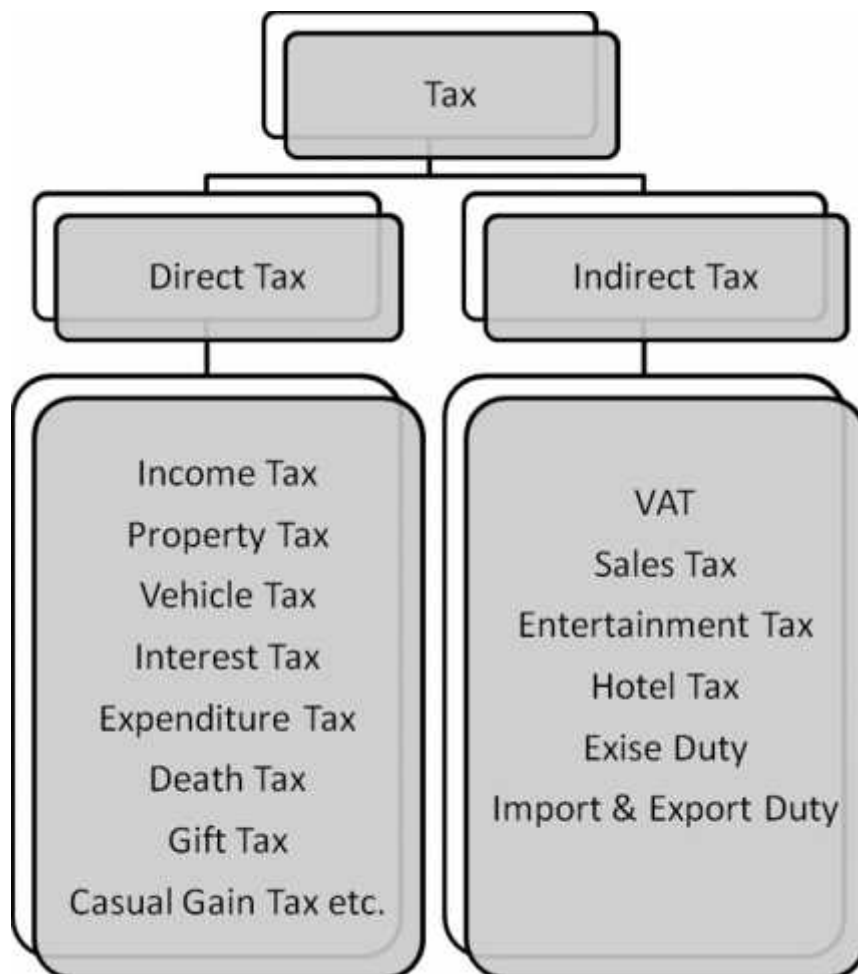
-) Direct taxes and indirect taxes
-) Progressive taxes and proportionate taxes
-) Regressive taxes and Digressive taxes.
-) Single taxes and multiple taxes etc. However, taxes are broadly classified into direct taxes and indirect taxes

Direct taxes and indirect taxes

If tax is levied directly on personal or corporate income, then it is a direct tax.

If tax is levied on the price of a good or service, then it is called an indirect tax.

Some of the example of Direct and Indirect Tax



Progressive taxes and Proportionate taxes

Progressive tax is a tax system in which those who earn higher incomes pay a higher percentage of their income than those with lower incomes.

Proportionate tax is an income tax that takes the same percentage of income from everyone regardless of how much (or little) an individual earns.

Regressive taxes and Digressive taxes

Regressive Tax is actually a form of tax where the tax rate decreases as the amount subject to taxation increases. There is an inverse relation between the tax rate and the ability of the taxpayer to pay the taxes, thus the burden of taxes is on the poor.

On the other hand, Digressive Taxes are a mixture of progressive and proportional tax system. The structure of Digressive Tax is such that the tax rates increase till a point and after wards a simple uniform tax rate is charged. The tax rate does not increase in same proportion as compared to the increase in income.

Single taxes and multiple taxes

Single tax system means only one kind of tax. The single tax might be proportional, progressive or regressive. It may be for a single fixed amount.

Multiple tax system means a tax system comprising several types of taxes. They may include both direct taxes and indirect taxes.

2.2.2.1 Direct tax

The direct tax whom it is legally imposed cannot be transferred to other i.e. in direct tax the person paying and bearing the tax is same.

In the general sense, a direct tax is one paid directly to the government by the persons (juristic or natural) on whom it is imposed (often accompanied by a tax return filed by the taxpayer). Examples include some income taxes, some corporate taxes, and transfer taxes such as estate (inheritance) tax and gift tax.

According to Dr. Dalton "A direct tax is really paid by the person on whom it is legally imposed (Amatya, 2060:2).

Advantages of Direct Tax

-) It is equitable as it is imposed on person as per the property or income.
-) In the direct tax, contribution in tax on the basis of his earning so it is certain
-) Since the tax payers know his contribution in the tax his consciousness increases to the expenditure of the government.
-) Tax rates are classic and can be adjusted as per the fiscal requirement of the country when there is need of more revenue government can impose high is low the tax rate can be minimized.

Disadvantages of Direct Tax

-) It gives the mental pinch to the tax payers due to curtain down of their incomes and properties.
-) Taxes should be pain in advance on the estimation of the future income. Tax rate is also higher than indirect tax so tax payers feel inconvenient.
-) The tendency of the evasion increases in the direct tax system because no one wants to cut down his or her incomes without the corresponding benefit.
-) The tax payers are limited in direct tax so the direct tax lacks mass participation.
-) Most of the earning has to pay to government in the firm of the direct tax. So, it discourages saving and investment.
-) It is expensive for the government to collect tax individually.

2.2.2.2 Indirect Tax

The indirect tax on which it is legally imposed can be transferred to other, which means in dire tax the person paying and bearing tax is same.

In the colloquial sense, an indirect tax (such as sales tax, value added tax (VAT), or goods and services tax (GST)) is a tax collected by an intermediary (such as a retail store) from the person who bears the ultimate economic burden of the tax (such as the customer).

According to Dr. Dalton “An indirect tax is imposed on one person but paid partly or wholly by another” (Amatya, 2065).

Advantages of Indirect Tax

-) There is less chance of tax evasion as the tax payers pay the tax collected from consumers.
-) Indirect tax is convenient to pay. It is charged services consumed by the consumers taxes are included in the price of goods and services so the tax payers do not feel that they are paying taxes.
-) Each and every consumer has to pay taxes while consuming the goods and services. So, there is mass participation of the tax payers in the indirect tax system.
-) Indirect tax is important tool for the checking of the consumption of the harmful goods and services by imposing the higher tax in the consumption of the harmful products like liquor, tobacco etc. can be reduced.
-) In the direct tax the change of the tax exaction is very much lower in compare to the direct tax because even the tax payer does not feel that he is paying tax.
-) Indirect tax is elastic in nature. In is an important tool of the government to apply its fiscal policy.

Disadvantages of the Indirect Tax

-) There is uncertainty of government revenue from indirect tax variation of demand in goods and services differ the government revenue.
-) It is not equitable to leave taxes on basic goods because the haves are not able to pay taxes in comparison to haveless.
-) Indirect taxes have bad effect on consumption, production and employment because higher tax increases the cost of goods and services. As a result, consumption decreases and industries slowly begin to decline, employment decreases and ultimately the economy of country declines.
-) Consumers do not know that they are paying taxes. So, they lack consciousness regarding the use of the public revenue.
-) The agent may not report to the government. Thus, there may be the change of consumer exploitation.

2.3 Review of Related Materials

In the course of the study various books articles, dissertations and other reference materials were reviewed. Some useful ones are mentioned below.

2.3.1 Review of Books and Articles

In 2003, Mr. Girija Prasad Koirala and Mr. Ishwor Bhattarai published two books. The first one is for BBS 3rd year named "Taxation in Nepal". The second one is for the BBS 2nd year named "Tax laws and tax planning". Both books have shown how taxable incomes have computed unclear employment business and investment sources.

In 2003, Mr. Surendra Keshar Amatya, Dr. Bihari Binod Pokharel and Rewant kumar Dahal wrote a book entitled "Taxation in Nepal". This book is also designed to meet the requirement of BBS 3rd year syllabus. Theoretical as well

as practical aspects of taxation have been included in the book. This book is a descriptive one, not analytical.

In 2003, Dr. Puspa Raj kadel published two books named 'Tax laws and Tax planning and second one was 'Nepal ko Bartaman Kar byabastha'. This book has been designed to the syllabus of BBS 3rd year. Theoretical as well as practical aspects of taxation have put in his book.

In 2004 Mr. Jagadish Agrawal has published a book entitled, "Income tax, theory and practice," this book has focused on the students of chartered accounts and taxation. This book has also focused to be a practicenor reference and handbook, rather than the cortical compilation on the subject. His book is not only based on description fact but also has interpreted the various provision of the new act. Some sections of ITA 2058 act have compared with the international act have compared with the international accounting standard.

Pant (2004), had written and article entitled "problems in tax administration and their remedies" published in journal of finance and development 'Rajaswa'2004, April vol1. He had comprehensively explained about the problems and their remedies related with tax revenue and major types of practical problems and challenges in tax administration. He had mentioned in his article were showing limited amount of transaction showing low selling price, lack of issuing and taxing bills, lack of showing the real factory cost, commercial trend, lack of co-operation in tax auditing, legal ambiguity in implementation and lack of coordination between inland Revenue Department and Revenue investigation unit. Meanwhile, he had recommended some valuable suggestions to solve the problem and to overcome the challenges. They were statistical and information system should be properly managed, fixed norms and standards should be used to assess selling price and factory cost, the billing should be made compulsory,

coordination between inland Revenue office with various entities of Government Revenue Investigation Department and its related unit should play the important role and auditing on the topic “corporate tax structure and production” in 1993 which prepared by Jeffrey Bernstein and Anwar Shah. They had conducted their research taking Mexico and Pakistan as a sample. As per their investment tax credits investment allowances and accelerated capital consumption allowances were most effective promoting investment then more general tax incentives such as corporate tax rate reduction from that research they reached the summery and conclusion in the elasticity of rental rate of capital stock and in the benefit-cost ratio.

In 2006 Mr. Surendra Keshar Amatya wrote an article entitled “Taxation of employment income in Nepal, concept, computation and contribution” in PRAVAHA, A Journal of Management Vol.16,July 2006. He has mentioned about Nepalese income Tax law, income year and assessment year, sources of income, concept and sources of income, concept of employment, computation of income from employment non chargeable incomes under employment common reductions income tax exemption assessment of income tax liability on employment income, surcharge and contribution of employment income to Tax revenue of Nepal. He has also shown about estimation and collection of employment income tax during the past decade. In this study he has clearly pointed that actual collection of employment tax is satisfactory.

Norregard,John &Khan, Techmina S. (Dec 2007), Tax policy; Recent Trends and coming Challenges. (IMF working paper)

This paper provides an overview of the key economic factors that shape tax policy reform in many high incomes. Countries, developing countries or transition economies. The paper describes and evaluates global and regional development with respect to tax rate and revenue ratios owner the last some

20 years, and discusses selected structural reform initiatives that have been high on the policy agenda over this period. In particular, it focuses on developments relating to experiments with the restructuring of corporate tax, the impact of corporate taxes on IDI key reform initiative that have been high on the policy agenda. Over this period in particular it focuses on developments relating to experiments with the restructuring of corporate tax, the impact of corporate taxes on IDI, key reform initiatives including dual income taxes and flat taxes, as well as the world wide spread of the VAT and policy development associated with climate change and natural resource taxation.

In 2007, Mr. Jit Bahadur K.C. wrote a book entitled “Tax Laws and Tax planning” for MBS second year. He has presented practical as well as theoretical aspects on taxation in this book. This book is useful to any one who is interested in the subject of taxation. This book is also useful to research work.

In 2008, Dr Kamal Deep Dhakal had written an article entitle “Historical perspective on income tax in Nepal” this article has describe previous income tax act and shown main fatigue of income tax act 2058 are a follows:

-) Provision of set and carry forward of losses.
-) Classification and pooling of depreciable Assets.
-) Tax on capital gain
-) International taxation
-) Medical tax credit
-) Withholding payment and quantification allocation and characterization of the amounts:

2.3.2 Brief Review of Previous Research Work

Chalise Rabindra (2007) conducted a research entitled “*A Study On Contribution Of Income Tax To Government Revenue*” **Mr. Chalise** had concerned his study to analyze the effect/impact of income tax evasion on government revenue of Nepal. It was submitted to *Shankar Dev Campus, TU*, and Kathmandu at December 2007.

The specific objectives of the study were:

-) To study the historical development of income tax in Nepal.
-) To analyze/view the structure of government revenue and position of income tax.
-) To identify the ways and causes of income tax evasion in Nepal.
-) To make suggestion and recommendation for the elimination of income tax evasion.

His major findings are as follows:-

-) Nepal has been suffering from capital shortage to accelerate the economic growth. A lot of funds are needed to meet additional financial requirement for the development activities of country
-) Nepal has been heavily relying on foreign loans and grants. Internal resource are preferable for sustainable economic development, thus fiscal deficit of Nepal has been increasing.
-) Income tax is one of the A Study on Contribution of Income Tax to Government Revenue most important resource of public revenue and it is considered as a good remedy to cure growing resource gap problem of Nepal.

His main recommendations were:

-) Government should try to reduce resource gap by increasing internal revenue and subsidies likewise government should only take the Foreign

loan for production sector or purposes which has high revenue generating possibility.

-) The income tax policy should be made such that the main goal of imposts income tax can be achieved.
-) Timely revision should be made in the matter of income tax policy according the economic policy of the country. The system of changing income tax policy with the change of government should better be avoided.
-) The terms and procedure under the Income Tax Act should be simplified so even laymen could understand it easily.

Dipendra Raman Neupane (2008) Entitled "*A Comparative Study on Contribution of Direct Tax and Indirect Tax to National Revenue of Nepal*" He studied the contribution of direct tax and indirect tax to the national revenue of Nepal comparatively. It was submitted to Shankar Dev Campus, TU, and Kathmandu at July 2008.

The specific objectives of the study were:

-) To find the contribution of direct tax and indirect tax to national revenue in Nepal.
-) To analyze the structure of direct and indirect tax.
-) To analyze the contribution of corporate tax to national revenue of Nepal.
-) To find out the most important factors for effectiveness of income tax in Nepal.
-) Provide suggestions for effective collection of direct and indirect tax in Nepal.

His major findings are as follows:-

-) The resource gap seems to be increasing every year.
-) The contribution of CITR to government revenue, total tax revenue total direct tax revenue total direct tax revenue during the study period seems to be increasing.

-) Unclear vision of government to corporate sector, frequent changes of rule and regulations and unstable political economic environment of Nepal have sharply damaged the corporate sector presently income tax revenue is collection in accordance to the income tax Act, 2058.

His main recommendations were:

-) Government should make a clear cut distinction between the role of public and private sector. It should take and endeavor to motive, facilitate and regulate to accelerate the private sectors.
-) There should be efficient and effective monitoring system to utilize government resource properly.
-) Proper tax incentive should be given for revival of sick industrial unit provisions should be made under the income tax Act for carry forward and set off a accumulated losses and unabsorbed depreciation of sick units if it is amalgamated with another company.

Atom Neupane August, (2009) Entitled "*Contribution of Direct Tax to National Revenue of Nepal*" He concerned his study in the contribution of Direct Tax and analyzed its contribution to the National Revenue of Nepal. It was submitted to Shankar Dev Campus, TU, and Kathmandu at August 2009.

The specific objectives of the study were:

-) To find the contribution of direct tax and indirect tax to national revenue in Nepal.
-) To analyze the structure of direct and indirect tax.
-) To analyze the contribution of income tax to national revenue of Nepal.
-) To analyze the structure of resources gap in Nepal.
-) To provide suggestions and recommendations for effective collection of direct and indirect tax in Nepal.

His major findings are as follows:-

-) There is a sharp rise in the current expenditure of the Nepalese government. Due to the low revenue growth and institutional weakness, there is lack of adequate resources for capital expenditure.
-) Fiscal deficit of Nepal has been increasing .To solve the fiscal deficit; tax revenue should plays important role.
-) Nepal has been unable for proper mobilization on internal resources.
-) It is need to raise the tax revenue by widening the tax base, refining the tariff structure at regular intervals to mobilize Nepal's tax system properly.
-) The income tax act 2002 and income tax rules system encompasses three taxes; these are income tax from employment, income tax from business and income tax from investment.

His main recommendations were:

-) Nepalese taxation should be moved towards the direct tax based collection which will be proved a more civilized tax system rather than giving a major role. To the individual tax.
-) People should be encouraged to pay tax voluntarily. A system should be introduced that a taxpaying citizen is entitled to receive more incentives than anon-taxpaying citizen.
-) Government should do proper homework before privatizing the enterprises and company and research should be undertaken why the performance of why the performance of private sector is poor even the government is giving more emphasis to it.
-) Government should reduce resource gap by increasing internal revenue and subsidies likewise, government should only take the foreign loan for productive sector or purpose which has high revenue generating possibility.

-) Nepalese income system should make electronic filing returns possible. Similarly, direct crediting of all refunds to the bank account of the taxpayer through electronic clearance system, has to be introduced.

Bidur Parajuli (2010), had studied on the topic “*A Study on Revenue Collection from Value Added Tax (VAT)*”. Mr. Parajuli had concerned his study to examine the Collection of Revenue from VAT in Nepal. It was submitted to *Shankar Dev Campus, TU, Kathmandu* at April 2010.

The specific objectives of the study were:

-) To examine the administrative system and legislative part of VAT in Nepal.
-) To explore the practice scenario of VAT in Nepal.
-) To find out the tax revenue structure in Nepal.
-) To find out the contribution of VAT in GDP, total revenue and tax revenue.
-) To forecast the VAT revenue and GDP for future 5 years based on the time series analysis.

His major findings are as follows:-

-) In Nepalese the amount of tax revenue is higher than that of nontax revenue.
-) The contribution of direct tax revenue on total tax revenue is very low than the contribution of indirect tax on it.
-) The trend of non-filing the tax return is of fluctuating nature.
-) The trend of credit return is higher than the debit return.
-) The share of VAT revenue from import is far higher than the VAT revenue from domestic product.

His main recommendations were:

-) Existing threshold and tax refund is two possible gates for tax evasion. It seems that existing exemption has a broad coverage. However, some exemptions are unavoidable due to administrative complexity and equity aspect. So, exemptions should be minimized gradually.
-) On various issues, such as the effect of VAT on price, economic growth, investment and measures for solving VAT problems research and investigation should be conducted by the expert group. VAT law needs to be reviewed on the basis of experience gained so far.
-) The legal requirements are not sufficient to meet all the provisions. There is need of amendment on the VAT Act and VAT Rules.
-) VAT collection on import is remarkably higher than domestic production. Government should take effective steps to encourage domestic production.
-) VAT should also be levied on agriculture sector with sufficient exception for increasing VAT/GDP ratio.

2.4 Research Gap

There is gap between this research and the previous research most of the previous researches have focused the contribution of various income in the government revenue, structure of the government revenue and the income tax from various sources, tax structure etc. they have found that the contribution of income tax in government revenue is significant and it should be mobilized to economic development of Nepal. Almost all of them have indicated that the tax administration is inefficient and there is high level of tax evasion. Most of the researches have suggested improving the tax administration increasing the contribution of income tax in resource mobilization and widening the tax coverage. But they had not studied the direct and indirect tax.

CHAPTER-III

RESEARCH METHODOLOGY

This chapter is mainly concern with detailed discussion of the methods used for information collection and data collection. There are six parts as research design, population and sampling, sources of data, procedure of data collection.

3.1 Research Design

The research topic entitled “A comparative study on contributing study on contributing of direct tax and indirect tax to National revenue of Nepal” is abstracted from the socio-economic environments of Nepal. As the income tax system and structure is based on various rule regulations and acts which are always setting an different countries own socio-economic in restructure, descriptive research design is more suitable to analyze Nepalese corporate tax structure for contribution of corporate income tax, the study needs to analyze its past performance indifferent time period with respective indirect. So historical as well as descriptive research design is used.

3.2 Population and Sampling

The targeted whole area relating to government or national revenue is set for the research population. Income tax is taken as size. The population for primary belonging to income tax of Nepal. 90 sample size is selected from there different groups of respondents. The following table shows the group of respondents and sample size.

| S.N | Group of Respondents | Sample size |
|-----|----------------------|-------------|
| 1. | Tax administrators | 30 |

| | | |
|-------|------------|----|
| 2. | Tax expert | 30 |
| 3. | Tax payer | 30 |
| Total | | 90 |

3.3 Sources of Data

According to the nature of the study, the study requires primary as well as secondary data.

3.3.1 Primary Data

Primary data were collected through a schedule of self structured questionnaires, informal dialogues, discussion and interviews with concerned persons. Separate sets of questionnaires were used to have options/ information from three- sample population. To get the accurate and actual information total 90 questions were distributed to selected respondents of different groups such as tax administrator, tax experts and tax payers. Set of 30 questionnaires were distributed and 25 of them were collected from each group for the purpose of analysis. The following table shows the questionnaires distributed and collected for each group of respondents:

| S.N | Group of Respondents | Questionnaires distributed | Questionnaire collected |
|-----|----------------------|----------------------------|-------------------------|
| 1. | Tax administrator | 30 | 25 |
| 2. | Tax expert | 30 | 25 |

| | | | |
|-------|-----------|----|----|
| 3. | Tax payer | 30 | 25 |
| Total | | 90 | 75 |

3.3.2 Secondary Data

Secondary data have been collected from various sources like:

Annual reports of IRD/N, economic survey, published by MOF/Govt. likewise economic bulletin of NRB, economic bulletin of various time and central business of statistics etc.

3.4 Data and Information Collection Procedure

Various numerical data and information were collected as per the objective of the study and research questions. Firstly, laws, rules, regulation and policies related to income tax and corporate tax are studied to get more information about corporate income tax including book related to public finance. Secondly, different libraries such as chamber of commerce, FNCCI and NRB are also consulted. Thirdly, the numerical data are collected from the publication of annual reports of IRD/N, economic bulletin of NRB, economic survey of MOF, publication of security Board, CBS, publication of CEDA/TU, budget speeches etc. Lastly, various journals, national newspaper were also reviewed. Respective parties were consulted while analyzing the research questions.

3.5 Data Analysis Procedure

The collected data were classified tabulated and analyzed in descriptive and analytical way as per the subject matter. Likewise, the required accounting

principle mathematical approaches and legal provision of ITA, 2058 are taken into consideration in data analysis procedure.

3.6 Presentation and Analytical Tools

Various tools were applied while conducting this study which is table, percentage, correlation time series analysis.

- a. Table: Various tables are formulated to tabulate the data. A matter table is also presented in the appendix.
- b. Charts and diagrams: These tools are used for visually description of the data, trend line, bar diagrams are used for the purpose.
- c. Correlation: Correlation may be defined as the degree of linear relationship between two or more variable are said to be correlated when the change in the value of one variable is accompanied by the change of another variables. Correlation analysis is defined as the statistical technique which measures the variable which lies between ± 1 . If the value of correlation (r) is nearer to +1, this relationship is said to be perfectly positively correlated and vice-versa. We can compute the correlation simply by using direct method.

$$r = \frac{N\sum XY - \sum X \sum Y}{\sqrt{N\sum X^2 - (\sum X)^2} \sqrt{N\sum Y^2 - (\sum Y)^2}}$$

Where,

N=No of observation

X=Variables

y=Variables.

- d. Analysis of Time Series Data

A series formed a set of statistical data arranged in accordance with their time of occurrence is said to be a time series. A time series shows the relation between two variables one being the time. The size of population in every decade the price level of the different in every month the volume of population indicate the relation between the time changes and the changes in the value of other variables.

Time series analysis is mostly used in Business and economics, by which we can predict the value of variable for the future. Mathematically, a time series is defined as the time 'T' may be yearly, quarterly monthly, weekly etc. There is various method of analyzing time series, least square method is showing trend and prediction in our research.

A widely and most commonly used method to describe the trend line and predication is method of least square. Under this method, a trend line is fitted to data satisfying $\sum(y-y_1) = 0$ and $\sum (y-y_1)^2$ is least from that the line obtained by this method is the line of best fit.

Where, y is the actual value and y_1 is the computed value of y .

Trend line, $y = a + bx$,

Where,

Y = Dependent variable

X = Independent variable

A = y intercept or value of y when $X = 0$

B = slope of the trend line of amount (of) change that comes in y for a unit change in x .

CHAPTER - IV

PRESENTATION AND ANALYSIS OF DATA

4.1 Tax Structure of Nepal

Modern economic planning of Nepal had started with the initiation of first economic planning in 1956. Since then taxes have been used for the achievement of national economic goals. So, taxes play vital role to the economic development of Nepal. Tax structure of any country comprises both direct and indirect taxes.

4.1.1 Composition of Total Revenue

Total revenue in Nepal is composed of both tax revenue and non-tax revenue when the Nepal Government presented first national budget in 1951/52.

Table 4.1 shows composition of total revenue of government which includes tax and non-tax revenue from FY 1998/99 to 2008/09. It seems that the share of tax revenue has always been greater than the share of non-tax revenue. In FY 2008/09, the share of tax revenue and non-tax revenue was 81.58% and 18.42% respectively as compared with 77.19% and 22.81% in FY 1998/99. This indicates that the tax revenue is increasing from past Fiscal Years, which is very good symptoms of increasing awareness of tax revenue to the public and the government. On the other hand, Non-tax revenue has decreased compared to last Fiscal Years. Tax revenue has been placed as major sources of government revenue in Nepal. The table shown as follows:

Table 4.1

Contribution of tax and non-tax revenue to total Revenue of Nepal

From 1998/99 to 2008/09.

Rs. in Ten Million and percentage

| Fiscal Year | Total Revenue | Tax Revenue | Tax revenue as % of total revenue | Non –tax Revenue | Non tax revenue as % of total revenue |
|--------------------|----------------------|--------------------|--|-------------------------|--|
| 1998/99 | 3725.13 | 2875.29 | 77.19 | 849.84 | 22.81 |
| 1999/00 | 4,289.37 | 3,315.21 | 77.29 | 974.16 | 22.71 |
| 2000/01 | 4,889.38 | 3,886.50 | 79.49 | 1,002.88 | 20.51 |
| 2001/02 | 5,044.66 | 3,933.06 | 77.96 | 1,111.60 | 22.04 |
| 2002/03 | 5,453.89 | 4,089.60 | 74.99 | 1,364.29 | 25.01 |
| 2003/04 | 6,233.10 | 4,817.30 | 77.29 | 1,415.80 | 22.71 |
| 2004/05 | 7,012.27 | 5,410.47 | 77.16 | 1,601.80 | 22.84 |
| 2005/06 | 7,228.20 | 5,743.04 | 79.45 | 1,485.16 | 20.55 |
| 2006/07 | 8,771.22 | 7,112.67 | 81.09 | 1,658.55 | 18.91 |
| 2007/08 | 10,762.25 | 8,515.55 | 79.12 | 2,246.70 | 20.88 |
| 2008/09 | 14,347.45 | 11,705.19 | 81.58 | 2,642.26 | 18.42 |
| Total | 77,756.92 | 61,403.88 | 78.97 | 16,353.04 | 21.03 |

| | | | | | |
|----------------|-----------------|-----------------|--------------|-----------------|--------------|
| Average | 7,068.81 | 5,582.17 | 78.97 | 1,486.64 | 21.03 |
|----------------|-----------------|-----------------|--------------|-----------------|--------------|

Source: Economic Survey 2001/02 and 2009/10, Yearly Report of IRD 2008/09

The above table 4.1 reflects that the tax revenue was gradually increasing in every year since 1998/99 amounting Rs. 28752.9 million to Rs.117,051.9 million in the Year 2008/09. But the percentage contribution of tax revenue was found fluctuating in different years. The contribution of tax revenue to total revenue was maximum 81.58% in FY 2008/09 and the contribution of tax revenue to total revenue was minimum 74.99% in FY 2002/03 during the study period and the average collection was 78.97% in different years.

The non tax revenue collection was in the increasing trend in 11 years i.e. Rs.8, 498.4 million in 1998/99 to Rs 26,422.6 million in 2008/09. The non-tax collection in 2005/06 was decreased to Rs.14,851.6 million in the FY 2005/06. After that, it was in the increasing trend.

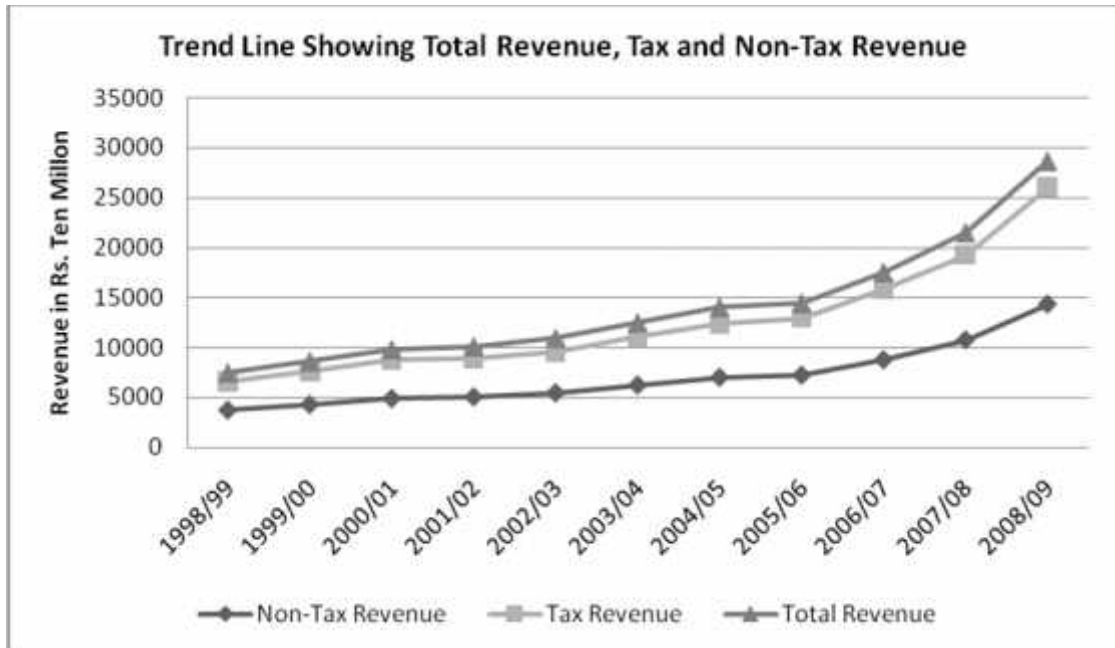
The tax revenue collection was seen to be in gradually increasing trend. The contribution portion of non tax revenue to total revenue was fluctuating during the study period. The collection of non tax to total revenue was maximum 25.01 % in FY 2002/03. The average contribution was 21.03% during the study period.

In average, contribution of tax revenue and non tax revenue are 78.97% and 21.03% respectively. This shows in Nepal, Tax revenue contributes more to the National revenue.

The contribution of tax and non tax revenue on total tax revenue is shown in the following trend line.

Figure 4.1

Trend Line Showing Total Revenue, Tax and Non-Tax Revenue



Source: Table 4.1

In this figure total revenue is shown in the Y-axis and fiscal year in X-axis. Figure shows three trends lines which are total revenue, tax revenue and non-tax revenue. It is clear that upper line is total revenue which is ascending upward. Middle is tax revenue it is higher than non tax revenue which is represented by lower line .So, total revenue is combination of tax and non-tax revenue.

4.1.2 Composition of Direct and Indirect Tax on Total Tax Revenue in Nepal

The structure of Nepalese tax revenue can be presented in terms of consumption income and capital based tax. Taxes on consumption are known as indirect tax and taxes on income as well as capital are known as direct taxes. Custom duties, excise duties, value added tax, entertainment tax, hotel tax, air flight tax and road bridge maintained taxes are included in indirect tax and

income tax, house and land registration, vehicle tax, wealth tax and other taxes are included in direct tax which is already discussed in the previous chapters.

Composition of direct tax and indirect tax is presented in table 4.2. The table shows that the share of indirect tax is more than the share of direct tax. The contribution of indirect and direct tax was Rs. 21,236.8 million and Rs. 7,516.1 million that was 73.86% and 26.14% of total tax revenue respectively in the fiscal year 1998/99.

It is seen that collection from direct tax is in increasing trend till 2008/09 except in the year 2002/03 it decreased to 10,105.8 million from 10,597.5 million in the FY 2001/02. Where as Indirect tax is always in the increasing trend from FY 1998/99 to 2008/09. The average collection of direct tax revenue was 14,788.3 million in study period.

But the percentage contribution of indirect tax revenue was found fluctuating in different years. The composition of indirect tax revenue to total tax revenue was maximum 76.27% in FY 2002/03. It is in the decreasing trend since FY 2005/06 and in the fiscal year 2008/09 it came upto 70.68% which is minimum till our study period. The composition of direct tax revenue to total tax revenue was maximum 29.32% in FY 2008/09 and minimum was 23.73% in FY 2002/03. The average contribution of indirect tax and direct tax was 73.58% and 26.42% during the study period.

Table and figure are as follows:

Table 4.2

Composition of Direct and Indirect tax on Total Tax Revenue

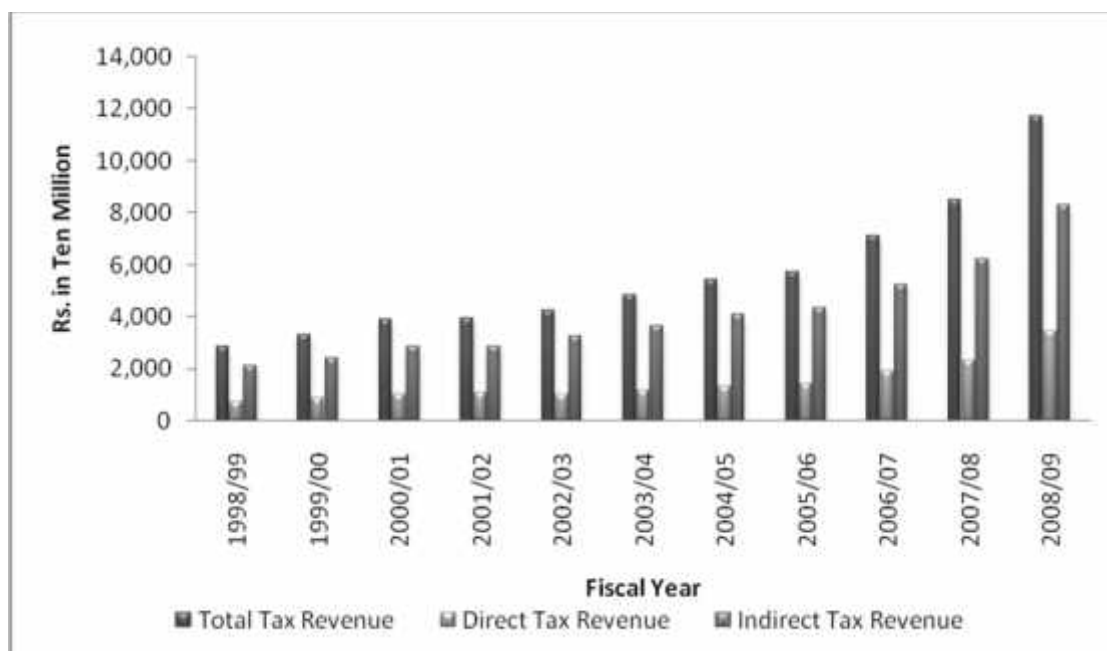
Rs. in Ten Million and Percentage

| Fiscal Year | Total Tax Revenue | Direct Tax Revenue | % share of direct tax on total tax revenue | Indirect Tax Revenue | % share of indirect tax on total tax revenue |
|-------------|-------------------|--------------------|--|----------------------|--|
| 1998/99 | 2,875.29 | 751.61 | 26.14 | 2,123.68 | 73.86 |
| 1999/00 | 3,315.21 | 895.15 | 27.00 | 2,420.06 | 73.00 |
| 2000/01 | 3,886.51 | 1,015.94 | 26.14 | 2,870.57 | 73.86 |
| 2001/02 | 3,933.06 | 1,059.75 | 26.94 | 2,873.31 | 73.06 |
| 2002/03 | 4,258.70 | 1,010.58 | 23.73 | 3,248.12 | 76.27 |
| 2003/04 | 4,817.30 | 1,191.26 | 24.73 | 3,626.04 | 75.27 |
| 2004/05 | 5,410.47 | 1,307.18 | 24.16 | 4,103.29 | 75.84 |
| 2005/06 | 5,743.04 | 1,396.81 | 24.32 | 4,346.23 | 75.68 |
| 2006/07 | 7,112.67 | 1,898.03 | 26.69 | 5,214.64 | 73.31 |
| 2007/08 | 8,515.55 | 2,308.77 | 27.11 | 6,206.78 | 72.89 |
| 2008/09 | 11,705.19 | 3,432.07 | 29.32 | 8,273.12 | 70.68 |
| Total | 61,572.99 | 16,267.15 | 26.42 | 45,305.84 | 73.58 |
| Average | 5,597.54 | 1,478.83 | 26.42 | 4,118.71 | 73.58 |

Source: 1) Economic Survey 2001/02, 2009/10

Figure 4.2

Bar Diagram Showing Direct and Indirect Tax on Total Tax Revenue



Source: Table 4.2

The table 4.2 reveals that our economy is heavily dependent on indirect tax in comparison to direct tax. Indirect taxation with a dominant role in tax structure could be taken as a symptom of developing country. To divert the economy in the channel of development those countries should increase the share of direct tax. The share of indirect tax is increasing and it is not good symptom of economic development. The share of direct tax Rs. 7,516.1 million which has 26.14% of total tax revenue in FY 1998/99. It was increased to 34,320.7million which have 29.32% in FY 2008/09. Therefore, the attention should be paid on the sufficient resource mobilization through internal resources.

4.1.3 Composition of Direct Tax Revenue in Nepal

The major components of direct tax are income tax, House and Land registration and Vehicle tax. The share of major components of direct tax is given in table 4.3.

Table 4.3**Major Sources of Direct Tax and Their Relative Percentage to Direct Tax from FY 1998/99 to 2008/09**

Rs. In Ten Million and Percentage

| Fiscal Year | Direct Tax revenue | | Income Tax | | House, Land registration | | Vehicle tax | |
|-------------|--------------------|---------|------------|---------|--------------------------|---------|-------------|----------|
| | Rs. | Total % | Rs. | %of DTR | Rs. | %of DTR | Rs. | % of DTR |
| 1998/99 | 751.62 | 100.00 | 617.03 | 82.09 | 100.32 | 13.35 | 34.27 | 4.56 |
| 1999/00 | 895.15 | 100.00 | 742.06 | 82.90 | 101.59 | 11.35 | 51.50 | 5.75 |
| 2000/01 | 1,015.94 | 100.00 | 911.40 | 89.71 | 61.29 | 6.03 | 43.25 | 4.26 |
| 2001/02 | 1,059.75 | 100.00 | 890.37 | 84.02 | 113.18 | 10.68 | 56.20 | 5.30 |
| 2002/03 | 1,010.57 | 100.00 | 813.19 | 80.47 | 141.43 | 14.00 | 55.95 | 5.54 |
| 2003/04 | 1,191.28 | 100.00 | 951.47 | 79.87 | 169.75 | 14.25 | 70.06 | 5.88 |
| 2004/05 | 1,307.18 | 100.00 | 1,046.61 | 80.07 | 179.92 | 13.76 | 80.65 | 6.17 |
| 2005/06 | 1,396.81 | 100.00 | 1,093.94 | 78.32 | 218.11 | 15.61 | 84.76 | 6.07 |
| 2006/07 | 1,898.03 | 100.00 | 1,573.18 | 82.88 | 225.35 | 11.87 | 99.50 | 5.24 |
| 2007/08 | 2,308.77 | 100.00 | 1,907.78 | 82.63 | 294.07 | 12.74 | 106.92 | 4.63 |
| 2008/09 | 3,432.07 | 100.00 | 2,724.74 | 79.39 | 522.34 | 15.22 | 185.00 | 5.39 |
| Total | 16,267.17 | 100.00 | 13,271.77 | 81.59 | 2,127.35 | 13.08 | 868.06 | 5.34 |
| Average | 1,478.83 | 100.00 | 1,206.52 | 81.59 | 193.40 | 13.08 | 78.91 | 5.34 |

NOTE: Since 1998/99 to 2001/02:-

Land Revenue has been included in house land registration.

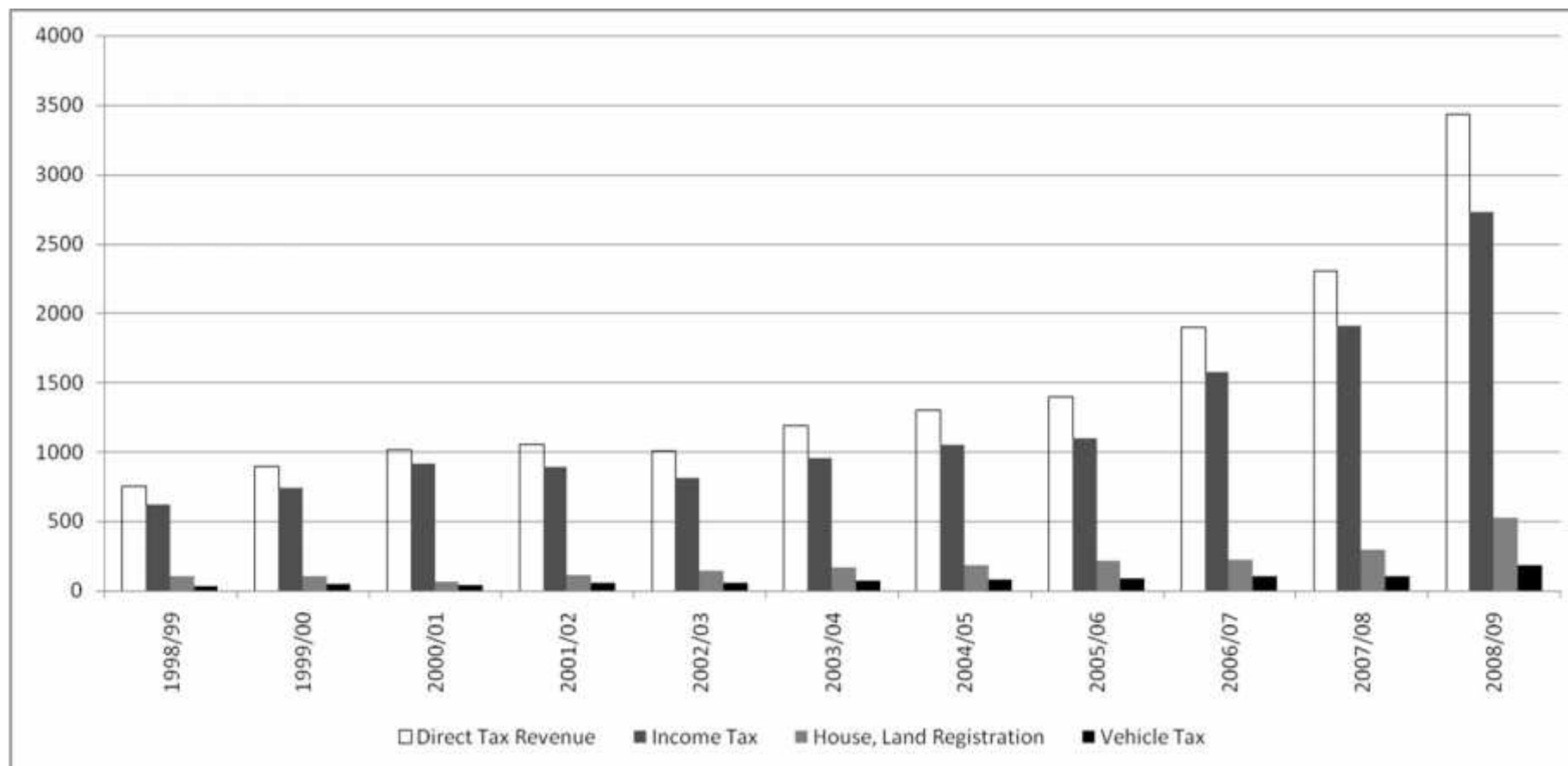
Urban House and Land Tax have been included in vehicle tax. Now, these are not government revenue.

Source:1) Economic Survey 2001/02, 2009/10,

2) Annual Report of IRD (2008/09.)

Figure 4.3

Bar Diagram Showing Composition of Direct Tax



Source : Table 4.3

Table 4.3 shows that the income tax occupied the largest share in the direct tax. The percent share of income tax to direct tax started with 82.09% amounting Rs.6,170.3 million in the fiscal year 1998/99 and in the increasing trend it reached up to Rs. 27,247.4 million in the fiscal year 2008/09 which was 79.39% of direct tax revenue. Maximum percentage of collection of income tax was 89.71% amounting Rs. 9,114 million in FY 2000/01 and minimum percentage of collection of income tax was 78.32% amounting Rs. 10,939.4 in FY 2005/06. It is seen that total amount of Income tax is in increasing trend but the percentage of income tax to direct tax is fluctuating.

House and Land registration have collected 13.35% amounting Rs. 1,003.2 million in the Fiscal Year 1998/99, which was decreased gradually and reduced to 6.03% amounting Rs 612.9 million in the FY 2000/01. Then after started to increase gradually till FY 2003/04. So, we found fluctuating the percentage of collection of House & Land registration to direct tax. It was maximum 15.61% amounting Rs. 2181.1 million in the FY 2005/06 and minimum 6.03% amounting 612.9 million in the year 2000/01. The average percentage of H&L registration to total direct tax was 13.08% amounting Rs.1934 million.

The share of vehicle tax to total direct tax was Rs. 342.7 million which contributed 4.56% in the FY 1998/99. Collection of vehicle tax was regularly increasing since 2001/02 till 2008/09 from Rs.562 million to Rs. 1,850 million but before 2001/02, it was fluctuating. And percentage collection of vehicle tax to direct tax was also fluctuated time and again. The portion of Vehicle Tax reached up to 6.17% in the year 2004/05 which is maximum it got minimum percentage of collection in 2000/01 which was 4.26% amounting Rs.432.5 million.

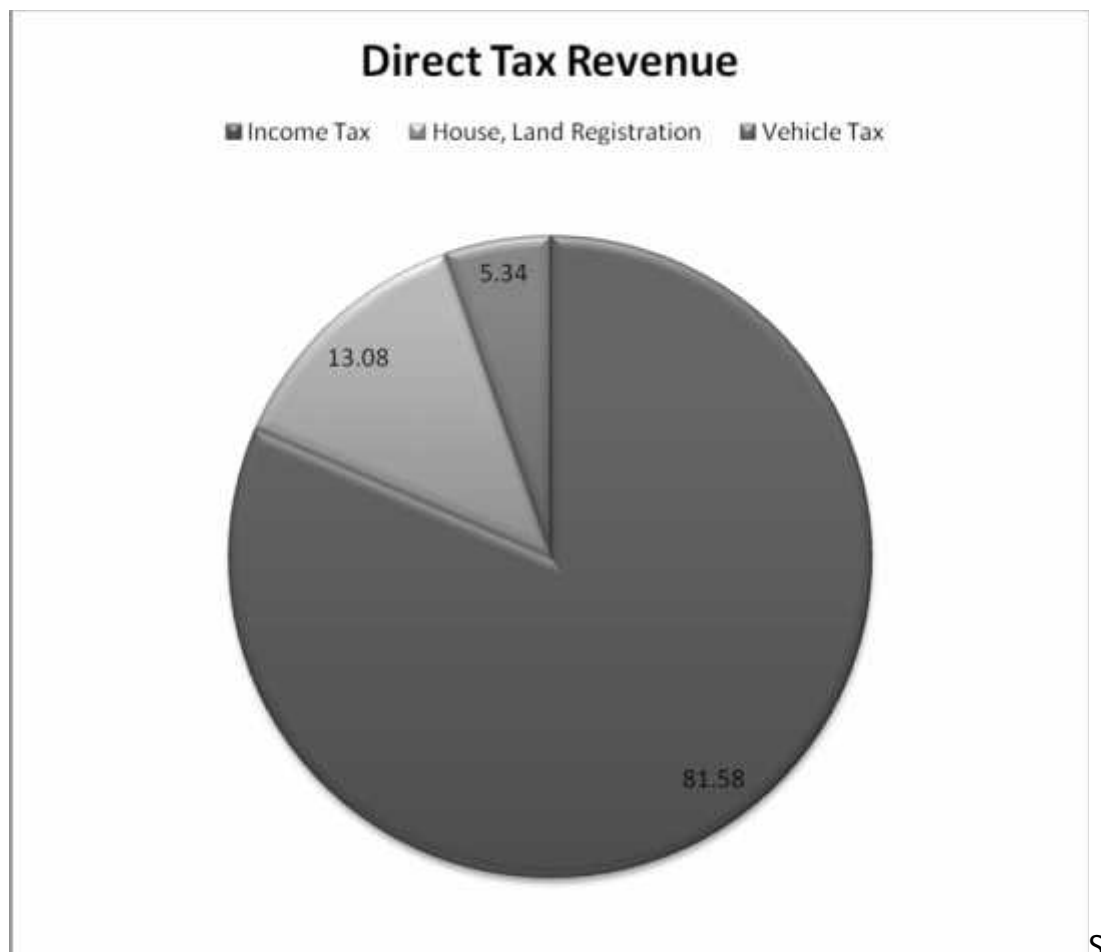
In average, contribution of income tax, house, land registration and vehicle tax were 81.59%, 13.08% and 5.34% respectively. The major portions of direct tax cover by income tax that's why to increase the volume of direct tax we must

focus in the income tax. The percentage of vehicle tax to direct tax is found to be very lower in comparison to income tax, House & Land registration.

This is shown in the following chart.

Figure 4.4

Average Combination of Direct Tax Revenue



Source: Table 4.3

4.1.4 Composition of Indirect Tax

The tax composition of Nepal is mainly dependent on indirect taxes which contributed 70.68% of total tax revenue in FY 2008/09. Nepalese tax revenue is dependent mainly on international trade and sales VAT on goods and services supplemented by taxes on income and property to some extent.

The major components of indirect tax in Nepalese tax structure constitutes custom duties, excise duties and VAT etc. Custom duty has been classified mainly into import duty, export duty and Indian excise. Value added tax components are selling and distribution tax, tourism, import and production etc. Table 4.4 shows the sources of indirect tax revenue is given as follows:

Table 4.4

Major Sources of Indirect Tax and Their Relative Percentage to Indirect

Tax from the FY 1998/99 to 2008/09

Rs. in Ten Million and Percentage

| Fiscal Year | Indirect Tax Revenue | | Custom Duties | | Excise Duties | | VAT | |
|-------------|----------------------|---------|---------------|-----------|---------------|-----------|----------|-----------|
| | Rs. | Total % | Rs. | % of IDTR | Rs. | % of IDTR | Rs. | % of IDTR |
| 1998/99 | 2,123.63 | 100.00 | 951.77 | 44.82 | 295.32 | 13.91 | 876.59 | 41.28 |
| 1999/00 | 2,420.06 | 100.00 | 1,081.33 | 44.68 | 312.76 | 12.92 | 1,025.97 | 42.39 |
| 2000/01 | 2,870.57 | 100.00 | 1,255.21 | 43.73 | 377.12 | 13.14 | 1,238.24 | 43.14 |
| 2001/02 | 2,873.31 | 100.00 | 1,265.88 | 44.06 | 380.70 | 13.25 | 1,226.73 | 42.69 |
| 2002/03 | 3,248.12 | 100.00 | 1,423.64 | 43.83 | 478.51 | 14.73 | 1,345.97 | 41.44 |
| 2003/04 | 3,626.04 | 100.00 | 1,555.48 | 42.90 | 622.67 | 17.17 | 1,447.89 | 39.93 |
| 2004/05 | 4,103.29 | 100.00 | 1,570.16 | 38.27 | 644.59 | 15.71 | 1,888.54 | 46.03 |
| 2005/06 | 4,346.23 | 100.00 | 1,534.40 | 35.30 | 650.76 | 14.97 | 2,161.07 | 49.72 |
| 2006/07 | 5,214.64 | 100.00 | 1,670.76 | 32.04 | 934.32 | 17.92 | 2,609.56 | 50.04 |

| | | | | | | | | |
|---------|-----------|--------|-----------|-------|----------|-------|-----------|-------|
| 2007/08 | 6,206.78 | 100.00 | 2,106.25 | 33.93 | 1,118.96 | 18.03 | 2,981.57 | 48.04 |
| 2008/09 | 8,271.47 | 100.00 | 2,679.29 | 32.39 | 1,622.09 | 19.61 | 3,970.09 | 48.00 |
| Total | 45,304.14 | 100.00 | 17,094.17 | 37.73 | 7,437.80 | 16.42 | 20,772.22 | 45.85 |
| Average | 4,118.56 | 100.00 | 1,554.02 | 37.73 | 676.16 | 16.42 | 1,888.38 | 45.85 |

Source:1) Economic Survey 2001/02, 2009/10

2) Annual Report of IRD 2008/09

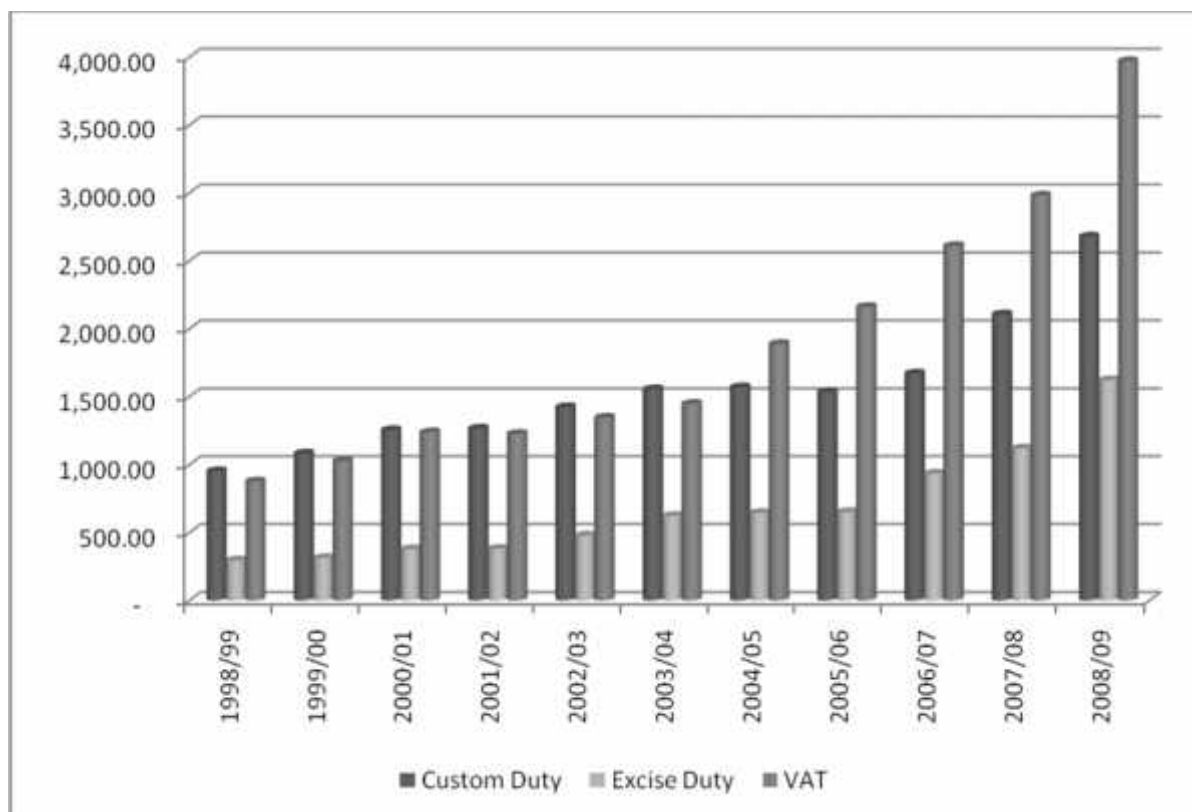
Note:-

1. Custom duties include import +export +Indian excise refund +others.
- 2) Excise duties include industrial products specially alcohol and tobacco.
3. VAT includes sales tax, tourism, production, import, contact and consultation and other services.

Bar diagram can be presented as follows:-

Figure No. 4.5

Bar Diagram Showing Custom Duties, Excise Duties and VAT on Indirect Tax



Source: Table 4.4

Table 4.4 reflects that the custom duty and VAT occupied major position of indirect tax which is in average 37.73% and 45.85% respectively. In FY 1998/99 the contribution of custom duty was 44.82% which fluctuated during the study period and it was 32.39% in the FY 2008/09. The average percentage collection of custom duty to indirect tax was 33.73% during the study period. The share of excise duty was 13.91% in FY 1998/99. Percentage of excise was fluctuated during the study period in reached up to 19.61% in the FY 2008/09, which is the highest percentage of excise. Its average contribution was 16.42% during the study period, which it is not satisfactory and it needs to increase in the future.

The VAT has become an important source of overall tax revenue with fluctuating trend which contributed 41.28% in FY 1998/99. Percentage of maximum contributed was 50.04% in FY 2006/07. It reached up to 48.00% in

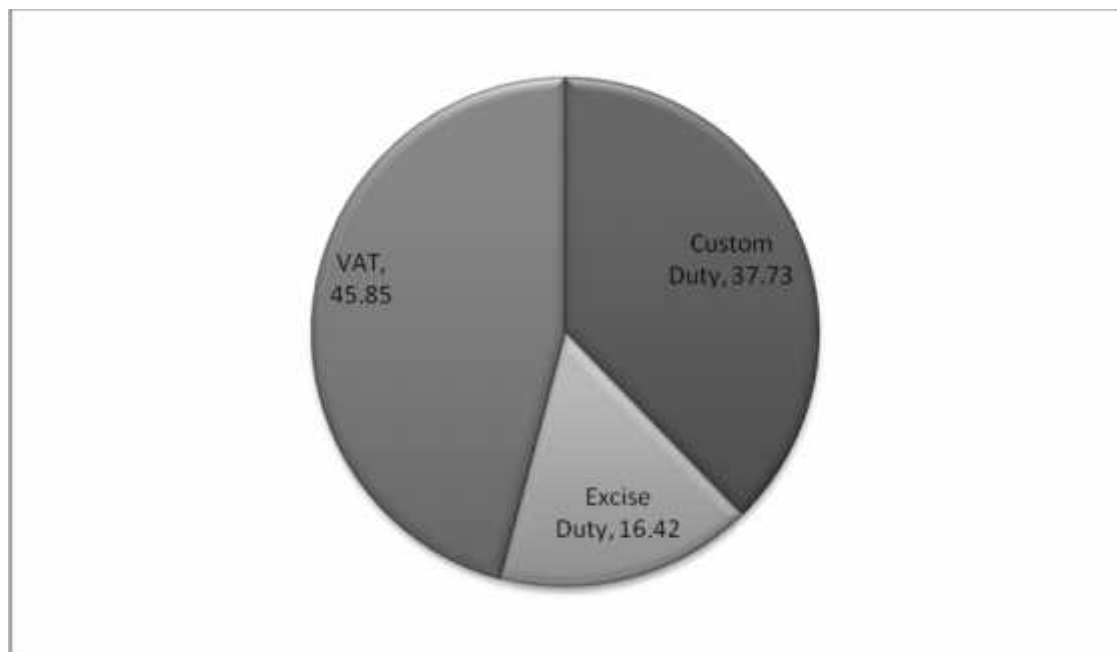
the FY 2008/09. The average of VAT contribution was 45.85% during the study period.

In average highest contribution was from VAT which is 45.85%, next is custom duty and excise duty having 37.73% and 16.42% respectively.

Average amount of components of indirect tax is shown as pie chart:-

Figure 4.6

Average Combination of Indirect Tax Revenue in percentage



Source: Table 4.4

4.1.5 Contribution of Direct Tax in GDP, Total Revenue and Total Tax Revenue

The contribution of direct tax on GDP, Total revenue and Total tax revenue is shown below.

Table 4.5

**Contribution of Direct Tax in GDP, Total Revenue and
Total Tax Revenue from the FY 1998/99 to 2008/09**

Rs. In Ten Million and Percentage

| Fiscal Year | Direct Tax Revenue | GDP at basic prices (current) | Total Revenue | Total Tax Revenue | % of DT in GDP | % of DT in Total Revenue | % of DT in Total Tax Revenue |
|----------------------|--------------------|-------------------------------|------------------|-------------------|----------------|--------------------------|------------------------------|
| 1998/99 | 751.61 | 33,001.80 | 3,725.10 | 2,875.29 | 2.28 | 20.18 | 26.14 |
| 1999/00 | 895.15 | 36,625.10 | 4,289.37 | 3,315.21 | 2.44 | 20.87 | 27.00 |
| 2000/01 | 1,015.94 | 41,342.90 | 4,889.39 | 3,886.51 | 2.46 | 20.78 | 26.14 |
| 2001/02 | 1,059.75 | 43,039.70 | 5,044.56 | 3,933.06 | 2.46 | 21.01 | 26.94 |
| 2002/03 | 1,010.58 | 46,032.50 | 5,622.97 | 4,258.70 | 2.20 | 17.97 | 23.73 |
| 2003/04 | 1,191.26 | 50,069.90 | 6,233.10 | 4,817.30 | 2.38 | 19.11 | 24.73 |
| 2004/05 | 1,307.18 | 54,848.50 | 7,012.27 | 5,410.47 | 2.38 | 18.64 | 24.16 |
| 2005/06 | 1,396.81 | 61,111.80 | 7,228.21 | 5,743.04 | 2.29 | 19.32 | 24.32 |
| 2006/07 | 1,898.03 | 67,585.90 | 8,771.22 | 7,112.67 | 2.81 | 21.64 | 26.69 |
| 2007/08 | 2,308.77 | 75,523.20 | 10,762.25 | 8,515.55 | 3.06 | 21.45 | 27.11 |
| 2008/09 [®] | 3,432.07 | 91,016.00 | 14,347.45 | 11,705.19 | 3.77 | 23.92 | 29.32 |
| Total | 16,267.15 | 600,197.30 | 77,925.89 | 61,572.99 | 2.71 | 20.88 | 26.42 |

Total tax Revenue = Direct tax Revenue + Indirect tax revenue

Total Revenue = Tax Revenue + Non-tax Revenue

R= Revised

Source:1) Economic survey 2001/02, 2008/09

2) Annual Report of IRD 2007/08 and Budget Speech 2009/10

According to the table 4.5 we found that the contribution of direct tax on GDP was 2.28% in FY 1998/99. The share of direct tax to GDP seems to be very low. It increased to 3.77% in FY 2008/09 which is the highest percentage till our study period. The contribution of direct tax on total revenue was fluctuated. Its contribution was 20.18% in FY 1998/99 and reached to 23.92% in FY 2008/09 which was maximum and minimum was 17.97% in FY 2002/03. The contribution of direct tax on total tax revenue was 26.14% in FY 1998/99. It was fluctuated time and again and reached to 29.32% in FY 2008/09, which is the maximum percentage till 2008/09.

It is seen that Total Revenue, total tax revenue and GDP all are maximum in the FY 2008/09 compared to past years, both in the amount and in the percentage. The average contribution of direct tax to total revenue, total tax revenue and GDP was 20.88%, 26.42% and 2.71% respectively during the study period.

4.1.6 Contribution of Indirect Tax in GDP, Total Revenue and Total Tax Revenue

The contribution of Indirect tax to GDP, total revenue and total tax revenue is shown below.

Table 4.6**Contribution of Indirect Tax in GDP, Total Revenue and Total Tax Revenue from the FY 1998/99 to 2008/09**

Rs. in Ten Million and Percentage

| Fiscal Year | Indirect tax | GDP at basic prices (current) | Total Revenue | Total Tax Revenue | % of IDT in GDP | % of IDT in Total Revenue | % of IDT in Total Tax Revenue |
|-------------|--------------|-------------------------------|---------------|-------------------|-----------------|---------------------------|-------------------------------|
| 1998/99 | 2,123.63 | 33,001.80 | 3,725.10 | 2,875.29 | 6.43 | 57.01 | 73.86 |
| 1999/00 | 2,420.06 | 36,625.10 | 4,289.37 | 3,315.21 | 6.61 | 56.42 | 73.00 |
| 2000/01 | 2,870.57 | 41,342.90 | 4,889.39 | 3,886.51 | 6.94 | 58.71 | 73.86 |
| 2001/02 | 2,873.31 | 43,039.70 | 5,044.56 | 3,933.06 | 6.68 | 56.96 | 73.06 |
| 2002/03 | 3,248.12 | 46,032.50 | 5,622.97 | 4,258.70 | 7.06 | 57.77 | 76.27 |
| 2003/04 | 3,626.04 | 50,069.90 | 6,233.10 | 4,817.30 | 7.24 | 58.17 | 75.27 |
| 2004/05 | 4,103.29 | 54,848.50 | 7,012.27 | 5,410.47 | 7.48 | 58.52 | 75.84 |
| 2005/06 | 4,346.23 | 61,111.80 | 7,228.21 | 5,743.04 | 7.11 | 60.13 | 75.68 |
| 2006/07 | 5,214.64 | 67,585.90 | 8,771.22 | 7,112.67 | 7.72 | 59.45 | 73.31 |

| | | | | | | | |
|-------------|-----------|------------|-----------|-----------|------|-------|-------|
| 2007/08 | 6,206.78 | 75,523.20 | 10,762.25 | 8,515.55 | 8.22 | 57.67 | 72.89 |
| 2008/09 (R) | 8,271.47 | 91,016.00 | 14,347.45 | 11,705.19 | 9.09 | 57.65 | 70.66 |
| Total | 45,304.14 | 600,197.30 | 77,925.89 | 61,572.99 | 7.55 | 58.14 | 73.58 |
| Average | 4,118.56 | 54,563.39 | 7,084.17 | 5,597.54 | 7.55 | 58.14 | 73.58 |

R=Revised

Source: 1) Economic Survey 2001/02 and 2008/09

2) Annual Report of IRD 2008/09 and Budget Speech 2009/10

From the above table 4.6 it is cleared that contribution of indirect tax on GDP was 6.43% in FY 1998/99 which is minimum and 9.09% in FY 2008/09 which is highest till study period. The share of indirect tax to GDP seems to be very low, so it must be increased. The contribution of indirect tax to total revenue was fluctuated. Its contribution was 57.01% in FY 1998/99. Maximum percentage of contribution of indirect tax to total revenue was 60.13% in FY 2005/06 and minimum was 56.42% in FY1999/00 and came to 57.65% during the study period. The contribution of indirect tax to total tax revenue was 73.86% in FY 1998/99. The maximum Percentage contribution of indirect tax to total tax revenue was 76.27% in FY 2002/03 and minimum was 70.66% in FY2008/09. The average of contribution of indirect tax to GDP, total revenue and total tax revenue were 7.55%, 58.14% and 73.58% respectively.

It is seen that amount of GDP, total revenue and total tax revenue are in the increasing trend. Percentage contribution of indirect tax to GDP is also in increasing trend but percentage contribution of total revenue and total tax revenue are fluctuating.

4.1.7 Structure of Income Tax in Nepal

Nepalese income tax structure is formed by contribution of income tax from public enterprises, semipublic enterprises, private corporate bodies, individuals, employment, tax on interest and others. This has been presented in table 4.7. Here, public enterprises consist of full government ownership, semipublic consists of more than 50% share of government, private corporate bodies mean public limited companies, individuals denotes sole traders, partnership and private companies and employment refers to salaries earned by government and non-government sectors employers. Other tax includes Capital gain tax, dividend, other income on investment, windfall gain tax etc.

Table 4.7

Collection from Major Sources of Income Tax in Nepal from the FY 1998/99 to 2008/09

Rs. in Ten Million and Percentage

| Fiscal Year | Total Income Tax Revenue | | Public enterprises | | Private Corporate Bodies | | Individuals | | Employments (Remuneration) | | Tax on Interest | | Other Taxes | |
|-------------|--------------------------|--------|--------------------|-------|--------------------------|-------|-------------|-------|-----------------------------|-------|-----------------|-------|-------------|------|
| | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % |
| 1998/99 | 617.02 | 100.00 | 152.65 | 24.73 | 115.50 | 18.72 | 277.27 | 44.94 | 39.65 | 6.42 | 31.95 | 5.19 | - | - |
| 1999/00 | 742.06 | 100.00 | 219.88 | 29.63 | 133.95 | 18.05 | 301.64 | 40.65 | 45.15 | 6.08 | 41.44 | 5.59 | - | - |
| 2000/01 | 911.40 | 100.00 | 292.80 | 32.12 | 192.43 | 21.11 | 320.05 | 35.12 | 59.73 | 6.55 | 46.39 | 5.10 | - | - |
| 2001/02 | 890.37 | 100.00 | 176.93 | 19.87 | 141.20 | 15.86 | 441.91 | 49.63 | 83.56 | 9.38 | 46.77 | 5.26 | - | - |
| 2002/03 | 813.19 | 100.00 | 125.10 | 15.38 | 123.63 | 15.20 | 336.22 | 41.35 | 125.26 | 15.40 | 86.40 | 10.64 | 16.58 | 2.03 |
| 2003/04 | 951.45 | 100.00 | 205.66 | 21.61 | 153.13 | 16.09 | 353.34 | 37.14 | 139.12 | 14.62 | 73.34 | 7.72 | 26.86 | 2.82 |
| 2004/05 | 1,046.61 | 100.00 | 133.24 | 12.73 | 246.78 | 23.58 | 392.63 | 37.51 | 167.59 | 16.01 | 75.70 | 7.24 | 30.67 | 2.93 |
| 2005/06 | 1,093.94 | 100.00 | 19.57 | 1.79 | 340.43 | 31.12 | 423.47 | 38.71 | 176.41 | 16.12 | 77.49 | 7.09 | 56.57 | 5.17 |

| | | | | | | | | | | | | | | |
|----------------|------------------|---------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|---------------|-------------|---------------|-------------|
| 2006/07 | 1,573.18 | 100.00 | 101.97 | 6.48 | 571.71 | 36.34 | 523.44 | 33.27 | 200.79 | 12.76 | 105.49 | 6.72 | 69.78 | 4.43 |
| 2007/08 | 1,907.78 | 100.00 | 20.46 | 1.07 | 718.65 | 37.67 | 638.12 | 33.45 | 245.10 | 12.85 | 108.79 | 5.70 | 176.66 | 9.26 |
| 2008/09 | 2,724.74 | 100.00 | 95.90 | 3.52 | 942.51 | 34.59 | 962.99 | 35.34 | 319.56 | 11.73 | 168.51 | 6.18 | 235.27 | 8.63 |
| Total | 13,271.74 | 100.00 | 1,544.16 | 11.63 | 3,679.92 | 27.73 | 4,971.08 | 37.46 | 1,601.92 | 12.07 | 862.27 | 6.50 | 612.39 | 4.61 |
| Average | 1,206.52 | 100.00 | 140.38 | 11.63 | 334.54 | 27.73 | 451.92 | 37.46 | 145.63 | 12.07 | 78.39 | 6.50 | 87.48 | 4.61 |

Source:-Economic Survey 2001/02 and 2008/09, Ministry of Finance.

From the above table 4.7, total income tax revenue seemed to have an increasing trend since FY 1998/99 to FY 2000/01. It was Rs. 6,170.2 million in FY 1998/99. Then in 2001/02 and 2002/03 it decreases to Rs. 8,903.7 million and Rs. 8,131.9 million. Then again in increasing trend it reached up to Rs. 27,247.4 million in FY 2008/09.

The income tax contribution of individuals has occupied first position in average income tax revenue of Nepal during the study period. In FY 1998/99 Rs. 2,772.7 million was collected from individual income tax, percent contribution was 44.94%. It was decreasing trend. It decreased contribution to 35.34% amounting Rs. 9,629.9 million in FY 2008/09. Its maximum contribution was 49.63% in FY 2001/02 amounting Rs. 4,419.1 million and minimum was 33.27% in FY 2006/07 amounting Rs. 5,234.4 million. The average contribution was 37.46% amounting Rs. 4519.2 million during the study period.

Private corporate bodies occupied second position out of average income tax revenue during the study period. In FY1998/99, private corporate bodies paid Rs. 1,155.0 million out of Rs. 6,170.2 million i.e. 18.72% of total income tax revenue. In FY 2006/07, private corporate bodies paid Rs. 5,717.1 million out of Rs. 15,731.8 million of total income tax revenue, i.e. it contributed 36.34%. In FY 2007/08 its contribution was 37.67% it was maximum. Till FY 2007/08 it was in increasing trend but in FY 2008/09. It decreased to 34.59% amounting Rs. 9,425.1 million. The average contribution of private corporate bodies was 27.73% during the study period.

Employment occupied third position out of average income tax revenue during the study period. In 1998/99, employment paid Rs. 396.5 million out of Rs.6,170.2 million of total income tax revenue, i.e. employment contributed 6.42% of total income tax revenue that FY. In the fluctuating trend it reached to 15.40% in the FY 2002/03. Its contribution was maximum in FY 2005/06

amounting Rs.1,764.1 million. Then its contribution decreased to 12.76 % to total income tax revenue. At the end of our study period it was 11.73% amounting RS.3,195.6 million. Average contribution was 12.07% amounting Rs. 1,456.3 million during the study period.

Income tax from public enterprises has occupied fourth position regarding its contribution in average income tax revenue of Nepal during the study period. In FY 1998/099, out of total income tax revenue of Rs. 6,170.2 million Rs. 1,526.5 million has been contributed by public enterprises, which was 24.73%. Its contribution has been increasing trends up to 2000/01. Then it was fluctuated. In FY2003/04 its contribution was maximum 21.61% amounting Rs. 2056.6 out of total income tax revenue of Rs. 9,514.5 million. Minimum was In FY 2007/08, it contributed 1.07% amounting Rs. 204.6 million. In FY 2008/09 it reached to 3.52%, it was increased compared to last FY. The average contribution of public enterprises in total income tax revenue has been computed to be 11.63% amounting Rs. 1,403.8 million during the study period.

Tax on interest occupied in fifth position out of average income tax revenue during the study period. It contributed 5.19% amounting Rs.319.5 in FY 1998/99. It is fluctuating till 2002/03. Its minimum contribution was 5.10 % in 2000/01. In 2002/03 its contribution was maximum 10.64% amounting Rs. 864 million. Then it goes in decreasing trend till 2007/08 and in FY 2008/09 it again increased to 6.18% amounting Rs.1,685.1 million compared to last FY. The average contribution was 6.50% amounting Rs. 783.9 million during the study period.

Other taxes occupied last position out of average income tax revenue during the study period. It was nil in FY1998/99 to 2001/02. In 2002/03 it contributed 2.03% amounting Rs. 165.8 million. It increased to 5.17% in FY 2005/06. then there is fluctuation in its contribution. It contributed maximum in FY 2007/08,

its contribution was 9.26%. At the end of our study period in FY 2008/09 it was 8.63% amounting Rs.2,352.7 million, which was high collection in amount. So it seems that it has been growing from FY 2002/03. Contribution of semi public was nil in studying periods.

4.1.8 Collection of Total Revenue in Nepal of the Fiscal Year 2008/09

Target and collection of national are given in the following table.

Table.4.8

Target and Collection of Total Revenue in FY 2008/09

Rs. in thousand

| Types of Revenue | Target | Collection | Collection % | Collection of last year | Growth Rate |
|------------------|-----------|------------|--------------|-------------------------|-------------|
| Total Revenue | 141722110 | 143474489 | 101 | 107622480 | 33% |
| Non- Tax Revenue | 23905110 | 22892174 | 96 | 19783843 | 16% |
| Tax Revenue | 116560000 | 111092373 | 95 | 85155457 | 30% |
| Indirect Tax | 81173000 | 82731168 | 102 | 62067698 | 33% |
| Direct Tax | 35387000 | 34320739 | 97 | 23087759 | 49% |
| Principal Return | 1257000 | 3530408 | 281 | 2683180 | 32% |

Source: Yearly Report2008/09 of IRD

According to above table 4.8, target total revenue was Rs. 141,722,110 thousand but actual collection was 101% amounting Rs.143,474,489 thousand. Target non-tax revenue was Rs.23,905,110 thousand and actual collection was 96% amounting Rs.22,892,174 thousand. Target tax revenue was Rs.116,560,000 thousand and actual collection was 95% amounting Rs.111,092,373 thousand. Target indirect tax revenue was Rs. 81,173,000 thousand and actual collection was 102% amounting Rs.82,731,168 thousand. Target direct tax revenue was Rs.35,387,000 thousand and actual collection was 97% amounting Rs. 34,320,739 thousand. Target principal return was Rs. 1,257,000 thousand and collection was 281% amounting Rs. 3,530,408 thousand. Compared to last year it can be observed that Collection in each sector had increased. Growth rate of collection of total revenue is 33%, non tax revenue is 16%, tax revenue is 30%,indirect tax 33%,direct tax 49% and principal return 32%.

From the above table 4.8 it is cleared that targets of total revenue, indirect tax and payment return are met and other non-tax revenue, tax revenue and indirect tax revenue are near to target but below the target.

4.1.9 Structural Composition of Corporate Income Tax

The corporate income tax structure comprises of public and private sector. Corporate taxable income calculated by adding all the allowable expenses the corporate tax base is explained and presented in the preceding sub chapter. After the enactment of income tax act 2058, the books of account of corporate sector have been kept a little bit differently from the income tax is computed by adding public and private income tax including individual and sole trading income and other institutions too. The following table has been drawn corporate income tax from the FY1998/99to 2008/09

Table. 4.9**Structural Composition of Corporate Income Tax**

Rs. in Ten Million and Percentage

| Fiscal Year | CITR | Total | Corporate Income Tax | | | |
|----------------|-----------------|---------------|----------------------|--------------|-----------------|--------------|
| | | | Public Sector | % | Private Sector | % |
| 1998/99 | 268.15 | 100.00 | 152.65 | 56.93 | 115.50 | 43.07 |
| 1999/00 | 353.83 | 100.00 | 219.88 | 62.14 | 133.95 | 37.86 |
| 2000/01 | 485.23 | 100.00 | 292.80 | 60.34 | 192.43 | 39.66 |
| 2001/02 | 318.13 | 100.00 | 176.93 | 55.62 | 141.20 | 44.38 |
| 2002/03 | 248.73 | 100.00 | 125.10 | 50.30 | 123.63 | 49.70 |
| 2003/04 | 358.79 | 100.00 | 205.66 | 57.32 | 153.13 | 42.68 |
| 2004/05 | 380.02 | 100.00 | 133.24 | 35.06 | 246.78 | 64.94 |
| 2005/06 | 360.00 | 100.00 | 19.57 | 5.44 | 340.43 | 94.56 |
| 2006/07 | 673.68 | 100.00 | 101.97 | 15.14 | 571.71 | 84.86 |
| 2007/08 | 739.11 | 100.00 | 20.46 | 2.77 | 718.65 | 97.23 |
| 2008/09 | 1,038.41 | 100.00 | 95.90 | 9.24 | 942.51 | 90.76 |
| Total | 5,224.08 | 100.00 | 1,544.16 | 34.60 | 3,679.92 | 65.39 |
| Average | 474.92 | 100.00 | 140.38 | 3.46 | 334.54 | 6.53 |

Source:-Economic Survey 2001/02 to 2009/10, Ministry of Finance.

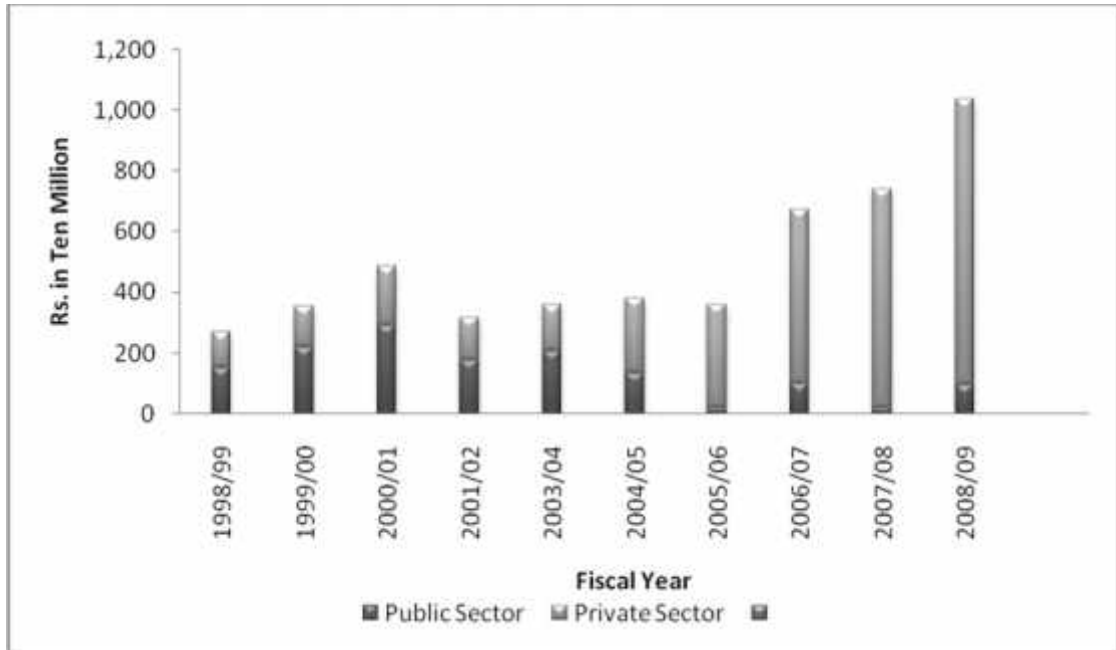
The above structural composition of corporate tax shows that major portion was covered by public sector in initial stages. It was 56.93% in the FY 1998/99 while the private sector contributed 43.07% in FY 1998/99.

The table 4.9 shows that major portion was covered by private sector at last stages. The share of private sector increased 94.46% in FY2005/06. The maximum increased to 97.23% in FY2007/08. Public sector seems to be in decreasing trend and reached to 2.77% in FY 2007/08. The CITR was Rs. 2,681.5 million in FY 1998/99, it was fluctuated to reach to Rs. 10,384.1 million in FY 2008/09. Total CITR is in increasing trend, the average contribution of private and public sector were 70.44% and 29.56% respectively. It is due to the increasing culture of privation after industrialization. The maximum contribution of private sector was 97.23% in FY 2007/08 and minimum was 37.86% in FY 1999/00. The maximum contribution of public sector was 62.14% amounting Rs. 2,198.8 million in FY 1999/00 and minimum was 2.77% in FY 2007/08.

The structural composition of CITR can be presented in bar diagram and chart from 1998/99 to 2008/09 as follows:

Figure 4.7

Bar Graph Showing CITR and its Composition

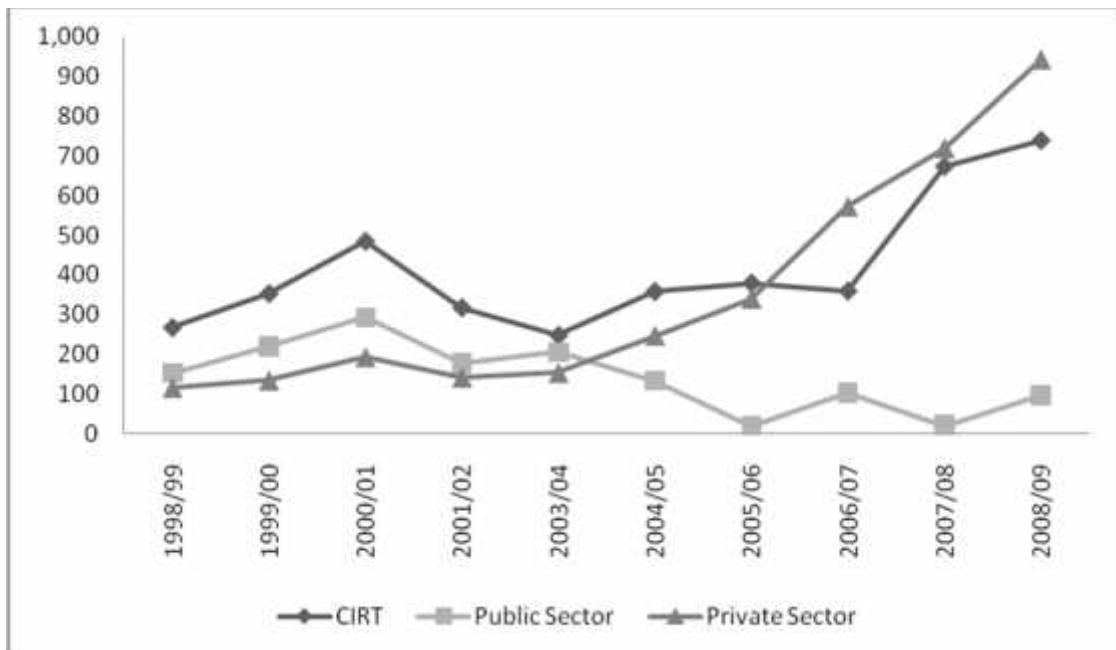


Source: table 4.9

In the above bar diagram different years are shown in X-axis and CITR shown in Y-axis.

Figure 4.8

Trend Line Showing Components of CITR



Source: Table 4.9

The above trend line represents the CITR, public sector and private sector respectively. It shows that the CITR was mostly fluctuated during the study period.

There was increased distance between public and private sector. It is cleared that public sector is decreasing and private sector is growing trend. The average contribution of public sector and private sector to CITR from FY 1998/99 to 2008/09 were 29.56% and 70.44% respectively.

4.1.10 Contribution of Corporate Income Tax Revenue on Income Tax Revenue

Income tax revenue includes corporate income tax, individual's income tax, employment, interest tax and others. The size of income tax revenue largely depends upon the size of corporate sector. Higher the size of corporate sector higher will be the CITR and total income tax revenue and vice versa so, CITR in Nepal has played a vital role in income tax revenue. Contribution of CITR to total income tax revenue is given as following table.

Table 4.10

Contribution of Corporate Income Tax Revenue on Income Tax Revenue from the FY 1998/99 to 2008/09

Rs. in Ten Million and Percentage

| Fiscal Year | Income Tax | Total % | Corporate Income Tax | | | | Total CITR | % |
|-------------|------------|---------|----------------------|-------|----------------|-------|------------|-------|
| | | | Public sector | % | Private Sector | % | | |
| 1998/99 | 617.02 | 100.00 | 152.65 | 24.74 | 115.50 | 18.72 | 268.15 | 43.46 |
| 1999/00 | 742.06 | 100.00 | 219.88 | 29.63 | 133.95 | 18.05 | 353.83 | 47.68 |
| 2000/01 | 911.40 | 100.00 | 292.80 | 32.13 | 192.43 | 21.11 | 485.23 | 53.24 |

| | | | | | | | | |
|----------------|------------------|---------------|-----------------|--------------|-----------------|--------------|-----------------|--------------|
| 2001/02 | 890.37 | 100.00 | 176.93 | 19.87 | 141.20 | 15.86 | 318.13 | 35.73 |
| 2002/03 | 813.19 | 100.00 | 125.10 | 15.38 | 123.63 | 15.20 | 248.73 | 30.59 |
| 2003/04 | 951.45 | 100.00 | 205.66 | 21.62 | 153.13 | 16.09 | 358.79 | 37.71 |
| 2004/05 | 1,046.61 | 100.00 | 133.24 | 12.73 | 246.78 | 23.58 | 380.02 | 36.31 |
| 2005/06 | 1,093.94 | 100.00 | 19.57 | 1.79 | 340.43 | 31.12 | 360.00 | 32.91 |
| 2006/07 | 1,573.18 | 100.00 | 101.97 | 6.48 | 571.71 | 36.34 | 673.68 | 42.82 |
| 2007/08 | 1,907.78 | 100.00 | 20.46 | 1.07 | 718.65 | 37.67 | 739.11 | 38.74 |
| 2008/09 | 2,724.74 | 100.00 | 95.90 | 3.52 | 942.51 | 34.59 | 1,038.41 | 38.11 |
| Total | 13,271.74 | - | 1,544.16 | 11.63 | 3,679.92 | 27.73 | 5,224.08 | 39.36 |
| Average | 1,206.52 | 100.00 | 140.38 | 11.63 | 334.54 | 27.73 | 474.92 | 39.36 |

Source:-Economic Survey 2001/02 and 2008/09, Ministry of Finance.

Above table reflects that the contribution of CITR to income tax revenue seems to be in increasing trend in the first two year it reached to 53.24% amounting Rs.4,852.3 million in FY 2000/01 which was maximum during the study period. Then it started decreasing till 2002/03 and reached to 30.59% amounting Rs. 2,487.3 million which was minimum during the study period. The structural composition of corporate sector seemed to be fluctuating during the study period.

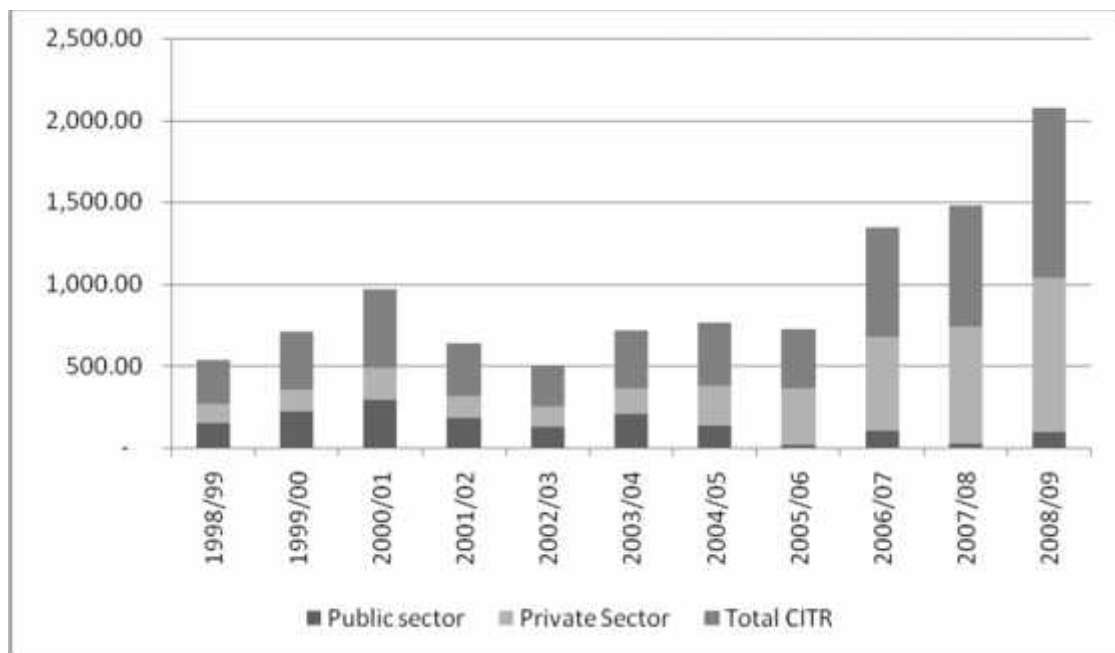
In FY 1998/99, 24.74% and 18.72% contribution was made by public and private sector respectively which changed to 3.52% and 34.59% respectively in FY 2008/09. It seems that tax collection from private sector was increasing and public sector was decreasing. Maximum contribution form public sector and private sector was in the same FY 2000/01 which was 32.13% and 53.24% respectively.

In average Total CIRT contributed 39.36% to the income tax in which 27.73% and 11.63% is from Private and public sector respectively.

The CIRT and income tax revenue position has been shown from 1998/99 to 2008/09 in the following bar diagram and chart:

Figure 4.9

Sub-Bar Diagram of CIRT and Income Tax Revenue

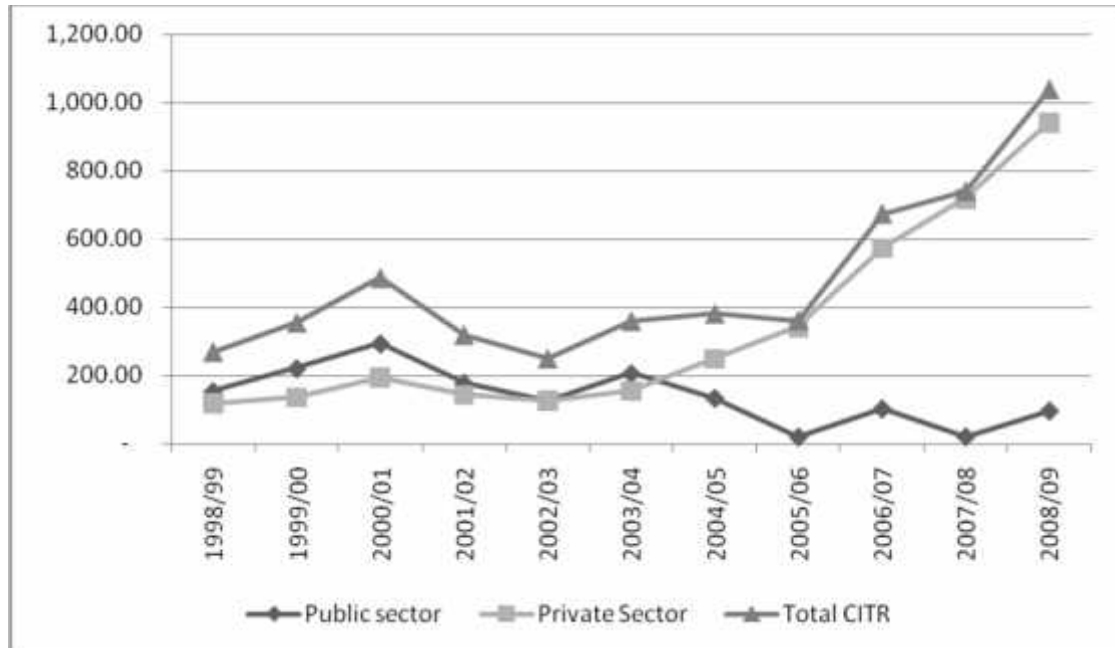


Source: Table 4.10

In the above bar diagram different years are shown in X-axis and total income tax revenue is shown in Y-axis. Where we can see the maximum contribution of CIRT to income tax revenue in 2000/01, then it share continuously decreased up to FY 2002/03.

Figure 4.10

Trend Line Showing Income Tax Revenue and CITR



Source: Table 4.10

Above trend line shows that total CITR was increasing up to 2008/09. Income from Public sector was height in the initial FY later it goes decreasing. Just opposite to it, Private sector was very low at the beginning and it goes on increasing during our study period. Till 2008/09 private sector is contributing almost total of CITR The relationship between CITR and income tax revenue from the FY 1998/99 to 2008/09 is positive.

4.1.11 Structure of Customs in Nepal from 1998/99 to 200/09

Customs is the main source of tax revenue in Nepal. The main source of customs is imports, exports, Indian excise refund and others. Composition of customs is given in the following table.

Table 4.11**Custom duties from 1998/99 to 2008/09****Major source of Custom duties and their relative percentage from****Rs in Ten Million and Percentage**

Source: Economic Survey 2001/02 and 2008/09

| Year | Custom Revenue | Total % | Imports | | Exports | | Indian Excise Refund | | Others | |
|----------------|------------------|---------------|------------------|--------------|---------------|-------------|----------------------|--------------|---------------|-------------|
| | | | Rs. | % | Rs. | % | Rs. | % | Rs. | % |
| 1998/99 | 951.77 | 100.00 | 769.83 | 80.88 | 37.80 | 3.97 | 120.60 | 12.67 | 23.54 | 2.47 |
| 1999/00 | 1,081.33 | 100.00 | 895.99 | 82.86 | 43.25 | 4.00 | 133.17 | 12.32 | 8.92 | 0.82 |
| 2000/01 | 1,255.21 | 100.00 | 1,039.19 | 82.79 | 49.26 | 3.92 | 145.62 | 11.60 | 21.14 | 1.68 |
| 2001/02 | 1,265.88 | 100.00 | 967.84 | 76.46 | 91.74 | 7.25 | 170.09 | 13.44 | 36.21 | 2.86 |
| 2002/03 | 1,423.64 | 100.00 | 1,056.77 | 74.23 | 85.56 | 6.01 | 237.06 | 16.65 | 44.25 | 3.11 |
| 2003/04 | 1,555.48 | 100.00 | 1,066.69 | 68.58 | 52.71 | 3.39 | 388.27 | 24.96 | 47.81 | 3.07 |
| 2004/05 | 1,570.16 | 100.00 | 1,229.91 | 78.33 | 69.79 | 4.44 | 218.83 | 13.94 | 51.63 | 3.29 |
| 2005/06 | 1,534.40 | 100.00 | 1,174.46 | 76.54 | 62.56 | 4.08 | 231.44 | 15.08 | 65.94 | 4.30 |
| 2006/07 | 1,670.76 | 100.00 | 1,362.61 | 81.56 | 70.87 | 4.24 | 189.65 | 11.35 | 47.63 | 2.85 |
| 2007/08 | 2,106.25 | 100.00 | 1,712.82 | 81.32 | 44.56 | 2.12 | 299.71 | 14.23 | 49.16 | 2.33 |
| 2008/09 | 2,679.29 | 100.00 | 2,205.66 | 82.32 | 79.64 | 2.97 | 321.11 | 11.98 | 72.88 | 2.72 |
| Total | 17,094.17 | 100.00 | 13,481.77 | 78.87 | 687.74 | 4.02 | 2,455.55 | 14.36 | 469.11 | 2.74 |
| Average | 1,554.02 | 100.00 | 1,225.62 | 78.87 | 62.52 | 4.02 | 223.23 | 14.36 | 42.65 | 2.74 |

According to the above table 4.11 imports is the main source of customs. Import was 80.88% amounting Rs. 7,698.3 in FY 1998/99 and it increased to 82.79% amounting Rs. 10,391.9 million in FY 2000/01. It decreased to Rs. 9,678.4 in the FY 2001/02 then again it is always in the increasing trend till

2008/09 and reached to 22,056.6 million. But the percentage of contribution to total custom revenue is seen to be fluctuated time and again during the study period. The minimum contribution was 68.57% amounting Rs.10666.9 in FY 2003/04 and maximum contribution was 82.86% amounting Rs. 8,959.9 million in FY 1999/00.

Contribution of export was 3.97% amounting Rs. 378.0 million in FY1998/99 which was the beginning of our study period, it fluctuated all the time and it was 2.97% amounting Rs.796.4 million in the FY 2008/09.The contribution of export to the total custom revenue is fluctuating both in the percentage and in amount. The maximum contribution was 7.25% in FY 2001/02 and minimum was 2.12% in FY 2007/08. The average contribution of Export to custom revenue was 4.02% till 2008/09 amounting Rs.625.2 million.

Contribution of Indian excise refund was 12.67% amounting Rs. 1,206 million in FY 1998/99 and it decreased to 11.06% amounting Rs. 1,456.2 million in FY 2000/01. Then time and again it is increasing and decreasing trend. The maximum contribution of Indian excise refund was 24.96% amounting Rs. 3,882.7 million in FY 2003/04.The minimum contribution of Indian excise refund was 11.35% amounting Rs. 1,896.5 million in FY 2006/07. The average contribution of Indian excise refund to custom revenue till our study period 2008/09 was 11.98% amounting Rs. 3,211.1 million.

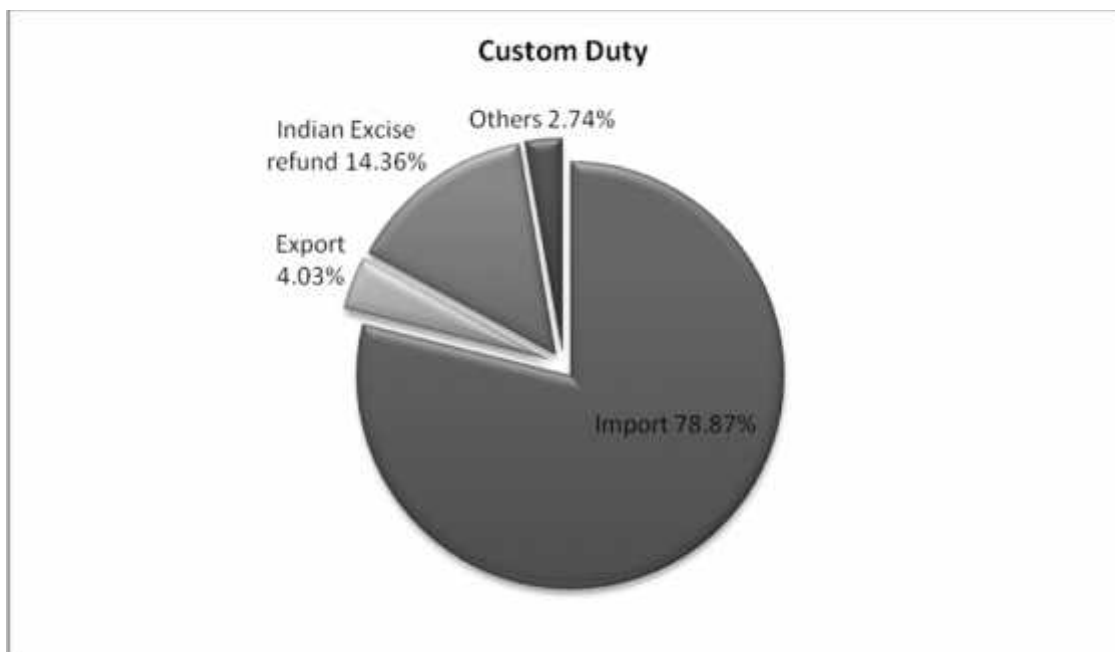
The contribution of others was 2.47% amounting Rs. 235.4 million in FY 1998/99 and it was decreased to 0.82% amounting Rs. 89.2 million in FY 1999/00 which was the minimum contribution till 2008/09.It fluctuated every year and at the end of our study period in FY 2008/09 it was 2.72% amounting Rs. 728.8. Maximum contribution was Rs. 4.30% amounting Rs. 659.4 million in FY 2005/06.

The average contribution of Imports, exports and others to custom duty were 78.87%, 4.02% and 2.74% amounting Rs.12,256.2 million, Rs.625.2 million and Rs. 426.5 million respectively during the study period. Large part of custom duty is covered by import duty. There is vast difference between Revenue Income from import and export.

The contribution of average amount can be presented as pie chart.

Figure 4.11

Pie Chart of Composition of Customs



Source: Table 4.11

Maximum area was occupied by the Import in the above pie chart. So, import was the one of the main source of customs.

4.1.12 Overall revenue Structure in Nepal

Composition of national revenue can be presented as overall revenue structure

Table 4.12

Summary of National Revenue in Nepal

| F.Y | 1998/99 | | 1999/00 | | 2000/01 | | 2001/02 | | 2002/03 | | 2003/04 | | 2004/05 | | 2005/06 | | 2006/07 | | 2007/08 | | 2008/09 | |
|-------------------|-----------------|------------|-----------------|------------|-----------------|------------|-----------------|------------|-----------------|------------|----------------|------------|----------------|------------|----------------|------------|----------------|------------|-----------------|------------|-----------------|------------|
| | Rs. | % | Rs | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % | Rs. | % |
| Total Rev. | 3,725.10 | 100 | 4,289.37 | 100 | 4,889.39 | 100 | 5,044.56 | 100 | 5,622.97 | 100 | 6,233.1 | 100 | 7,012.2 | 100 | 7,228.2 | 100 | 8,771.2 | 100 | 10,762.2 | 100 | 14,347.4 | 100 |
| N.TR | 849.81 | 22.8 | 974.16 | 22.7 | 1,002.88 | 20.51 | 1,111.50 | 22.04 | 1,364.29 | 25.01 | 1,415.8 | 22.71 | 1,601.8 | 22.84 | 1,485.1 | 20.55 | 1,658.5 | 18.42 | 2,246.70 | 21.03 | 2,642.26 | 18.42 |
| Tax Rev. | 2,875.29 | 77.1 | 3,315.21 | 77.2 | 3,886.51 | 79.49 | 3,933.06 | 77.96 | 4,089.60 | 74.99 | 4,817.5 | 77.29 | 5,410.4 | 77.16 | 5,743.0 | 79.45 | 7,112.6 | 81.58 | 8,515.55 | 78.97 | 11,705.1 | 81.58 |
| IDTR | 2,123.68 | 100 | 2,420.06 | 100 | 2,870.57 | 100 | 2,873.31 | 100 | 3,248.10 | 100 | 3,626.0 | 100 | 4,103.2 | 100 | 4,346.2 | 100 | 5,214.6 | 100 | 6,206.78 | 100 | 8,271.47 | 100 |
| Custom | 951.77 | 44.8 | 1,081.33 | 44.6 | 1,255.21 | 43.73 | 1,265.88 | 44.06 | 1,423.64 | 43.83 | 1,555.4 | 42.90 | 1,570.1 | 38.27 | 1,534.4 | 35.30 | 1,670.7 | 32.04 | 2,106.75 | 33.93 | 2,679.29 | 32.39 |
| Excise | 295.32 | 13.9 | 312.76 | 12.9 | 377.12 | 13.14 | 380.70 | 13.25 | 478.51 | 14.73 | 622.67 | 17.17 | 644.59 | 15.71 | 650.76 | 14.97 | 934.32 | 17.92 | 1,118.96 | 18.03 | 1,622.09 | 19.61 |
| VAT | 876.59 | 41.2 | 1,025.97 | 42.4 | 1,238.24 | 43.13 | 1,226.73 | 42.69 | 1,447.89 | 39.93 | 2,609.5 | 50.04 | 1,345.9 | 41.44 | 1,888.5 | 46.02 | 2,161.0 | 49.73 | 2,981.57 | 48.04 | 3,970.09 | 48.00 |
| DT | 751.61 | 100 | 895.15 | 100 | 1,015.94 | 100 | 1,059.75 | 100 | 1,010.58 | 100 | 1,191.2 | 100 | 1,307.1 | 100 | 1,396.8 | 100 | 1,898.0 | 100 | 2,308.77 | 100 | 3,432.07 | 100 |
| Income | 617.03 | 82.0 | 742.06 | 82.9 | 911.40 | 89.71 | 890.37 | 84.02 | 813.19 | 80.47 | 951.47 | 79.87 | 1,046.6 | 80.07 | 1,093.9 | 78.32 | 1,573.1 | 82.88 | 1,907.78 | 82.63 | 2,724.74 | 79.39 |
| H&L Reg. | 100.32 | 13.3 | 101.59 | 11.3 | 61.29 | 6.03 | 113.18 | 10.68 | 141.43 | 14.00 | 169.75 | 14.25 | 179.92 | 13.76 | 218.11 | 15.61 | 225.35 | 11.87 | 294.07 | 12.74 | 522.34 | 15.22 |
| Vehicle | 34.27 | 4.56 | 51.50 | 5.75 | 43.25 | 4.26 | 56.20 | 5.30 | 55.95 | 5.53 | 70.06 | 5.88 | 80.65 | 6.17 | 84.76 | 6.07 | 99.50 | 5.24 | 106.92 | 4.63 | 185.00 | 5.39 |

Source: Economic survey 2001/02 and 2008/09, Annual Report of IRD 2007/08 and Budget Speech 2009/010

Since 1998/99 to 2001/02: Land Revenue has been included in house land registration.

Urban House and Land Tax have been included in vehicle tax. Now, these are not government revenue.

According to above table 4.12 it is cleared that there are different sources of national revenue.

National revenue can be classified into tax revenue and non-tax revenue. Tax revenue always has greater amount than non tax revenue. Tax revenue contributed 77.19% to total revenue in FY 1998/99 and reached to 81.85% in FY 2008/09 fluctuating time and again. Whereas non tax revenue contributed only 22.81% in FY 1998/99 and reached to 18.42%. Tax revenue always contributed more than non tax revenue. Tax revenue can be classified into direct tax revenue and indirect tax revenue. From the above table, Indirect tax revenue always has greater amount than direct tax revenue. Indirect tax revenue was Rs.21,236.8 million in FY 1998/99 whereas Direct tax collection was only Rs.7,516.1 million. Both direct tax revenue and indirect tax revenue are increasing every year but contribution of indirect tax is always higher than direct tax. At the End of our study period in FY 2008/09 Indirect tax contributed Rs. 82,734.7 million and direct tax contributed Rs.34,320.7 million. Custom duties, Excise duty and VAT are main components of indirect tax in Nepal. Custom duties took greater part of indirect tax in initial period, but VAT played vital role in ending period. Custom duty contributed to IDT by 44.82% in FY 1998/99 and VAT contributed to IDT by 41.27% in FY1998/99. Excise contributed to IDT by 13.91% in FY 1998/99. Custom was decreasing trend and Excise was increasing comparatively during the study period. Custom contributed 32.39% in FY 2008/09, VAT contributed 48% and Excise contributed 19.61%. The VAT has become an important source of overall

tax revenue with fluctuating trend which contributed 41.28% in FY 1998/99. Percentage of maximum contributed was 50.04% in FY 2006/07. It reached up to 48.00% in the FY 2008/09. The average of VAT contribution was 45.85% during the study period. In average highest contribution was from VAT which is 45.85%, next is custom duty and excise duty having 37.73% and 16.42% respectively.

Income tax House and Land registration and Vehicle tax are main components of direct tax revenue in Nepal. From the above table, Income tax was one of major component of direct tax revenue. It played vital role to increase or decrease direct tax revenue. Income tax revenue a little fluctuated during the study period. It contributed 82.09% in FY 1998/99 and reached to 89.71% in FY 2000/01 during the study period. Income tax contributed 82.63% in FY 2007/08 and decrease to 79.39% in FY 2008/09. House and Land Registration contributed 13.35% amounting Rs. 1,003.2 million in FY 1998/99 and reached to 15.61% in FY 2005/06 during the study period. It contributed 15.22% amounting Rs. 5,223.4 million in FY 2008/09. Vehicle tax is the part of direct tax revenue which contributed to direct tax 4.56% amounting Rs. 342.7 million in FY 1998/99 and reached to 6.17% amounting Rs. 806.5 in FY 2004/05 during the study period which was maximum till 2008/09. It was 5.39% amounting Rs.1,850 million in FY 2008/09. In average Income tax contributes maximum to direct tax revenue. House and land registration comes in second position and vehicle tax provides less to direct tax revenue.

We can see from the above table the sources of overall revenue collection of Nepal.

4.2 Problems of Resources Gap in Nepal

The resources mobilization is the main challenge in the economic development of the country. The internal resource plays vital role in economic development of the country. Government collects their resources from different ways. The tax structure is major source of revenue for the government. Government has imposed two types of tax like direct and indirect tax. In the present tax structure the government revenue comes more from indirect taxes than that of direct tax. Tax policy has to be made a part of the instrument of the development goals.

The resource mobilization has been a major problem in financing of growing government expenses. Since the beginning of planned development of Nepal there has been tremendous increment in the size of government expenditure. The development works have to be carried out by the government in the initial stage. An increase in government expenditure creates additional demand in the economy through multiplier effects and there by induces arise in aggregate output. The government resources have been concentrated more on expanding economic over head in the form of transport, power and communication which will simulate agriculture, industry and transport in the private sectors.

The government expenditure is the main source of gross national investment and capital formation. Many studies have been attempted to examine the problem of resource gap and prospect of internal resource gap is the amount of excluding net foreign grants and loans. But the overall resource gap includes the contributions made by foreign grants and loans in financing public expenditure. The problem of resource gap has increased from one year to another which been recovered through massive inflow if external capital regular expenditure is fulfilled by internal resources where as development expenditure is mostly depending in external resources. The dependence on foreign aid and deficit

finance has not shown any declining trend. If the resource gap is minimized through the over dependence of foreign loans it can further creates the resource problem in the near future.

The problem of resource mobilization and resource gap is related to the saving and investment the level of income and the rate of interest influence the saving structure. The low rate of saving is prevailing in the country as result of low level of income of the people the low level of income creates the problem of resource mobilization for undertaking investment programmed in a large scale by both government and private sector.

Table 4.13

Domestic Resource Gap Pattern of Nepal

from the FY 1998/99 to 2008/09

Rs. in Ten Million

| Fiscal Year | Total Govt. Exp.(A) | Total Govt. Revenue (B) | Resource Gap (A-B) | % of resource Gap |
|-------------|---------------------|-------------------------|--------------------|-------------------|
| 1998/99 | 5,957.90 | 3,725.10 | 2,232.80 | 37.48 |
| 1999/00 | 6,627.25 | 4,289.37 | 2,337.88 | 35.28 |
| 2000/01 | 7,983.51 | 4,889.39 | 3,094.12 | 38.76 |
| 2001/02 | 8,007.22 | 5,044.56 | 2,962.66 | 37.00 |
| 2002/03 | 8,400.61 | 5,622.97 | 2,777.64 | 33.06 |
| 2003/04 | 8,944.26 | 6,233.10 | 2,711.16 | 30.31 |

| | | | | |
|----------------|-------------------|------------------|------------------|---------------|
| 2004/05 | 10,256.04 | 7,012.27 | 3,243.77 | 31.63 |
| 2005/06 | 11,088.92 | 7,228.21 | 3,860.71 | 34.82 |
| 2006/07 | 13,360.46 | 8,771.22 | 4,589.24 | 34.34 |
| 2007/08 | 16,134.99 | 10,762.25 | 5,372.74 | 33.30 |
| 2008/09 | 21,966.19 | 14,347.45 | 7,618.74 | 34.68 |
| Total | 118,727.35 | 77,925.89 | 40,801.46 | 380.66 |
| Average | 10,793.40 | 7,084.17 | 3,709.22 | 34.61 |

Source: Economic Survey 2001/02 and 2008/09, Budget Speech 2009/10

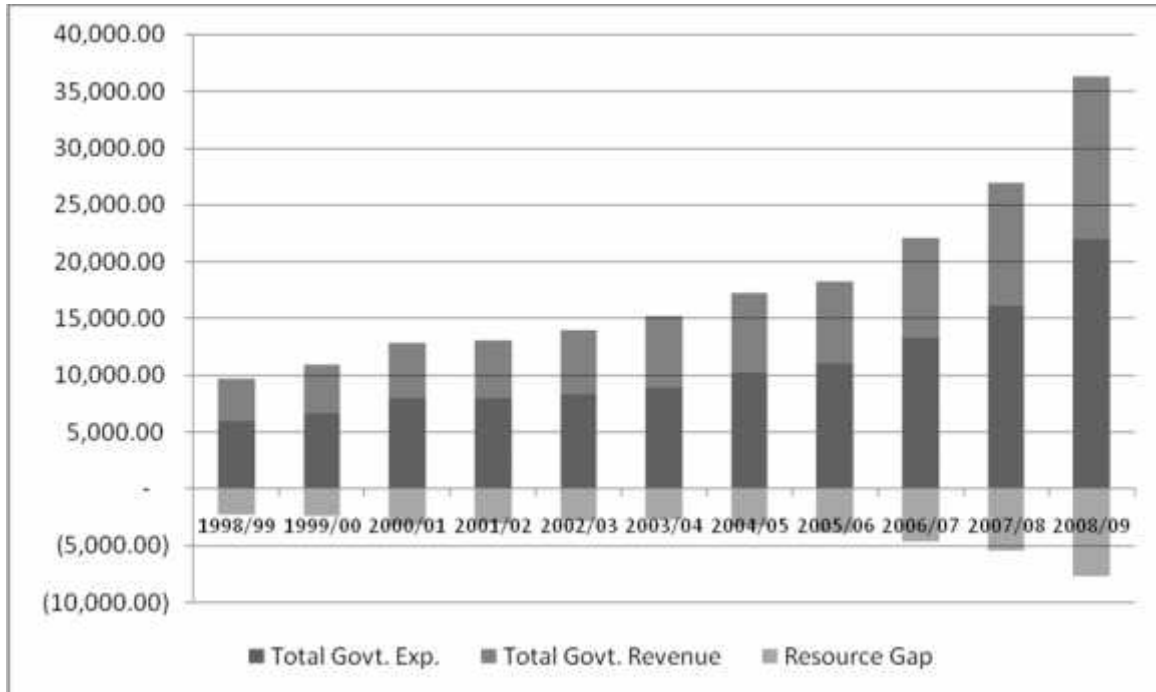
From the above table 4.2 it is found that during the last 11 years period Government expenditure is increasing. Though government revenue is also in increasing trend but it can't afford government expenditure. That's why with the increasing government expenditure, resource gap is also in increasing trend. Government expenditure was Rs. 59,579 million and revenue was Rs. 37,251 million in 1988/99 that year resource gap was Rs. 22,328 million which was 37.48%. With increasing trend government expenditure and revenue reached to Rs. 219,661.9 million and Rs. 143,474.5 million respectively in FY 2008/09 it created the resource gap of Rs. 76,187.4 million which was 34.68%.

Revenue should be greater than the total Govt. expenditure to reduce the resource gap. Nepal fulfills some of these resource gaps by foreign aid like grant, loan etc.

Bar Diagram showing resource gap is given below.

Figure 4.12

Bar Diagram Showing Resource Gap



Source: Table 4.2

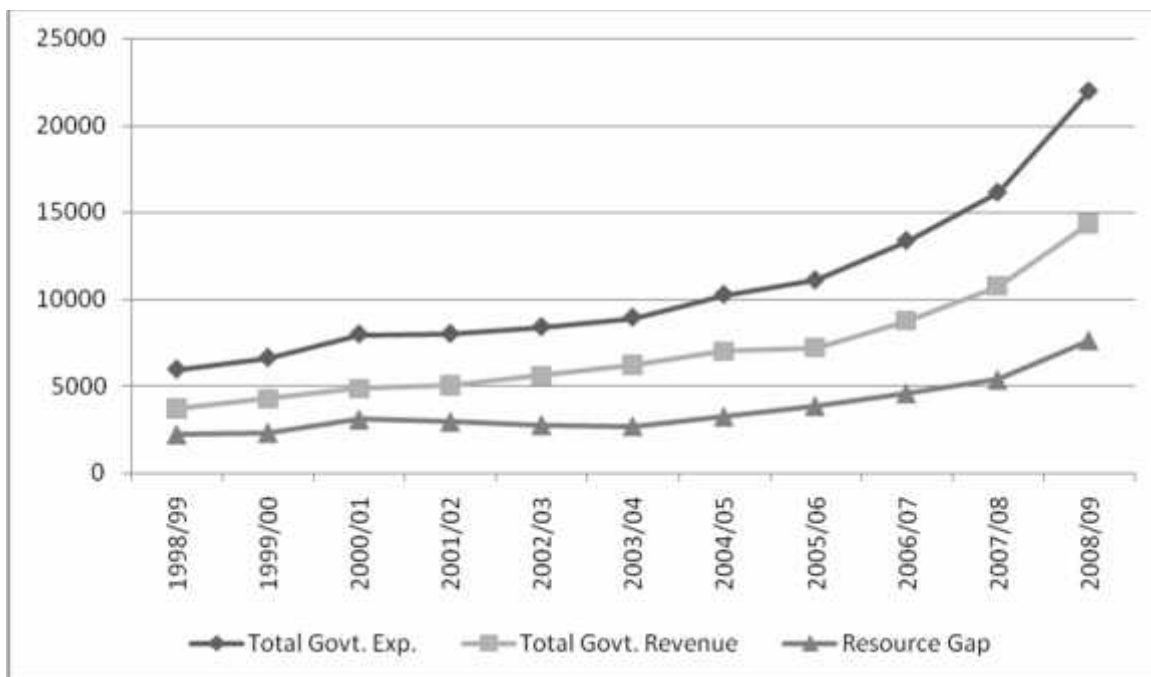
In the above subdivided bar diagram higher part (dark shaded portion) is government Expenditure, little fewer part above the origin or above the x-axis is government revenue. Since resource gap is the difference between expenditure and revenue it represents loss and shown below the origin or x-axis.

It can be presented as trend line given below:

Figure 4.13

Trend Line Showing Resource Gap in Nepal

Source: Table 4.2



The above trend line shows that the total government expenditure is high and at the top among three trend lines. Second one is government revenue which is less than government expenditure and comes below the government expenditure. Resource gap is the last line, it is cleared that the amount of resource gap is growing every year. Total expenditure is increasing highly but total revenue is increasing slowly.

4.2.1 Revenue Expenditure

Revenue expenditure gap is known as resource gap. In this contest, three types of gaps are measured and used in the analysis of resource gap. The table has been given below:

Table 4.14

Overall Resource Gap Pattern of Nepal

from the FY 1998/99 to 2008/09

Rs. in Ten Million

| FY | Total Govt. Ex. (A) | Total Govt. Revenue (B) | Resource Gap-1 (A-B) | Foreign Grants (C) | Resource Gap-2 A-(B+C) | Foreign Loan (D) | Resource Gap-3 A-(B+C+D) |
|---------|---------------------|-------------------------|----------------------|--------------------|------------------------|------------------|--------------------------|
| 1998/99 | 5,957.90 | 3,725.10 | 2,232.80 | 433.66 | 1,799.14 | 1,185.24 | 613.90 |
| 1999/00 | 6,627.25 | 4,289.37 | 2,337.88 | 511.77 | 1,826.11 | 1,181.22 | 644.89 |
| 2000/01 | 7,983.51 | 4,889.39 | 3,094.12 | 675.34 | 2,418.78 | 1,204.40 | 1,214.38 |
| 2001/02 | 8,007.22 | 5,044.56 | 2,962.66 | 668.61 | 2,294.05 | 769.87 | 1,524.18 |
| 2002/03 | 8,400.61 | 5,622.97 | 2,777.64 | 1,133.91 | 1,643.73 | 454.64 | 1,189.09 |
| 2003/04 | 8,944.26 | 6,233.10 | 2,711.16 | 1,128.34 | 1,582.82 | 762.90 | 819.92 |
| 2004/05 | 10,256.04 | 7,012.27 | 3,243.77 | 1,439.12 | 1,804.65 | 926.61 | 878.04 |
| 2005/06 | 11,088.92 | 7,228.21 | 3,860.71 | 1,382.75 | 2,477.96 | 821.43 | 1,656.53 |
| 2006/07 | 13,360.46 | 8,771.22 | 4,589.24 | 1,580.08 | 3,009.16 | 1,005.35 | 2,003.81 |

| | | | | | | | |
|---------|------------|-----------|-----------|-----------|-----------|-----------|-----------|
| 2007/08 | 16,134.99 | 10,762.25 | 5,372.74 | 2,032.07 | 3,340.67 | 897.99 | 2,442.68 |
| 2008/09 | 21,966.19 | 14,347.45 | 7,618.74 | 2,638.28 | 4,980.46 | 996.89 | 3,983.57 |
| Total | 118,727.35 | 77,925.89 | 40,801.46 | 13,623.93 | 27,177.53 | 10,206.54 | 16,970.99 |
| Average | 10,793.40 | 7,084.17 | 3,709.22 | 1,238.54 | 2,470.68 | 927.87 | 1,542.82 |

Source: Economic Survey 2001/02 and 2009/10, Budget Speech 2009/10

Resource Gap 1(A-B)

It is taken as difference between total expenditure and total revenue .This resource gap was Rs. 22,328 million in Fiscal Year 1998/99 it was minimum gap of resource during the study period. Resource gap is always in increasing trend and reached to maximum Rs.76,187.4 million in FY 2008/09. From the table, it was cleared that this type resource gap was increasing trend. The average resource gap was Rs. 37,092.2 million.

Resource Gap 2 A-(A-B)

This resource gap is after the foreign grants. It is taken as difference between total expenditure and total revenue plus foreign grants. This type of resource gap was Rs. 17,991.4 million for the FY 1998/99 which was increased to Rs. 49,804.6 million in FY 2008/09 which was also maximum resource gap. The minimum resource gap was Rs. 15,828.2 million in FY 2003/04. Government expenditure was increasing every year, but not sufficient increased government revenue so resource gap was also growing. It shows that foreign grants should be encouraged to increase for minimizing the resource gap. The average resource gap was Rs. 24,706.8 million during the study period.

Resource Gap 3 A-(B+C+D)

This resource gap is taken as the difference between total expenditure and total revenue plus foreign grants plus foreign loan. In FY 1998/99 the gap was minimum Rs. 6,139.0 which was increased to Rs. 39,835.7million in FY 2008/09, it was maximum resource gap. The average gap was Rs. 15,428.2 million during the study period.

Moreover, foreign loan largely depends on the fiscal policy adopted by the nation. Foreign loan creates extra burden to the economy because debt servicing charge increase every year. The foreign loan should be taken as a complementary resource. Focused should be in mobilizing internal resource properly.

4.2.2 Problems in Public Expenditure

Government expenditure is increasing along with its expanding activities in development and social activities. The increasing trend of government expenditure can be fulfilled either by internal resources or through inflow of foreign aid. The increasing rate of growth in government expenditures creates many problems in public expenditure management. As a result, deficit financing takes place in the economy. On the one hand resource gap problem is increasing and on the other hand it has grown the inflation and price UN stabilization in the economy. There is two ways relationship between resource mobilization and expansion is budgetary in developing country.

Government policy should be reformed for maximum resource mobilization in accordance with the expansion in economy that has taken place through the investment of public sector in development activities.

Development expenditure is mostly prepared in accordance with commitment of the donor agencies. But the disbursement of foreign aid has not been as per the commitment the lack of funding compels to delay the completion of the project. In the same way the donor agencies are too much involved in the decision making which creates many problems in implementation and for the completed project by the finding agencies the problem stands to the government on the operation and maintains of the project.

Table 4.15

Share of Government Revenue and Foreign Aid

from the FY 1998/99 to 2008/09

Rs. In Ten million and percentage

| Fiscal Year | Total Govt. Exp. (A) | Total Govt. Revenue (B) | Total Rev. as % of Total Govt. Expenditure | Foreign Aid | Foreign Aid as % of Total Govt. Expenditure |
|-------------|----------------------|-------------------------|--|-------------|---|
| 1998/99 | 5,957.90 | 3,725.10 | 62.52 | 1,618.90 | 27.17 |
| 1999/00 | 6,627.25 | 4,289.37 | 64.72 | 1,752.39 | 26.44 |
| 2000/01 | 7,983.51 | 4,889.39 | 61.24 | 1,879.74 | 23.55 |
| 2001/02 | 8,007.22 | 5,044.56 | 63.00 | 1,438.48 | 17.96 |
| 2002/03 | 8,400.61 | 5,622.97 | 66.94 | 1,588.55 | 18.91 |

| | | | | | |
|----------------|-------------------|------------------|--------------|------------------|--------------|
| 2003/04 | 8,944.26 | 6,233.10 | 69.69 | 1,891.24 | 21.14 |
| 2004/05 | 10,256.04 | 7,012.27 | 68.37 | 2,365.73 | 23.07 |
| 2005/06 | 11,088.92 | 7,228.21 | 65.18 | 2,204.18 | 19.88 |
| 2006/07 | 13,360.46 | 8,771.22 | 65.65 | 2,585.43 | 19.35 |
| 2007/08 | 16,134.99 | 10,762.25 | 66.70 | 2,930.06 | 18.16 |
| 2008/09 | 21,966.19 | 14,347.45 | 65.32 | 3,635.17 | 16.55 |
| Total | 118,727.35 | 77,925.89 | 65.63 | 23,889.87 | 20.12 |
| Average | 10,793.40 | 7,084.17 | 65.63 | 2,171.81 | 20.12 |

Source: Economic Survey 2001/02 and 2008/09, Budget Speech 2009/10

Table indicates the contribution of government revenue and foreign grants in financing public expenditure. Total government revenue was only 62.52% of total government expenditure in FY 1998/99. Maximum share of revenue to expenditure was 69.69% in FY 2003/04 and minimum was 61.24% in FY 2000/01 during the study period. In average the government revenue was 65.63% of total government expenditure. It shows that Nepal government is not able to cut its cloth according to its coat. There is 34.37% resource gap which is generally covered by foreign grants, loan and other sources.

Similarly, the contribution made by foreign aid comprising both foreign grants and loan came to 20.12% amounting Rs. 21,718.1 million on average. It is also clear from the table that contribution made by foreign aid to government expenditure was fluctuated during the study period. It was maximum 21.17% in FY 1998/99 and reached to 16.55% in FY 2008/09 which was minimum till our

study period. It is in decreasing trend since last five years i.e. FY 2004/05 The Conclusion from the above analysis is that government disserving is increasing every year. Government's expenditure is increasing at a higher rate than the growth of government revenue. The growth rate of domestic saving has not increased substantially even the external capital inflow has been increasing with higher rate. As a consequence of which the resource gap is highly increasing instead of minimizing.

4.3 Empirical Investigation

An empirical investigation has been conducted in order to find out various aspects of tax imposition in Nepal. This chapter analysis information collected from primary sources i.e., through questionnaire. The questionnaire was distributed to the tax administrator's, tax exports and tax payers. The responses received from various respondents have been arranged tabulated and analyzed in order to facilitate the descriptive analysis of the study.

The questionnaire was asked either for a yes/no response or asked for ranking of the choices according to the number of alternatives where the first choice was the most important the last choice was the important. For analysis purpose choices were assigned weight according to the number of alternatives. If the number of alternatives were five the first preferred choice would get five points and the last preferred choice would get one point. Any alternative which was not ranked didn't get any point. The total points available to each choice were converted into present with reference to the total points available for all choices. The choice with the present score was ranked as the most important choice and the one with the present score was ranked as the last choice.

The respondents were requested to response on questionnaire by two ways:-

-) They were requested response simply by yes or no response.
-) They could response by selecting one or more potions.
-) They could response by ranking the choices starting from 1 to most important as per number of choice.
-) Respondents had also option to put their views by writing wherever necessary.

Table 4.16

Determinations of Respondents Code Used

| S.N | Denominations of Respondents | Sample size | Code Used |
|-------|------------------------------|-------------|-----------|
| 1. | Tax administrators | 25 | A |
| 2. | Tax exports | 25 | B |
| 3. | Tax payers | 25 | C |
| Total | | 75 | |

Source: - Opinion Survey, 2010

4.3.1 Attitude towards Tax Education

To know the responses attitude towards tax education, a question was asked “Do you think that people are well inform about the tax system in Nepal”? The responses have been tabulated below:

Table 4.17

People's Knowledge towards Tax System

| Responses | Yes | | No | | Total | |
|-----------|-----|------|-----|-------|-------|-----|
| | No. | % | No. | % | No. | % |
| A | - | - | 25 | 100 | 25 | 100 |
| B | - | - | 25 | 100 | 25 | 100 |
| C | 2 | 8 | 23 | 92 | 25 | 100 |
| Total | 2 | 2.67 | 73 | 97.33 | 75 | 100 |

Source: Opinion Survey, 2010

From the above table it has been clear that 97.33% of the respondents were against the question “Do you think that people are well informed about the tax System in Nepal?” and 2.67% respondents were positive in this question it can be concluded that tax education is most necessary in Nepal to increase the tax consciousness of tax payer.

4.3.2 Attitude towards Direct and Indirect tax System in Nepal

To know whether the direct and indirect tax system of Nepal, a question was asked: “Can you classify the direct and indirect tax of Nepal”? The responses have been tabulated below:

Table 4.18

Opinion towards Classification of Direct and Indirect tax of Nepal

| Respondents | Yes | | No | | Total | |
|-------------|-----|-------|-----|-------|-------|-----|
| | No. | % | No. | % | No. | % |
| A | 20 | 80 | 5 | 20 | 25 | 100 |
| B | 24 | 96 | 1 | 4 | 25 | 100 |
| C | 5 | 20 | 20 | 80 | 25 | 100 |
| Total | 49 | 65.33 | 26 | 34.67 | 75 | 100 |

Source: - Opinion Survey, 2010

From the table 4.5 it has been cleared that 96% Of the tax exports were answered this question and only 4% was not answered. 80% of tax administrators were answered this question and 20% respondents were not answered. Only 20% tax payers were answered this question and 80% tax payers were not answered this question. So, it can be concluded that classification of tax education is most necessary in Nepal to increase the tax consciousness of tax payer.

4.3.3 Specific Objective of Income Tax in Nepal

In order to know the specific objectives of income tax in Nepal, respondents were requested to rank their responsible. The question was asked “what should be the specific objective of income tax in Nepal”? Table 4.3 gives the breakdown of responses:

Table 4.19**Opinion towards Objectives of Income Tax**

| S.N. | Objective of IT | Group | | | Total Points | Percent | Rank |
|------|--|-------|----|----|-----------------|---------|------|
| | | A | B | C | | | |
| 1. | To enhance the revenue of Government | 72 | 70 | 80 | 222 | 24.67 | 1 |
| 2. | To meet the government expenditure | 65 | 58 | 60 | 183 | 20.33 | 4 |
| 3. | To narrow the income Gap between rich & poor | 67 | 67 | 61 | 196 | 21.78 | 3 |
| 4. | To achieve the goals of national development and equal economic distribution | 72 | 70 | 69 | 211 | 23.44 | 2 |
| 5. | To check inflation | 30 | 27 | 31 | 88 | 9.78 | 5 |
| | Total | | | | 900 | 100 | |

Source: Opinion Survey, 2010

There was 100% responses received from the respondents. Most of the respondents are supporting the objectives of the enhance the revenue of the government 24.67% are in favor of the objective of to enhance the revenue of the government 23.44% of them choose the objective of national development and equal economic distribution, another 21.78% choose the objective of to narrow the income gap between rich and poor, 20.33% are of them choose to

meet the government expenditure and 9.78% of them gave to check inflation. (See table No. 4.3 for details).

Specific objective of income tax are ranked below in order to preference.

1. To enhance the revenue of the government
2. To achieve the goals of nation development and equal economic distribution.
3. To narrow the income gap between rich and poor.
4. To meet the income government expenditure.
5. To check the inflation.

4.3.4 Attitude towards Income tax system in Nepal.

To know whether the income tax system of Nepal is sound and efficient or not a question asked, “Are you satisfied with the existing income tax system of Nepal?”

The responses received from the various respondents are tabulated as follows:

Table 4.20

Satisfaction towards existing income tax system.

| Respondents | Yes | | No | | Total | |
|-------------|-----|---|-----|----|-------|-----|
| | No. | % | No. | % | No. | % |
| A | 2 | 8 | 23 | 92 | 25 | 100 |

| | | | | | | |
|-------|---|------|----|-------|----|-----|
| B | - | - | 25 | 100 | 25 | 100 |
| C | 2 | 8 | 23 | 92 | 25 | 100 |
| Total | 4 | 5.33 | 71 | 94.67 | 75 | 100 |

Source: Opinion Survey, 2010

From the above table 4.3 it has been clear that most of the respondents i.e. 94.67% of respondents are not satisfy with the existing income tax system of Nepal.

In order to know, the cause of not satisfy with the existing income tax system of Nepal the next question was asked “If no, what are the major problems of the income tax system of Nepal?” The respondents were requested to rank their answer from 1 to 11 tables 4.4 gives a breakdown of responses.

Table 4.21

Major Problems of Income Tax System

| S.N. | Major problems | Group | | | Total Points | Percent | Rank |
|------|--|-------|-----|-----|--------------|---------|------|
| | | A | B | C | | | |
| 1. | In adequate economy policy | 47 | 65 | 86 | 198 | 6.36 | 9 |
| 2. | Inefficient income tax administrative | 129 | 191 | 172 | 492 | 15.81 | 1 |
| 3. | Complicated income tax act, rules & regulation | 102 | 109 | 174 | 325 | 10.44 | 4 |

| | | | | | | | |
|-------|---|-----|-----|-----|------|-------|----|
| 4. | In appropriate rates exemption | 41 | 52 | 47 | 140 | 4.5 | 11 |
| 5. | Difficulty in maintain account for tax purpose | 17 | 58 | 73 | 148 | 4.76 | 10 |
| 6. | Lack of education to tax payers | 91 | 87 | 71 | 249 | 8 | 8 |
| 7. | Lack of awareness to tax payers | 147 | 109 | 71 | 327 | 10.51 | 3 |
| 8. | Lack of training & sufficient incentives to employees | 99 | 94 | 106 | 299 | 9.61 | 5 |
| 9. | Lack of expert in tax management | 58 | 121 | 116 | 295 | 9.48 | 6 |
| 10. | Practice of tax evasion | 157 | 97 | 121 | 375 | 12.05 | 2 |
| 11. | Illegal business actives | 94 | 68 | 102 | 269 | 8.64 | 7 |
| Total | | | | | 3112 | | |

Source: Opinion Survey, 2010

The major problems of income tax system of Nepal were ranked in order of the preference of the respondents as follows:

1. The efficient income tax administrative
2. Practice of tax evasion
3. Practice of awareness to tax payer.
4. Complicated income tax act, rules and regulation.
5. Lack of training and sufficient incentives to employees.

6. Lack of exports in tax management.
7. Illegal business activities.
8. Lack of education to tax payers.
9. Inadequate economic policy.
10. Difficulty in maintaining account for tax purpose.
11. In appropriate rate and exemption limit.

It can be concluded from the above results that in the opinion of respondents, the income tax system of Nepal is not sound and efficient, basically due to inefficient income tax administration, practice of tax evasion and lack of awareness to tax payers.

4.3.5 Appropriate Method while Assessing the Income tax in Nepal.

Method of income tax assessment is very important in the assessment of income tax sound and appropriate assessment procedure is essential for collection of the large amount in the form of income tax. It is very important in managing the income tax because the amount of income tax I realized through the assessment finding out an appropriate method of income tax assessment a question put toward to the respondents asking “What method is more appropriate in Nepal while assessing the income tax?” The responses received are tabulated below:

Table 4.22

Appropriate Method while Assessing the Income Tax in Nepal

| S.N. | Methods | Group | | | Total | |
|-------|--|-------|----|----|-------|-------|
| | | A | B | C | NO. | % |
| 1. | Assessment on the basis of account submitted | 4 | 6 | 4 | 14 | 18.67 |
| 2. | Self assessment | 18 | 12 | 15 | 45 | 60 |
| 3. | Assessment on the best judgment | 2 | 4 | 5 | 11 | 14.67 |
| 4. | Assessment by the committee | 2 | 3 | - | 5 | 6.66 |
| Total | | | | | 75 | |

Source: Opinion Survey, 2010

From the opinion survey, it has been clear self- assessment method is more appropriate for Nepal while assessing income tax 60% of respondents have positive opinion about self- assessment followed by 18.67% of respondents about account basis assessment.

4.3.6 Income tax Evasion in Nepal

In order to find out whether the income tax evasion is practical in Nepal or not, the question was asked “In your opinion is there a major problem of tax evasion in Nepal?” The responses of respondents were tabulated below:

Table 4.23

Income Tax Evasion in Nepal

| S.N. | Response | Groups | | | Total | % |
|-------|----------|--------|----|----|-------|-------|
| | | A | B | C | | |
| 1. | Yes | 20 | 23 | 21 | 64 | 85.33 |
| 2. | No | 5 | 2 | 4 | 11 | 14.67 |
| Total | | 25 | 25 | 25 | 75 | 100 |

Source: Opinion Survey, 2010

The above table 4.6 reveals, those 85.33 respondents supported tax evasion as a major problem of income tax evasion in Nepal. Rest 14.67% was again above view. It can be noted that almost all the person with high denominates were in favor of the question.

There may be much response for wide spread tax evasion. In order to know the main reason for tax evasion, the respondents were provide eight reasons and were provide eight reasons and were provide eight reasons and were requested to rank them. The response has received are tabulated as below:

Table 4.24**Factors Responsible for Tax Evasion**

| S.N. | Response | Groups | | | Total Points | Percent | Rank |
|-------|--|--------|-----|----|--------------|---------|------|
| | | A | B | C | | | |
| 1. | Defective tax administration | 95 | 106 | 93 | 294 | 18.4 | 1 |
| 2. | Inefficient income tax policy | 60 | 59 | 68 | 187 | 11.7 | 5 |
| 3. | In appropriate income tax rate | 33 | 42 | 46 | 121 | 7.75 | 8 |
| 4. | Loopholes in income tax act | 37 | 45 | 53 | 135 | 8.45 | 7 |
| 5. | Unwillingness of tax payers to pay tax | 87 | 104 | 79 | 270 | 16.9 | 2 |
| 6. | Lack of unconscious in tax payers | 65 | 65 | 63 | 193 | 12.08 | 4 |
| 7. | Corruption in tax authority | 72 | 82 | 83 | 227 | 14.21 | 3 |
| 8. | Lack of political commitment | 47 | 67 | 57 | 171 | 10.70 | 6 |
| Total | | | | | 1598 | 100 | |

Source: Opinion Survey, 2010

The major reasons for evasion of income tax from the above table according to the respondent's performance are as follows:-

1. Defective tax administration.
2. Unwillingness of tax authority.
3. Corruption in tax payers to pay tax.
4. Lack of unconscious in tax payers.
5. In appropriate incomes tax policy.
6. Lack of political commitment.
7. Loopholes in income tax act.
8. In appropriate income tax act.

Thus it can be concluding that the main reasons for tax evasion are due to defective tax administration and other after that. The other factors started by a respondents are wide spread practice of illegal business inadequate auditing and investigation and poor develop of corporate system.

4.3.7 Efficiency of VAT in Nepal

Table 4.25

Opinion of Economic Efficiency of VAT in Nepal

| Respondents | Yes | | No | | Total | |
|------------------------|-----|-----|-----|---|-------|-----|
| | No. | % | No. | % | No. | % |
| Tax Administrators (A) | 25 | 100 | - | - | 25 | 100 |

| | | | | | | |
|-----------------|----|-----|---|---|----|-----|
| Tax Experts (B) | 25 | 100 | - | - | 25 | 100 |
| Tax payers (C) | 25 | 100 | - | - | 25 | 100 |
| Total | 75 | 100 | - | - | 75 | 100 |

Source: Opinion Survey, 2010

Experience and various empirical has shown that there is not doubtful of VAT effectiveness to increase revenue in the country. Moreover it has more reliability in developing countries. But there can be raised question really VAT create economic efficiency in the country. To fulfill this question was asked, “VAT is effective instrument to create economic efficiency in Nepal? Do you agree? Obtained data related no one can deny virtue of VAT in Nepal.

However, there is no doubt of not available substitution of VAT system in the world yet. Although various technical difficulties have been burning issue to get optional implementation in the Nepalese land experts mentioned. Register into VAT office by business firms and not practice of billing system at the time of purchase and sales.

4.3.8 Self Assessment System in Nepal.

Theoretically for reducing arbitrary power of the tax administrator self-assessment system for computation income is brought in to practice. For regarding the question has asked to respondents group, “Is self assessment system for computation of taxable income effective in Nepal?” Most of those expressed effective of self-assessment out of that large percentage occupy by tax payer and tax experts respectively first and second.

Table 4.26

Opinion towards effectiveness of self-Assessment System in Nepal

| Respondents | Yes | | No | | Total | |
|-----------------------|-----|----|----|----|-------|-----|
| | No. | % | No | % | NO | % |
| A(Tax Administrators) | 10 | 40 | 15 | 60 | 25 | 100 |
| B(Tax Experts) | 8 | 32 | 17 | 68 | 25 | 100 |
| C (Tax Payers) | 18 | 72 | 7 | 28 | 25 | 100 |
| Total | 36 | 48 | 39 | 52 | 75 | 100 |

Source: Opinion Survey, 2010

The table 4.8 presents that majority part (i.e.68%) of expert to deny for accepting self-assessment system effective in Nepal. Further they added due to poor practice of paying tax and corrupt administrative aspect this system has created culture of negative for original philosophy. Therefore they focused to implement loyal and committed auditing mechanism with the base of day-to-day research reports, to bring overall effectiveness in the tax system.

4.3.9 Attitude toward provisions of fees, fines and penalties.

Income tax system of Nepal has the provisions of fees, fines and penalties for the regulation of low to find out the reasonability of these provisions, a question was asked, “Are penalties under income tax system is reasonable?” the response are tabulated as below:

Table 4.27

**Attitude towards Reasonability of Existing Provisions of Fees,
Fines and Penalties**

| Respondents | Yes | | No | | Total | |
|-------------|-----|-------|-----|-------|-------|-----|
| | No. | % | No. | % | No. | % |
| A | 19 | 76 | 6 | 24 | 25 | 100 |
| B | 20 | 80 | 5 | 20 | 25 | 100 |
| C | 14 | 56 | 11 | 44 | 25 | 100 |
| Total | 53 | 70.67 | 22 | 29.33 | 75 | 100 |

Source: Opinion Survey, 2010

Above table 4.9 shows that 70.67% of respondents have expressed the provisions of fines and penalties are reasonable and 30% respondents have not taken the provision of fees, fines and penalties as reasonable. The respondents, who were against provisions of fees, fines and penalties a question was asked “How can it be made reasonable?” the responses of respondents are as follows:

Table 4.28

Measures to make the Provision of Fines, Fees and Penalties Responsible

| S.N. | Measures | Tax Adm. | Tax Expert | Tax Payer | Total | Percent |
|-------|---------------|----------|------------|-----------|-------|---------|
| 1. | By increasing | 5 | 10 | 2 | 17 | 36.17 |
| 2. | By Decreasing | - | 10 | 20 | 30 | 63.83 |
| Total | | | | | 47 | 100 |

Source: Opinion Survey, 2010

It is clear from the above table 36.17% of respondents who do not agree the provisions of fees, fines and penalties as reasonable felt it should be increased and 63.83% have felt it should be decreased.

4.3.10. Most Important factors for effectiveness of Income Tax in Nepal.

In order to know the most important factor for effectiveness of tax in Nepal respondents were requested to rank their responses on given choices. The question was “What is the most important factor for effectiveness of tax in Nepal?” Table 4.8 gives a breakdown of responses:

Table 4.29

Important factors for effectiveness of Tax in Nepal

| S.N. | Factors | Groups | | | Total points | Percent | Rank |
|------|---------|--------|---|---|--------------|---------|------|
| | | A | B | C | | | |

| | | | | | | | |
|-------|---------------------------------|----|----|----|-----|-------|---|
| 1. | Honest tax officers | 56 | 56 | 56 | 162 | 27 | 1 |
| 2. | Honest tax payer | 61 | 43 | 40 | 144 | 24 | 3 |
| 3. | Clear act, rules and regulation | 52 | 46 | 60 | 158 | 26.33 | 2 |
| 4. | Effective tax administration | 32 | 54 | 50 | 136 | 22.67 | 4 |
| Total | | | | | 600 | 100 | |

Source: Opinion Survey, 2010

The important factors for effectiveness of tax was ranked in order of the preference of the respondents were as follows:

(See table 4.9 for details)

1. Honest tax officers
2. Clear act, rules and regulation
3. Honest tax payer
4. Effective tax administration

It can be concluded that honest factor for the effectiveness of tax in Nepal.

4.3.11 Effectiveness of Income Tax Administration in Nepal

In order to find out effectiveness of income tax administration, a question was asked “What do you feel about the current income tax administration of Nepal?” The respondents who do you agree on the effectiveness, they have got alternative to choose about the position of income tax administration. The responses received from respondents are as follows:

Table 4.30**Effectiveness of Income Tax Administration**

| S.N | Responses | Respondents | | | Total | Percentage |
|-------|--------------|-------------|----|----|-------|------------|
| | | A | B | C | | |
| 1. | Efficient | 15 | 3 | 5 | 23 | 30.67 |
| 2. | Inefficient | 1 | 15 | 16 | 100 | 42.67 |
| 3. | Satisfactory | 9 | 7 | 4 | 20 | 22.66 |
| Total | | 25 | 25 | 25 | 75 | 100 |

Source: Opinion Survey, 2010

From above table 4.11 it is clear that income tax administration is not efficient to collect tax and has got majority percentage from the respondent's i.e. 42.67% and they ranked some causes given in the questionnaire as tabulated below. For this purpose the question asked was, "What are the causes of inefficiency of Nepalese income tax administration?"

Table 4.31**Causes of Inefficient of Nepalese income Tax Administration**

| S.N. | Responses | Groups | | | Total Points | Percent age | Rank |
|------|-----------------------------------|--------|----|----|--------------|-------------|------|
| | | A | B | C | | | |
| 1. | Lack of trained and competent tax | 7 | 76 | 86 | 169 | 17.14 | 1 |

| | | | | | | | |
|-------|---|----|----|----|------|-------|---|
| | person | | | | | | |
| 2. | Complicated tax laws | 8 | 77 | 76 | 161 | 16.33 | 2 |
| 3. | Lack of proper communication | 10 | 42 | 63 | 115 | 11.66 | 5 |
| 4. | Lack of proper direction | 3 | 46 | 49 | 98 | 9.94 | 6 |
| 5. | Lack of voluntary compliance by tax payers | 9 | 67 | 55 | 131 | 13.29 | 4 |
| 6. | Unnecessary outside pressure | 4 | 40 | 41 | 85 | 8.62 | 8 |
| 7. | Undue delay in malty assessment | 6 | 63 | 64 | 134 | 13.59 | 3 |
| 8. | Lack of co-ordination of the tax department with other department | 5 | 39 | 49 | 93 | 9.43 | 7 |
| Total | | | | | 1598 | 100 | |

Source: Opinion Survey, 2010

The causes of ineffectiveness of Nepalese income tax administration ranked in order of preference of respondents are as follows:

1. Lack of trained and competent tax personal
2. Complicated tax laws
3. Undue delay in making assessments
4. Lack of Voluntary compliance by tax payers
5. Lack of proper direction
6. Lack of proper communication

7. Lack of co-ordination of the department with other departments
8. Unnecessary outside Pressure.

It can be conclude that the lack of trained and competent tax personnel, complicated tax laws, undue delay in making assessments are the most important causes of in effectiveness of Nepalese tax administration.

4.3.12 Suggestions for Achieving Effectiveness of Income Tax in Nepal

To know the other important factors for effectiveness of income tax a question was asked “Do you have any other suggestion for achieving effectiveness of taxes in Nepal?” The responses are as follows:

1. Government economic policy is the main cause for unsatisfactory of effectiveness of tax in Nepal. So, it should be corrected in purchased of effectiveness of tax.
2. Effective tax management and training and seminar to the tax personnel.
3. Development of check and balance system.

4.4 Major Findings of the Study

On the basis of data presentation and analysis in above mention sub chapter some important findings of the study is summarized below:

- 1) The study shows that the contribution of tax revenue was 79.12% and that of non tax was 20.88% in FY 2007/08 shows that attention has been major sources of government revenue. But the contribution of total revenue was not more formulated trend. Its contribution was 77.19% in FY 1998/99

- 2) Nepalese tax revenue is composed of both direct and indirect tax revenue. There is dominant role of indirect tax revenue in Nepalese tax revenue. The contribution of direct tax and indirect tax to total tax revenue was 27.11% and 72.89% respectively in 2007/08. It reveals that tax structure of Nepal is not a justifiable on equity ground and progressiveness because indirect tax is considered regressive in nature.
- 3) The contribution of custom duty, VAT on indirect tax were 44.82%, 13.91%, 41.27% respectively in FY 1998/99 and contribution each taxes were reached 33.93%, 18.03% and 48.04% respectively in FY 2007/08. It shows that a custom duty was in decreased trend and excise duty and VAT were in increasing trend.
- 4) The contribution of income tax, House and Land registration tax and Vehicle tax to direct tax revenue in FY1998/99 were 82.09%, 13.35% and 4.56% respectively which reached to 82.63%, 12.74% and 4.63% respectively in FY 2007/0. In the composition of direct tax, income tax was the giant one which contribution seems to be increasing every year. The percentage contribution of house and land registration was in decreasing trend and the other remaining taxes portion came to nil in the preceding years. Income tax has occupied third position at present on the basis of mean contribution to GDP. It contribution to government revenue is in increasing trend so the income tax in future will also contribute very well.
- 5) Income tax has been considered as suitable sources for mobilization internal resources. It can be used as a positive instrument to boost up government revenue collection, to develop the economic condition of Nepalese people and promote distributive justice and to cure resource gap problem.

- 6) Contribution of direct tax to GDP was 2.28% in FY 1998/99 which reached to 2.81% in FY 2006/07. It was fluctuated, this ratio is not satisfactory.
7. Contribution of indirect tax to GDP was 6.43% in FY 1998/99, which related to 7.71% in FY 2006/07. It was increasing trend.
- 8) Income tax is composed of corporate income tax, individual income tax, employment, tax on interest and others. All those taxes contribution were in increasing trend.
- 9) Custom duty is composed of import, export, Indian excise refund and others. All those taxes contribution were in fluctuating trend.
- 10) CITR portion in income tax revenue was 53.24% of maximum in FY 2000/01. Minimum contribution of CITR to total income tax revenue was 30.58% in FY 2002/03 and it was 38.74% in 2007/08. CITR had contributed 41.19% to income tax revenue on average during the year.

This shows that CITR occupied major portion in income tax. But the fluctuation in CITR collection and its percentage contribution was due to the effect of unfriendly political and economic environment and lack of developing competently by public and private sector.

- 11) In the structural composition of CITR Private was dominated the sector. The average portion covered by public and private sector was 40.12% and 59.88% respectively.
- 12) The domestic resource gap has been fluctuated. It was Rs. 22328.0 million in FY 1998/99 and which was increased to Rs. 30941.2 million in FY 2000/01. It reached to Rs. 53727.4 million in FY 2007/08 and average % of resource gap to Govt. expenditure was 34.60% during the study period. Domestic resource gap is increasing every year.

- 13) One an average contribution of total Govt. revenue to total Govt. expenditure was 65.40% amounting Rs. 63578.4 million during the study period. Government revenue was 69.69% of maximum level in FY 2003/04 and 61.24% in minimum level in FY 2000/00. Similarly, the contribution made by foreign at comprising both grants and loan was 21.56% amounting Rs. 20254.7 million on an average. This indicates the indebtedness of the country.

On the basis of empirical analytical analysis some major findings can be drawn which summarized as given below.

-) Tax education is most necessary in Nepal to increase the tax consciousness of tax payers.
-) The major objective of the income tax in Nepal is to enhance the revenue of the government to achieve the goals of National Development and equal economic distribution and narrow the gap between rich and poor. Income tax system of Nepal is not sound and efficient basically due to inefficient tax evasion and lack of awareness of tax payers.
-) Income tax evasion is the major problem of Nepal for income tax generation.
-) Main reason for tax evasion is due to defective tax administration, unwillingness of tax payers to pay tax and corruption in tax authority.
-) Provision of fines and penalties of Nepal are reasonable for which 70.67% of respondents have supported and remaining 29.33% were in against.
-) Income tax administration is not efficient to collect tax.
-) Lack of trend and competent tax personal, complicated tax laws and undue delay in making assessment are the most important cause of ineffectiveness of Nepalese tax administration.
-) Honest tax officer and clear act, rules and regulations are the most important tractors for the effectiveness of income tax in Nepal.

CHAPTER-V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

Government requires sufficient revenues to carry out development plans to handle day to day administration to maintain peace and security and to launch other public welfare activities. In order to carry out such activities the government collects revenue from various sources. The sources of government revenue classified in to external and internal source. Main external source of government revenues are foreign grants, loan and internal sources are tax revenue, non- tax revenue and internal loan etc. In developing countries like Nepal lack of sufficient financial resources is the main constraint for national economic development. A lot of fund is required to meet the additional financial requirements for the development activities of the country. Nepal has been suffering from capital shortage to accelerate the economic growth the expenditure of Nepalese government is increasing year by year. To meet the additional capital requirements Nepalese government has been using external resources are preferable for sustainable economic development. Nepal has been unable for proper mobilization of internal resources. Thus fiscal deficit and resource gap of Nepal have been fluctuated.

From the secondary data, the study shows that the contribution of tax revenue was 81.58% and that of non tax was 18.42% in FY 2008/09 it shows that tax revenue has been major sources of government revenue. But the contribution to total revenue was not more formulated. Its contribution was 77.19% in FY 1998/99. Nepalese tax revenue is composed of both direct and indirect tax revenue. There is dominant role of indirect tax revenue in Nepalese tax revenue.

The contribution of direct tax and indirect tax to total tax revenue was 29.32% and 70.68% respectively in 2008/09. It reveals that tax structure of Nepal is not a justifiable on equity ground and progressiveness because indirect tax is considered regressive in nature. The contribution of custom duty, VAT on indirect tax were 44.82%, 13.91%, 41.27% respectively in FY 1998/99 and contribution of each taxes were reached 32.39%, 19.61% and 48% respectively in FY2008/09. It shows that a custom duty was in decreased trend and excise duty and VAT were in increasing trend. The contribution of income tax, House and Land registration tax and Vehicle tax to direct tax revenue in FY 1998/99 were 82.09%, 13.35% and 4.56% respectively which reached to 79.39%, 15.22% and 5.39% respectively in FY 2008/09. In the composition of direct tax, income tax was the giant one which contribution seems to be increasing every year. Other remaining taxes portion came to nil in the preceding years. The percentage contribution of house and land registration was in decreasing trend and the Income tax has occupied third position at present on the basis of mean contribution to GDP. Its contribution to government revenue is in increasing trend so the income tax in future will also contribute very well. Income tax has been considered as suitable sources for mobilization internal resources. It can be used as a positive instrument to boost up government revenue collection, to develop the economic condition of Nepalese people and promote distributive justice and to cure resource gap problem.

Contribution of direct tax to GDP was 2.28% in FY1998/99 which reached to 3.77% in FY 2008/09. It was fluctuated, this ratio is not satisfactory. Contribution of indirect tax GDP was 6.43% in FY 1998/99, which related to 9.09% in FY 2008/09. It was in increasing trend. Income tax is composed of corporate income tax, individual income tax, employment, tax on interest and others. All those taxes contribution were in increasing trend.

Domestic resource gap has been fluctuated. Government expenditure was Rs. 59579 million and revenue was Rs. 37251 million in 1988/99 that year resource gap was Rs. 22328 million which was 37.48%. With increasing trend government expenditure and revenue reached to Rs.219661.9 million and Rs.143474.5 million respectively in FY 2008/09 it created the resource gap of Rs.76187.4 million which was 34.68%. Average gap to government expenditure was 34.61%. On an average contribution of total government revenue to total Govt. expenditure was 65.63% during the study period. Government revenue was 69.69% of maximum level in FY 2003/04 and 61.24% in minimum level in FY 2000/00. Similarly, the contribution made by foreign at comprising both grants and loan was 20.12% on average. This indicates the indebtedness of the country.

Secondary data as well as primary data are used in this study. Economic survey has been used as the major secondary data. Opinion survey technique has been used in this study to collect primary data. Primary data have been collected from three respondents group's tax administrators, tax experts and tax payers. Tax experts consist of chartered accountants, lowers, writers and teachers. Tax administrators consist of government officers and employees. Tax payers consist of bankers, businessmen and others. On the basis of empirical analytical analysis.

Major finding can be summarized as given below.

-) Contribution of income tax for the economic development of Nepal has been increasing significantly in recent year as compared to past 10 years but it does not mean that the share is that much satisfactory. So much effort should be made to increase it.
-) Tax education is most necessary in Nepal to increase the tax consciousness of tax payers.

-) Nepal has been heavily relying on foreign loans and grants. Internal resources are preferable for sustainable economic development, thus fiscal deficit of Nepal has-been increasing.
-) The major objective of the income tax in Nepal is to enhance the revenue of the government to achieve the goals of National Development and equal economic distribution and narrow the gap between rich and poor. Income tax system of Nepal is not sound and efficient basically due to inefficient tax evasion and lack of awareness of tax payers.
-) Self-assessment method is the major problem of Nepal for income tax generation.
-) Income tax administration is not efficient to collect tax.
-) Honest tax officer and clear act, rules and regulations are the most important tractors for the effectiveness of income tax in Nepal.
-) Lack of trend and competent tax personal, complicated tax laws and undue delay in making assessment are the most important cause of ineffectiveness of Nepalese tax administration etc.

5.2 Conclusion

Nepalese economy has been suffering from serious and growing problems of financial resource gap. The gap has been sharply increasing in recent years leading the countries to the state of external dependency, which has produced bitter experience and mixed consequences and burden of foreign loan. The major reasons for this problem are significant increase in regular and development expenditure of government, increasing burden of debt servicing charges, poor utilization of natural resources base, poor economic growth, inadequate tax efforts of the government as well as political instability and more expenditure

used in armed, police force. War of Maoist and royal place accident has left long run effect in the economy of Nepal.

Resource gap in Nepal has been morally increasing the internal revenue is sometime insufficient even to meet regular expenditure and most to the development activities depend on foreign aid where Nepal has been compelled to harmonize the donor. The major problems of domestic resource mobilization are poor utilization of the natural resource base small and stagnant industrial sector, poor performance of public sector enterprises poor economic growth and inadequate tax effort etc. So, in this context, revenue generations from internal sources are very important in which income tax is one of major sources.

Nepalese tax revenue is heavily dominated by indirect tax revenue. Only one fourth of tax revenue has been contributed by direct tax revenue. It is necessary to increase the share of direct revenue so as to direct the economy in the channel of development. Resource mobilization through direct taxation should be focused. The contribution of income tax revenue to total tax revenue and direct tax revenue to total tax revenue should be increased by making withholding effective change in income tax policy rules and regulation. Bringing new tax payers into tax net help increase income tax's share in tax and direct tax revenue. The contribution of employment income in income tax revenue has been increasing in the recent years as compared to previous years. In such a way that high earner should be made to pay higher income taxes. Filing of income returns by employee should be enhanced for collecting more income tax revenue.

Among various taxes custom duty, excise duty and value added tax were three major sources of indirect tax revenue. Custom duty was decreasing trend, excise duty was increasing trend and VAT was fluctuated during the certain study period. Income tax, Land and House Registration and Vehicle were major

components of direct tax. Income tax was one of the major components of direct tax. It contributed to direct tax was 79.39% in FY 2008/09 It was decreased in comparison to 2007/08. It may be due to the political instability. Over the past several years Nepal has been adopting the policy of lowering tax rates and widening its coverage, which is not supported by credible reform measures lower the revenue collection. In this regard, providing adequate education to tax payers, simplifying and making income assessment procedure more transparent reforming tax administration, promoting 'Self Assessment System' and utilizing other effective measures to off set the revenue loss caused by lower tax rates has been focused very significant to strengthen internal revenue base of country. Contribution of tax revenue to GDP has been focused very nominal compare to the same ratio in other neighboring SAARC and other developing countries. Nepal's Tax/GDP ratio was focused to be 9.2% and the same ratio was found 11.8% in India, 13.6% in Pakistan and 16.8% in Shree Lanka. Direct tax to GDP ratio was 2.71% on average and indirect tax to GDP ratio was 7.55% on average during the certain study period. Income tax to GDP ratio also was found very insignificant. Total income tax revenue has been found to be composition of income tax from public enterprise, private corporate bodies, individuals, tax on interest and others. Individuals was the major portion of income tax, it was contributed by 37.46% on average during the study period. Private Corporation Bodies was increasing trend and public was decreasing trend which shows that Nepal is going towards Privatization.

Corporate sector is in initial stage of development in Nepal which is small and stagnant in nature comparing to other developing country. The performance of corporate sector, especially the industry is very poor their number profitability, investment in fixed assets, share of market transactions are all in weak position nevertheless, the importance of contribution of corporate income tax to

government revenue is important to Nepal like developing country. Corporate income tax is based on socio-economic infrastructure and environment. In the corporate income tax structure the debate is going on use of appropriate type of tax incentives treatment of inflation, method and rate of depreciation. The present provision of tax incentives are found insufficient in the changing global economic scenario especially for re3vival of sick industrial unit the statutory corporate tax rates are found frequently changed during the study period.

An empirical investigation has been conducted in order to find out various aspects of tax imposition in Nepal. The questionnaire was distributed to the tax administrators, tax experts and tax payers. It has concluded that Government should increase the tax education in Nepal to increase the tax consciousness of tax payers. Lack of trend and competent tax personal competent tax personal complicated tax laws and undue delay in making assessment are the most important cause of ineffectiveness of Nepalese tax administration.

It is the most important to increase our revenue mobilization capabilities. Our economy is exceeding reliant on indirect taxes for revenue mobilization. Effort should be made to increase the contribution of direct tax, more precisely the income tax in the revenue structure. It is imperative now to take a close look at the role of income tax in the total tax structure with a view to improving the horizontal as well as vertical equity as far as possible without losing any amount of the tax revenue. This imperative tax policy should concentrate on expanding the tax base thereby improving the resource mobilization capacity of tax system.

The tax policy needs a clear out and long term vision. Frequent changes in fiscal policies and programmed show a never-ending phenomenon of transitional period. It is difficult but not impossible to think over seriously by concerned high authority and general people to bring income tax system in the right direction

and right shape in order to enhance the economic development of Nepal. Manpower development planning within the administration is desired for the efficiency of tax personnel side by side, tax education packages are to be made and imitated hence tax administration and tax compliance could be improved.

5.3 Recommendations

On the basis of above analysis and conclusions, the following specific suggestions have been recommended for the collection of revenue from direct and indirect taxation in Nepal.

-) Generally 15 % to 18 % total tax GDP ratio is regarded as moderate standard but Nepalese total tax/GDP ratio is contributing 9.2% in an average. To increase the total tax revenue, bringing the private educational institute, public transportation etc. into tax net should increase direct tax revenue.
-) A nation wide campaign should be launched to inform and explain tax rules and regulations, tax programs and benefits of paying tax with a view of stimulating public to pay taxes through the media of Radio, FM, Television, newspapers and social programs in the educational institutions and public places.
-) Nepalese tax revenue is heavily dominated by indirect tax revenue. Only one fourth of tax revenue has been contributed by direct tax revenue. It is necessary to
-) Increase the share of direct tax revenue so as to direct the economy in the channel to development. Resource mobilization through direct taxation should be focused.
-) The growing problem of resources gap in Nepalese finance should be tackled with significant reduction in government expenditure (especially regular expenditure) by utilizing natural resource base effectively and

- mobilizing additional financial resources internally to meet resource requirements rather than opting for foreign sources of deficit financing.
-) Government should appoint the capable market supervisors to increase the direct tax and to apply the tax rules and regulations.
 -) Account based taxation and self assessment system should be encouraged to make it revenue productive and self tax assessment system should be encouraged to make it revenue productive and tax payer friendly.
 -) Tax evasion and avoidance should be minimized enforcing heavy fines and penalties, controlling widespread illegal business activities and increasing administrative efficiency of the tax authorities and through the awareness programs among tax payers.
 -) Tax payers, who submit true statement within the specified period of time. Should be provided certain percentage of tax rebate.
 -) Income tax rules and regulations should be clear and simple for all the tax payers as well as for tax administrators. The following recommendations are made in income tax law.
 - i. The language of act should simple and clear.
 - ii. The assessment and tax collection provisions should be making clear and simple, so that tax payers would be encourage paying income tax.
 - iii. Discretionary power of the tax officials should be curtailed in the act.
 - iv. The assessment of the time limit after the submission of income assessment should be reducing.
 - v. The definition made in income tax act should further classified and well defined.

-) Income tax administration implements the tax laws. Therefore, effectiveness of income tax system depends upon the income tax administration. In Nepal, one of the most important reasons for unsound income tax system is inefficient and unscientific income tax administration. Following recommendations are made for improvement of income tax administration.
-) Delays in assessment should be reduced as possible.
-) Computerized information system is necessary to keep up to date records of income tax.
-) Proper tax education should be provided to tax officials as well as tax payers regularly.
-) Cost of income tax collection is one of the determinants of efficiency of administration. Therefore, the concerned authority should pay due attention to it should be reduced.
-) Unnecessary outside pressure should be avoided.
-) The range of taxpaying circle under the tax net is very narrow in Nepal. The tax administration has not been able to induce individuals to pay income tax. One of the effective steps to encourage people to pay tax may be the incentive to regular taxpayers. The challenge of bringing more people under the tax net can be faced only through effective tax administration and by educating taxpayers.

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